

Report of the Directors

The directors of Chitaly Holdings Limited (the “Company”) present their report and the audited financial statements of the Company and its subsidiaries (collectively referred to as the “Group”) for the year ended 31 December 2006.

PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding. Details of the principal activities of the subsidiaries are set out in note 18 to the financial statements. There were no significant changes in the nature of the Group’s principal activities during the year.

RESULTS AND DIVIDENDS

The Group’s profit for the year ended 31 December 2006 and the state of affairs of the Company and the Group at that date are set out in the financial statements on pages 30 to 94.

No interim dividend was paid during the year. The directors recommend the payment of a final dividend of HK2 cents per ordinary share note 12 in respect of the year, to shareholders on the register of members on 4 June 2007. This recommendation has been incorporated in the financial statements as an allocation of retained profits within the equity section of the balance sheet.

SEGMENT INFORMATION

An analysis of the Group’s turnover and contribution to operating profit for the year by principal activities is set out in note 4 to the financial statements.

SUMMARY FINANCIAL INFORMATION

The following is a summary of the consolidated/combined financial results and of consolidated/combined assets and liabilities of the Group for the last five years, prepared on the basis set out in the note below:

	Year ended 31 December				
	2006 HK\$'000	2005 HK\$'000	2004 HK\$'000	2003 HK\$'000	2002 HK\$'000
RESULTS					
REVENUE	489,143	413,257	403,766	300,719	207,020
PROFIT BEFORE TAX	23,411	80,446	131,857	88,998	51,252
Tax	(307)	(2,254)	(23,855)	(11,754)	(6,738)
Net profit from ordinary activities attributable to shareholders	23,104	78,192	108,002	77,244	44,514
ASSETS AND LIABILITIES					
Non-current assets	344,021	247,809	184,013	134,167	75,662
Current assets	252,885	297,007	245,285	142,422	118,931
Current liabilities	(204,878)	(178,756)	(177,188)	(105,352)	(61,571)
Non-current liabilities	(17,464)	(18,094)	(18,634)	(6,363)	(6,363)
	374,564	347,966	233,476	164,874	126,659

PROPERTY, PLANT AND EQUIPMENT

Details of movements in the property, plant and equipment of the Group during the year are set out in note 14 to the financial statements, respectively.

SHARE CAPITAL AND SHARE OPTIONS

Details of movements in the Company's share capital and share options during the year are set out in note 27 to the financial statements.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's articles of association or the laws of the Cayman Islands which would oblige the Company to offer new shares on a pro rata basis to existing shareholders.

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

Neither the Company, nor any of its subsidiaries purchased, redeemed or sold by the Company's listed securities during the year.

RESERVES

Details of movements in the reserves of the Company and the Group during the year are set out in note 29 to the financial statements and in the consolidated summary statement of changes in equity, respectively.

DISTRIBUTABLE RESERVES

As at 31 December 2006, the Company's reserves available for distribution, calculated in accordance with the provision of the Companies Law of the Cayman Islands, amounted to HK\$138,988,000 of which HK\$5,848,000 has been proposed as a final dividend for the year. In addition, the Company's share premium account, in the amount of HK\$102,346,000 may be distributed in the form of fully paid bonus shares.

CHARITABLE CONTRIBUTIONS

During the year, the Group made no charitable contributions. (2005: HK\$250,000).

MAJOR CUSTOMERS AND SUPPLIERS

Sales to the Group's five largest customers accounted for approximately 8.1% of the total sales for the year and sales to the largest customer included therein amounted to 2.2%. Purchases from the Group's five largest suppliers accounted for approximately 47.4% of the total purchase for the year and purchase from the Group's largest supplier included therein amounted to 10.3%.

None of the directors of the Company or any of their associates or any shareholders (which, to the best knowledge of the directors, own more than 5% of the Company's issued share capital) had any beneficial interest in the Group's five largest customers.

DIRECTORS

The directors of the Company during the year were:

Executive directors:

Mr. Tse Kam Pang (*Chairman*)

Mr. Lam Toi

Mr. Ma Ming Fai, Gary

Independent non-executive directors:

Mr. Donald H. Straszheim

Mr. Yau Chung Hong

Mr. Chang Chu Fai J. Francis

In accordance with article 87 of the Company's articles of association, one-third of the directors will retire by rotation and, being eligible, will offer themselves for re-election at the forthcoming annual general meeting.

