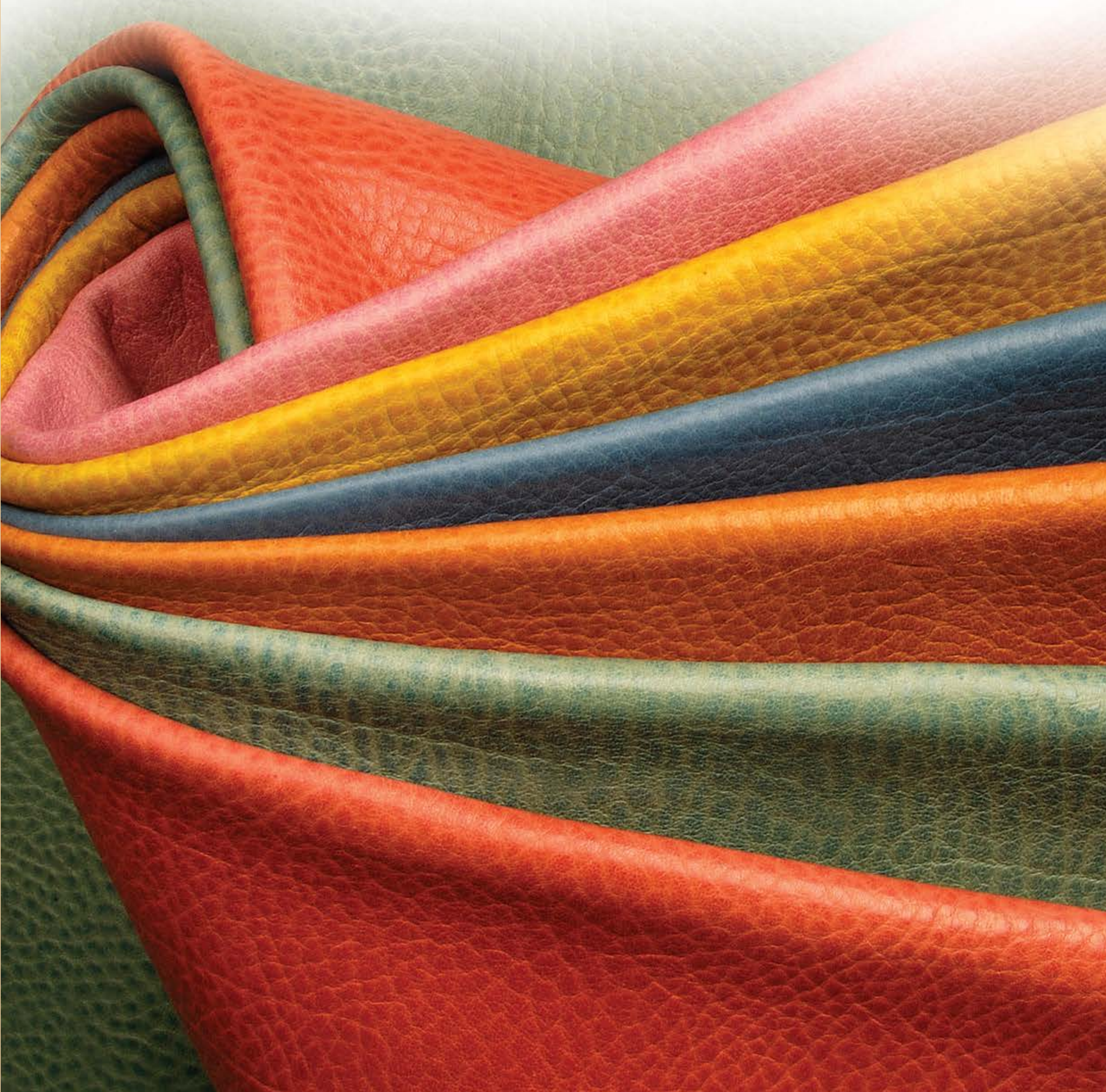
粵海制革有限公司
GUANGDONG TANNERY LIMITED

（股份代號 Stock Code: 1058）

ANNUAL REPORT 2018 年報



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Corporate Information

BOARD OF DIRECTORS

Sun Jun *(Chairman and Managing Director)*
Xiao Zhaoyi#
Kuang Hu#
Ding Yatao#
Fung Lak*
Choi Kam Fai, Thomas*
Chan Cheong Tat*

Non-Executive Director
* *Independent Non-Executive Director*

AUDIT COMMITTEE

Fung Lak *(Chairman)*
Choi Kam Fai, Thomas
Chan Cheong Tat

REMUNERATION COMMITTEE

Choi Kam Fai, Thomas *(Chairman)*
Fung Lak
Chan Cheong Tat

NOMINATION COMMITTEE

Sun Jun *(Chairman)*
Fung Lak
Choi Kam Fai, Thomas
Chan Cheong Tat

COMPANY SECRETARY

Lo Sze Sze

AUDITOR

Ernst & Young

REGISTERED OFFICE

29th Floor, Guangdong Investment Tower
148 Connaught Road Central
Hong Kong

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SHARE REGISTRAR

Tricor Tengis Limited
Level 22, Hopewell Centre
183 Queen's Road East
Hong Kong

SHARE INFORMATION

Place of Listing	:	Main Board of The Stock Exchange of Hong Kong Limited
Stock Code	:	1058
Board Lot	:	2,000 shares
Financial Year End	:	31 December

Highlights

	For the year ended 31 December		
	2018	2017	Change
Sales volume of cowhides (in thousand square feet)	**14,155**	16,684	−15.2%
Revenue (in thousand HK$)	**238,317**	322,146	−26.0%
Loss for the year (in thousand HK$)	**(81,241)**	(99,623)	+18.5%
Basic loss per share (in HK cent)	**(15.10)**	(18.52)	+18.5%

	As at 31 December		
Key Indicators	**2018**	2017	Change
Current Ratio[1]	**2.85 times**	2.75 times	+3.6%
Quick Ratio[2]	**1.16 times**	0.99 times	+17.2%
Debt to asset ratio[3]	**79.2%**	64.1%	+23.6%
Total assets (in thousand HK$)	**284,736**	420,915	−32.4%
Net asset value per share (HK$)	**0.11**	0.28	−60.7%

Notes:

1. $\frac{\text{Current assets}}{\text{Current liabilities}}$

2. $\frac{\text{Current assets} - \text{Stock}}{\text{Current liabilities}}$

3. $\frac{\text{Total liabilities}}{\text{Total assets}}$

Chairman's Statement

RESULTS

I would like to present to the shareholders that the consolidated loss attributable to shareholders of Guangdong Tannery Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") for 2018 was HK$81,241,000 (2017: HK$99,623,000), representing a decrease in loss of 18.5%. Basic loss per share was HK15.10 cents (2017: HK18.52 cents).

DIVIDEND

The board of directors of the Company does not recommend the payment of a final dividend for the year ended 31 December 2018 (2017: Nil).

REVIEW

The year of 2018 witnessed an overall economic downturn in the industry, coupled with a continuous tightening of the environmental protection policies and requirements in relation to the industry. This led to production disruptions among small regional footwear manufacturers, which in turn reduced the demand for footwear leather. Besides, in view of the constant diversification of footwear materials and the growing trend of using new materials as alternatives, the market demand for real leather was gradually dwindling, with de-capacity continuing to gain momentum in the industry. Meanwhile, the increase in the tariffs on US-imported goods led to a rise in the procurement costs, lowering the profitability of industry enterprises and constituting ginormous pressure for the production and operations of the leather processing industry. Against the macro backdrop of an overall diminishing demand in the market, the Group's operating results recorded a loss during the year. In the course of the year, adhering to the business strategy of "stable operations to ensure asset safety", the Group stepped up its efforts in stock reduction with destocking and the realization of positive cash flows as its objectives, so as to ensure funding for the Group's normal operations. Meanwhile, the Group stepped up its efforts in proprietary research and development, enhanced the promotion of its products, worked toward the construction and refinement of environmentally friendly facilities, endeavored to maintain stable production and operations, and mitigated the risks arising from operating business under the weak economic environment.