Details of the directors to be retired and offered for re-election at the forthcoming annual general meeting of the Company are contained in the circular to be despatched together with this annual report.

The Company has received annual confirmations of independence from Mr. Donald H. Straszheim, Mr. Yau Chung Hong and Mr. Chang Chu Fai Francis, and as at the date of this report still considers them to be independent.

DIRECTORS' AND SENIOR MANAGEMENT'S BIOGRAPHIES

Biographical details of the directors of the Company and the senior management of the Group are set out on pages 16 to 17 of the annual report.

DIRECTORS' SERVICE CONTRACTS

Mr. Tse Kam Pang and Mr. Lam Toi have entered into a service agreement with the Company for an initial term of two years commencing from 1 May 2002, respectively, which will automatically continue thereafter until terminated by not less than two months' notice in writing served by either party to the other. Mr. Ma Ming Fai, Gary has entered into a service agreement with Company for a term of two years commencing from 21 January 2005.

All independent non-executive directors have also entered into a letter of appointment with the Company for a term of three years commencing from 26 May 2006.

All directors are subject to retirement and re-election at annual general meetings of the Company in accordance with the rotation requirements under the articles of association of the Company.

Apart from the foregoing, no director proposed for re-election at the forthcoming annual general meeting has a service contract with the Company which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

MANAGEMENT CONTRACTS

No contracts concerning the management and administration of the whole or any substantial part of the business of the Group were entered into or existed during the year under review.

DIRECTORS' REMUNERATION

The directors' fees are subject to shareholders' approval at general meetings. Other emoluments are determined by the Company's board of directors with reference to directors' duties, responsibilities and performance and the results of the Group.

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARES AND UNDERLYING SHARES AND DEBENTURES

As at 31 December 2006, the interests and short positions of the directors and chief executive in the shares (the "Shares") and underlying shares and debentures of the Company or its associated corporations (within the meaning of Part XV of Securities and Futures Ordinance (the "SFO")), as recorded in the register required to be kept by the Company pursuant to Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers, were as follows:

Long positions in ordinary shares of the Company:

Name of director	Notes	Number of Shares held, capacity and nature of interest			Percentage of the Company's issued share capital
		Directly beneficially owned	Through controlled corporation	Total	
Mr. Tse Kam Pang	(a)	4,600,000	71,450,000	76,050,000	29.24%
Mr. Ma Ming Fai, Gary	(b)	200,000	1,106,000	1,306,000	0.50%
Dr. Donald H. Straszheim	(c)	800,000	—	800,000	0.31%
Mr. Chang Chu Fai J. Francis	(c)	200,000	—	200,000	0.08%
Mr. Yau Chung Hong	(c)	200,000	—	200,000	0.08%

The interests of the directors in the share options of the Company are separately disclosed in note 28 to the financial statements.

Notes:

- (a) The 71,450,000 Shares are held by Crisana International Inc. ("Crisana"), a company incorporated in the British Virgin Islands. As at 31 December 2006, Mr. Tse Kam Pang held 100% of the issued share capital of Crisana.
- (b) The 1,106,000 Shares are held by Upwise Investments Limited, a company incorporated in the British Virgin Islands. The entire issued share capital of Upwise Investments Limited is owned by Mr. Ma Ming Fai, Gary.
- (c) These represent Shares to be issued upon exercise of the share option granted to them, details of which are set out in the section headed "Share Option Scheme" in this report.

No directors have non-beneficial personal equity interests in certain subsidiaries held for the benefit of the Company solely for the purpose of complying with the minimum company membership requirements.

Save as disclosed above, as at 31 December 2006, none of the directors had registered an interest or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations that was required to be recorded pursuant to Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers.

DIRECTORS' INTEREST IN COMPETING BUSINESS

None of the directors or any of their respective associates had any interest in a business which competes or is likely to compete, either directly or indirectly, with the business of the Group.

DIRECTORS' RIGHTS TO ACQUIRE SHARES

Save as disclosed in the share option scheme disclosures in note 28 to the financial statements, at no time during the year were rights to acquire benefits by means of the acquisition of shares in or debentures of the Company granted to any director or their respective spouse or minor children, or were any such rights exercised by them; or was the Company, its holding company, or any of its subsidiaries and fellow subsidiaries a party to any arrangement to enable the directors to acquire such rights in any other body corporate.