In response to the dwindling footwear leather market, at the beginning of the year, the Group formulated its budget plan with reference to the market changes to set its production and business targets. Against the backdrop of a more rigorous law enforcement in relation to environmental protection, the Group made reasonable production arrangements during the year through the adjustment and optimization of its technical skills, and reinforced its production sites management as well as products quality inspection and testing for ensuring compliance with the environmental protection indicators and requirements, which mitigated the adverse effects arising from changes in the operating environment to a certain extent. In terms of sales, during the year, the Group proactively tapped into weak markets, refined its customer positioning, and stepped up its efforts toward customer visits, so as to stay abreast of the market changes and prevailing product trends. The Group also endeavored to explore directions for future product development, sparing no effort in furthering its stock reduction. In terms of procurement, during the year, the Group exercised rigorous control over procurement size by adopting a targeted inventory replenishment approach that only involved small quantities but multiple batches, which led to further improvements in its inventories in terms of both structure and aggregate volume, enhanced the development and sales of the work in progress and finished goods constituting the inventories, and contributed to the positive conversion of inventories to cash flows.

Chairman's Statement (Continued)

PROSPECTS

In 2019, economic downturn is expected to carry on in the industry. Given the continuously dwindling overall demand in the footwear leather market, the tannery industry will be met with further challenges. The Group would follow through with each strategic deployment in a holistic approach, adhere to the business strategy of "stable operations to ensure asset safety", and undertake its various activities with a focus on a proactive compression of inventory, a commitment to maintaining its positive cash flows and operational stability. The Group would steadfastly further its operating strategy on destocking, perform product research and development with reference to its inventories, and focus on the development of products with a high added value, so as to bring about further improvements in the inventories in terms of both structure and aggregate volume. Meanwhile, the Group would continue to step up its efforts in market research and survey, enhance the promotion of its products, and maintain the stability of its production and sales. Besides, the Group would continue to foster the construction of a risk control system, and enhance its supervision over safe production in order to ensure compliance with the environmental protection requirements, while making every effort to mitigate all risks and striving to reduce losses.

Sun Jun
Chairman

Hong Kong, 28 March 2019

Management Discussion and Analysis

RESULTS

The Group's consolidated loss attributable to shareholders for the year ended 31 December 2018 was HK$81,241,000, representing a decrease of loss of HK$18,382,000, or 18.5% as compared to the consolidated loss attributable to shareholders of HK$99,623,000 for last year.

The net asset value of the Group as at 31 December 2018 was HK$59,093,000, representing a decrease of HK$92,179,000 and HK$43,226,000 as compared to the net asset value as at 31 December 2017 and 30 June 2018, respectively.

The board of directors of the Company does not recommend the payment of a final dividend for the year ended 31 December 2018.

BUSINESS REVIEW

In 2018, amid the constant changes in the external market environment, an increasing variety of footwear materials as well as the diversification of consumers' demands, de-capacity gained further momentum in the footwear leather industry. The aforesaid, coupled with more stringent governance levels in relation to environmental protection, led to the closure or production suspension of small- and medium-sized footwear manufacturers, resulting in a continuous shrinkage of the demand in the footwear leather market, thus exerting hefty pressure on the production and operation of the leather processing industry. During the year, the Group adhered to its prudent operating strategy with "stable operations to ensure asset safety" as its principal operating concept. Nonetheless, the Group recorded a loss given the fall of both sales volume and selling prices, which further compressed the profitability of the Group. During the year, in order to mitigate the adverse effects arising from the weak economic environment, on one hand, the Group tapped into markets, refined its customer positioning, and proactively developed its external subcontracting business so as to endeavor to reduce its fixed costs; on the other hand, it enhanced its inventory development, adjusted its product structure and stepped up its destocking efforts, in a bid to transform slow-moving inventory into cash flows and ensure funding for the Group's normal operations. To a certain extent, the above measures have mitigated the operating risks arising from the downturn in the industry.

On environmental protection, the national government has been continuously raising its minimum statutory requirements for environmental protection on operations, such that environmental investigations and enquiries are constantly commenced across the country. This has resulted in a large number of small- and medium-sized footwear manufacturers going out of business or suspending their production, which has in turn led to a decline in demand across the entire downstream real leather market. During the year, faced with the adverse and complex external environment, the Group continued to promote the use of clean production technology in order to ensure compliance with sewage discharge standards. Meanwhile, the Group also took active steps in following up with sludge clean-up and transportation and enhanced its all-embracing internal controls in relation to environmental protection, thereby addressing environmental investigations and enquiries properly and ensuring that no environmental protection incident would arise for which the Group might be held liable, which would serve to maintain its operational stability.

Management Discussion and Analysis (Continued)

BUSINESS REVIEW (CONTINUED)

During the year, the total production volume of cowhides was 13,051,000 sq. ft., representing a decrease of 3,329,000 sq. ft. or 20.3% as compared to 16,380,000 sq. ft. for last year. The production volume of grey hides was 3,812 tons, representing a decrease of 3,896 tons or 50.5% as compared to 7,708 tons for last year. During the year, the total sales volume of cowhides was 14,155,000 sq. ft., representing a decrease of 2,529,000 sq. ft. or 15.2% as compared to 16,684,000 sq. ft. for last year. The sales volume of grey hides was 4,010 tons, representing a decrease of 3,712 tons or 48.1% as compared to 7,722 tons for last year.

The consolidated turnover of the Group for 2018 was HK$238,317,000, representing a decrease of HK$83,829,000 or 26.0% from HK$322,146,000 for last year, of which the sales value of cowhides amounted to HK$223,663,000 (2017: HK$296,705,000), representing a decrease of 24.6%, and that of grey hides and other products amounted to HK$14,654,000 (2017: HK$25,441,000), representing a decrease of 42.4%. During the year, the growing trend of using new materials as alternatives, the overall diminishing demand prevailing in the footwear leather market, an inadequate purchasing power of footwear manufacturers and fierce market competition, as well as the Group's enhanced efforts toward the marketing of low-priced products for destocking purposes during the year, all led to tumbled sales volume and unit prices of footwear leather products, accompanied by a decline in sales revenue.

In terms of sales, in light of the use of diversified footwear materials in the market, a reduced demand for real leather, and leather overcapacity in recent years, some of the domestic branded footwear manufacturers have met with operational difficulties, and small- and medium-sized industry enterprises have been seen to suspend their production or go out of business, all resulting in a year-on-year decrease in demand in the tannery market. Faced with the abovementioned hardship, during the year, the Group stepped up its efforts in marketing and on-site market research with particular reference to the market changes and prevailing product trends. It increased its devotion to product research and development with a focus on the development of product varieties that would foster destocking. Besides, the Group was proactively engaged in product promotion and order tracking, and enhanced its sales efforts in relation to the low- and middle-end markets, thereby refining its customer positioning. Meanwhile, the Group strengthened its production sites control and management, as well as safeguarding the product quality and enhancing the added value of its products.

In terms of purchasing, during the year, the Group closely monitored the domestic and international price movements of cowhides, and continuously stepped up its exploration of and research on the latest market circumstances. With stringent control over procurement and a focus on inventory reduction as its overall strategy, the Group adopted a targeted raw materials replenishment approach that involved procurement in small quantities but with multiple batches, such that the funding pressure could be eased. Moreover, in view of the Group's concern surrounding the surges in the prices of chemicals, it implemented procurement of chemicals in a group- or batch-wise manner and was engaged in bargaining and price negotiations with suppliers of chemicals. It reinforced its dynamic management of warehouses and took active steps in identifying alternative products, thereby controlling the costs of chemicals as well as mitigating the risks of chemicals being degenerated and its inventories becoming stagnant. During the year, with destocking and the realization of cash flows as the foremost priorities, the total purchases amounted to HK$166,398,000, representing a decrease of 43.0% as compared to the same period last year.