SHARE OPTION SCHEME

The Company operates a share option scheme (the "Scheme") for the purpose of providing incentives and rewards to eligible participants who contribute to the Group's operations. Under the Scheme, the directors may, at their discretion, invite any employees, directors or consultants of any company in the Group to acquire options. The Scheme became effective on 26 April 2002 and, unless otherwise cancelled or amended, will remain in force for 10 years from that date.

The maximum number of shares in respect of which options may be granted under the Scheme and under any other share option scheme of the Company pursuant to which options may be granted to directors, consultants and/or employees of any company in the Group, shall initially not exceed 10% of the relevant class of securities of the Company in issue excluding, for this purpose, shares issued on exercise of options under the Scheme and any other share option scheme of the Company. Upon the grant of options for shares up to 10% of the relevant class of securities of the Company and subject to the approval of the shareholders of the Company in general meetings, the maximum number of shares to be issued under this scheme when aggregated with securities to be issued under any other share option scheme of the Group, may be increased by the board of directors, provided that the shares to be issued upon exercise of all outstanding options do not exceed 30% of the relevant class of securities in issue.

No option may be granted to any one person such that the total number of shares issued and to be issued upon the exercise of options granted and to be granted to such person in any 12-month period up to the date of the latest grant exceeds 1% of the issued share capital of the Company.

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An option may be exercised in accordance with the terms of the Scheme at any time during the option period (and not more than 10 years after the date of grant). The option period will be determined by the board of directors and communicated to each grantee. The board of directors may provide restrictions on the time during which the options may be exercised. There are no performance targets which must be achieved before any of the options can be exercised. However, the board of directors retains discretion to accelerate the vesting of the fixed-term options in the event that certain performance targets are met.

The subscription price for the Company's shares under the Scheme will be a price determined by the board of directors and notified to each grantee. The subscription price will be the highest of: (i) the nominal value of a share; and (ii) the closing price of the shares as stated in the Stock Exchange's daily quotation sheet on the date of grant, which must be a trading day; and (iii) the average closing price of the shares as stated in the Stock Exchange's daily quotation sheets for the five trading days immediately preceding the date of grant. An option shall be deemed to have been granted and accepted by an eligible participant (as defined in the Scheme) and to have taken effect when the acceptance form as described in the share option scheme is completed, signed and returned by the grantee with a remittance in favour of the Company of HK\$1.00 by way of consideration for the grant.

As at 31 December 2006, the number of shares issuable under share options granted under the Scheme was 18,600,000, which represented 7% of the Company's shares in issue as at that date. The maximum number of shares issuable under share options which may be granted to each eligible participant in the Scheme within any 12-month period up to the date of latest grant, is limited to 1% of the shares of the Company in issue at any time. Any further grant of share options in excess of this limit is subject to the shareholders' approval in a general meeting.

The directors have estimated the values of the share options granted during the year, calculated using a binomial pricing model as at the date of grant of the options:

Grantee	Number of options granted during	Theoretical value the year of share options HK\$'000
Other employees	17,300,000	6,520

The value of an option varies with different variables of certain subjective assumptions. Any change to the variables used may materially affect the estimation of the fair value of an option.

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The share options granted under the Scheme for a consideration of HK\$1.00 per grant during the year are set out below:

Name or category of participant	At the beginning of the year	Number of share options				At the end of the year	Date of grant of share options*	Exercise period	Price of the Company's shares ***			
		Granted during the year	Exercised during the year	Cancelled during the year	Forfeited during the year				Exercise price per share **	At grant date of options	Immediately before the date of exercises	At exercise date of options
								HK\$	HK\$	HK\$	HK\$	
Directors												
Donald H. Straszheim	800,000	-	-	-	-	800,000	28/9/2004	29/9/2004 to 28/9/2014	4.8	4.8	-	-
Yau Chung Hong	200,000	-	-	-	-	200,000	8/4/2005	9/4/2005 to 8/4/2015	7.45	7.45	-	-
Chang Chu Fai, J. Francis	200,000	-	-	-	-	200,000	6/9/2005	7/9/2005 to 6/9/2015	4.57	4.35	-	-
Others												
Members of senior management and other employees of the Group	2,400,000	1,500,000	-	-	(2,400,000)	1,500,000	9/1/2006	10/1/2006 to 9/1/2016	3.675	3.675	-	-
	100,000	-	-	-	-	100,000	28/9/2004	29/9/2004 to 28/9/2014	4.8	4.8	-	-
	3,600,000	15,800,000	-	-	(3,600,000)	15,800,000	15/11/2006	16/10/2006 to 15/11/2016	1.116	1.116	-	-
	6,100,000	17,300,000	-	-	-	17,400,000						
In aggregate	1,200,000	-	-	-	-	1,200,000						
	6,100,000	17,300,000	-	-	(6,000,000)	17,400,000						
	7,300,000	17,300,000	-	-	-	18,600,000						