Management Discussion and Analysis (Continued)

BUSINESS REVIEW (CONTINUED)

As of 31 December 2018, the Group's consolidated inventory amounted to HK$134,131,000 (31 December 2017: HK$218,900,000), representing a decrease of HK$84,769,000 or 38.7% over that of 31 December 2017. The Group steadfastly implemented its operating strategy on destocking, strengthened the synergy among production, supply and sales, developed its sales channels, and furthered the research and development in relation to its technical skills. Factoring in the market demands, the Group performed reasonable group processing and adjustments regarding its inventories in a bid to transform slow-moving inventories into cash flows and ensure funding for the Group's normal operations. The Group reassessed the value of inventories based on its aging and net realizable value, and a net provision for inventories of HK$987,000 was made for the year 2018 (2017: HK$24,004,000).

As at 31 December 2018, the Group's property, plant and equipment amounted to HK$47,057,000 (31 December 2017: HK$65,887,000), representing a decrease of HK$18,830,000 or 28.6% over that of 31 December 2017. Due to the posting of a loss in the operating results of the Group during the year, the recoverable amount of the plant and equipment was calculated by using a value in use calculation based on the discounted cash flow method, and an impairment loss of HK$12,365,000 in respect of the plant and equipment was made for the year 2018 (2017: HK$21,794,000).

FINANCIAL REVIEW

Liquidity and Financial Resources

As at 31 December 2018, the Group's cash and cash equivalents amounted to HK$27,513,000 (31 December 2017: HK$29,108,000), representing a decrease of HK$1,595,000 or 5.5% as compared to the same as at 31 December 2017, which was denominated in Hong Kong dollars (5.7%), Renminbi (92.5%) and United States dollars (1.8%). During the year, net cash inflow from operating activities was HK$40,801,000, which was mainly attributable to a reduction in inventory, resulting in an increase in net cash inflow. Net cash outflow from investing activities was HK$375,000, which was mainly attributable to a decrease in pledged bank deposits. Net cash outflow from financing activities amounted to HK$40,764,000, which mainly consisted of the repayment of short-term loan from a fellow subsidiary.

As at 31 December 2018, the Group's interest-bearing borrowings amounted to HK$142,379,000 in total (31 December 2017: HK$128,956,000), of which interest-bearing borrowings in Hong Kong dollars amounted to HK$65,000,000, and interest-bearing borrowings in United States dollars amounted to HK$77,379,000. The Group's borrowings consisted of long-term unsecured borrowings from the immediate holding company with a balance of HK$142,379,000, on which interests were charged at floating rates.

As at 31 December 2018, the Group's gearing ratio of the interest-bearing borrowings to shareholders' equity plus interest-bearing borrowings was 70.7% (31 December 2017: 46.0%). During the year, the annual interest rates of the borrowings ranged from approximately 2.3% to 5.7%. The Group's interest expenses during the year amounted to HK$5,973,000, representing a decrease of 12.3% from the same period last year, which was mainly attributable to a decrease in the loan amounts granted by banks during the year.

As at 31 December 2018, the total banking facilities of the Group were nil. As at 31 December 2017, the total banking facilities of the Group was HK$119,630,000, of which banking facilities of HK$119,630,000 were unutilized. Taking into account the existing cash resources, the Group has adequate financial resources to meet its day-to-day operational requirements.

Management Discussion and Analysis (Continued)

FINANCIAL REVIEW (CONTINUED)

Capital Expenditure

As at 31 December 2018, the carrying value of non-current assets including prepaid land lease payments and property, plant and equipment amounted to HK$58,516,000, representing a decrease of HK$19,684,000 over the carrying value as at 31 December 2017 of HK$78,200,000. The capital expenditure for the year amounted to HK$1,430,000 (2017: HK$4,661,000), which mainly represented the payments for acquisition of machinery and equipment to meet the production requirements of the Group.

Pledge of Assets

As at 31 December 2018, certain of the Group's bank balances with a total of nil (31 December 2017: HK$1,066,000) were pledged to banks to secure general banking facilities granted to the Group.

Foreign Exchange Exposure

The assets, liabilities and transactions of the Group are basically denominated in Hong Kong dollars, United States dollars, European dollars or Renminbi. The Group is exposed to foreign currency risk primarily from import purchases from overseas suppliers that are denominated in a currency other than the functional currency of the operations to which they relate. The currency giving rise to this risk is mainly the United States dollars against Renminbi. The Group did not hedge its exposure to risks arising from fluctuations in exchange rates during the year. Should the Group consider that its exposure to foreign currency risk justifies hedging, the Group may use forward or hedging contracts to reduce the risks.

Remuneration Policy for Employees

As at 31 December 2018, a total of 393 employees (31 December 2017: 461) were employed by the Group. The Group's remuneration policy is based on the Group's operating results and the employees' performance. The Group has adopted a performance-based appraisal scheme for its employees focusing on "accountability and performance". The incentive bonuses to the management, key officers and staff with outstanding performance under the incentive scheme are determined by reference to the Group's operating net cash flow and profit after tax, calculated by various profit rankings and by applying a measure that links bonuses with the operating results of the Group and further taking into account the individual performance of the staff concerned with an aim to motivate the contribution of its employees. In addition, the Group offered social and medical insurances and pension schemes to all employees in different areas.

Biographical Details of Directors and Senior Management

(A) EXECUTIVE DIRECTOR

Mr. Sun Jun (Age: 45)

Mr. Sun Jun was appointed an Executive Director and the Managing Director of the Company in February 2010. He was appointed the Chairman of the Company with effect from February 2016 and continued to act as the Managing Director of the Company. He is an economist in the People's Republic of China (the "PRC"). He graduated from 西安公路學院 (Xian Highway College) (now known as 長安大學 (Chang'an University)) and obtained a bachelor's degree in 工程機械與起重運輸 (Mechanical Engineering and Lifting Transportation Program). Mr. Sun worked with certain companies of GDH Limited ("GDH"), the immediate controlling shareholder of the Company, from November 2002 to August 2003. He then worked with the Company and its subsidiaries in September 2003 and was appointed to certain posts, including, inter alia, acting as assistant general manager and deputy general manager of the Company from March 2004 to December 2005 and from July 2007 to February 2010 respectively. Mr. Sun currently holds the following posts of wholly-owned subsidiaries of the Company, including the chairman and the general manager of 徐州南海皮廠有限公司 (Xuzhou Nanhai Leather Factory Co., Ltd.), 徐州港威皮革有限公司 (Xuzhou Gangwei Leather Co., Ltd.) and 粵海制革(徐州)有限公司 (Guangdong Tannery (Xuzhou) Limited); and an executive deputy project director of relocation project of 徐州南海皮廠有限公司 (Xuzhou Nanhai Leather Factory Co., Ltd.).

(B) NON-EXECUTIVE DIRECTORS

Mr. Xiao Zhaoyi (Age: 55)

Mr. Xiao Zhaoyi was appointed a Non-Executive Director of the Company in February 2016. He graduated from the Department of Law of Southwest University of Political Science and Law. He obtained a Master's degree in Law from Hainan University and a Master's degree in Business Administration from Murdoch University, Australia. Mr. Xiao had worked as a judge and deputy office director of High People's Court of Guangdong. From December 1996 to October 2005, he acted as the assistant general manager and the general manager of the office of Guangnan (Holdings) Limited ("Guangnan Holdings"), a director of Guangdong Investment Limited ("GDI"), the general manager in Administrative Department and the Company Secretary of GDH and a director and the general manager of China City Water Supply Investment Holding Limited. GDI and Guangnan Holdings are currently the subsidiaries of GDH. Mr. Xiao was then transferred back to the judiciary in October 2005 where he worked at the Guangzhou Intermediate People's Court. He was the division level judge, the third grade senior judge. He also served on a number of leading roles including the division level researcher of the Fourth Civil Court, the division level judge and the presiding judge of the Third Civil Court, the director of Judicial Administration Management Office Equipment, the office director. He was appointed as the general manager of the Legal Department of 廣東粵海控股集團有限公司 (Guangdong Holdings Limited) ("Guangdong Holdings"), the ultimate controlling shareholder of the Company, and GDH for the period from October 2015 to June 2016 and has acted as the chief legal officer of Guangdong Holdings and GDH since June 2016.