* The vesting period of the share options is from the date of the grant until the commencement of the exercise period.

** The exercise price of the share options is subject to adjustment in the case of rights or bonus issues, or other similar changes in the Company's share capital.

*** The price of the Company's shares disclosed as at the date of the grant of the share options is the Stock Exchange closing price on the trading day immediately prior to the date of the grant of the options. The price of the Company's shares disclosed as at the date of the exercise of the share options is the weighted average of the Stock Exchange closing prices over all of the exercises of options within the disclosure line.

SUBSTANTIAL SHAREHOLDERS' AND OTHER PERSONS' INTERESTS IN SHARES

At 31 December 2006, the following interests of 5% or more of the issued share capital of the Company were recorded in the register of interests required to be kept by the Company pursuant to Section 336 of the SFO:

Long positions:

Name	Notes	Capacity and nature of interest	Number of ordinary shares held	Percentage of the Company's issued share capital
Crisana	(a)	Directly beneficially owned	71,450,000	27.47%
Fidelity International Limited		Directly beneficially owned	13,042,000	5.01%
Assetbest Limited	(b)	Directly beneficially owned	32,272,000	12.41%
Templeton Investment Counsel, LLC		Directly beneficially owned	25,132,000	9.66%
Merrill Lynch & Co., Inc.		Directly beneficially owned	14,345,000	5.51%

Notes:

(a) Crisana is wholly owned by Mr. Tse Kam Pang, a director.

(b) Assetbest Limited is wholly owned by Huang Wai Jei.

Save as disclosed above, as at 31 December 2006, no person, other than the directors and chief executive of the Company, whose interests are set out in the section headed "Directors' and chief executive's interests and short positions in shares, underlying shares and debentures" above, had registered an interest of short position in the shares or underlying shares of the Company that was required to be recorded pursuant to Section 336 of the SFO.

SUFFICIENCY OF PUBLIC FLOAT

Based on information that is publicly available to the Company and within the knowledge of the directors, at least 25% of the Company's total issued share capital was held by the public as at the date of this report.

POST BALANCE SHEET EVENT

Details of the significant post balance sheet event of the Group are set out in note 35 to the financial statements.

EMPLOYMENT AND REMUNERATION POLICY

The total number of employees of the Group as at 31 December 2006 was 3,000 (2005: 3,200). The Group's remuneration policies are in line with local market practices where the Group operates and are normally reviewed on an annual basis. In addition to salary payments, there are other staff benefits including provident fund, medical insurance and performance related bonus share option may also be granted to eligible employees and persons of the Group. At 31 December 2006, there were outstanding share options of approximately 18.6 million.

CORPORATE GOVERNANCE

The Company is committed to maintaining the highest standard of corporate governance practices. Information on the corporate governance practices adopted by the Company is set out in the Corporate Governance Report on page 9 to 15.

AUDIT COMMITTEE

The Company has an audit committee which was established in compliance with Rule 3.21 of the Listing Rules for the purpose of reviewing and providing supervision over the Group's financial reporting process and internal controls. The audit committee comprises the three independent non-executive directors of the Company. The financial statements of the Group and of the Company for the year ended 31 December 2006 together with the notes attached thereto have been reviewed by the audit committee, which was of the opinion that such statements complied with the applicable accounting standards, Listing Rules and the legal requirements, and that adequate disclosure has been made.

AUDITORS

Ernst & Young retire and a resolution for their reappointment as auditors of the Company will be proposed at the forthcoming annual general meeting.

ON BEHALF OF THE BOARD

Tse Kam Pang

Chairman and Executive Director

Hong Kong

16 April 2007