Biographical Details of Directors and Senior Management (Continued)

(B) NON-EXECUTIVE DIRECTORS (CONTINUED)

Mr. Kuang Hu (Age: 41)

Mr. Kuang Hu was appointed a Non-Executive Director of the Company in February 2016. He graduated from the Department of International Economics and Trading of Beijing Normal University, PRC. He obtained a Master's degree in World Economics and a Doctoral degree in Finance from Sun Yat-sen University, the PRC. In July 2003, Mr. Kuang joined 廣東粵港投資控股有限公司 (Guangdong Yue Gang Investment Holdings Company Limited) (now known as 廣東粵海控股集團有限公司 (Guangdong Holdings Limited) and defined as "Guangdong Holdings" herein) and worked in Strategic Development Department. From November 2012 to June 2015, he was appointed deputy general manager of Strategic Development Department of both Guangdong Holdings and GDH. He currently acts as the general manager of the Operation Department of Guangdong Holdings and GDH. Mr. Kuang also acts as a director of 徐州南海皮廠有限公司 (Xuzhou Nanhai Leather Factory Co., Ltd.) and 粵海制革(徐州)有限公司 (Guangdong Tannery (Xuzhou) Limited), both of which are wholly-owned subsidiaries of the Company.

Mr. Ding Yatao (Age: 36)

Mr. Ding Yatao was appointed a Non-Executive Director of the Company in March 2018. He graduated from Hubei Normal University, PRC and holds a Bachelor's degree in Economics. He was also a postgraduate in International Trade and holds a Master's degree in Economics from Jinan University, PRC. He worked as a researcher of Canton Public Opinion Research Centre from 2006 to 2008. Between 2008 and 2016, he worked for a number of departments of the People's Government of Guangdong Province in various positions including deputy director of Research Department of Information Centre of the Economic and Trade Commission, director and senior economist of Research Department of Information Centre of the Economic and Information Commission, senior economist of 國際經貿發展中心 (International Economic and Trade Development Centre) and deputy director of General Office of Department of Commerce. Mr. Ding joined Guangdong Holdings and GDH in 2017. He currently acts as general manager of Strategic Development Departments of Guangdong Holdings and GDH. He also acts as a director of certain subsidiaries of Guangdong Holdings and GDH.

(C) INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Fung Lak (Age: 71)

Mr. Fung Lak was appointed an Independent Non-Executive Director of the Company in November 2002. He holds a bachelor degree in Science (Economics) major in Accounting and Finance from the London School of Economics and Political Science of University of London. He is also a fellow member of Hong Kong Institute of Certified Public Accountants, a fellow member of the Institution of Chartered Accountants in the United Kingdom, a fellow member of the Association of Chartered Certified Accountants and a member of the Taxation Institute of Hong Kong. Mr. Fung was the former president of the Society of Chinese Accountants and Auditors. Mr. Fung has over 30 years' experience in the accounting and finance and is a director of Lak & Associates C.P.A. Limited.

Biographical Details of Directors and Senior Management (Continued)

(C) INDEPENDENT NON-EXECUTIVE DIRECTORS (CONTINUED)

Mr. Choi Kam Fai, Thomas (Age: 73)

Mr. Choi Kam Fai, Thomas was appointed an Independent Non-Executive Director of the Company in October 2004. He is a Chartered Professional Accountant with the Chartered Professional Accountants of British Columbia, Canada. He holds a bachelor degree in Commerce and Business Administration from the University of Alberta, Canada and completed the Executive Development Program organized by J.L. Kellogg Graduate School of Management of the Northwestern University, U.S.A. Mr. Choi is the General Manager of the Internal Audit Department of Henderson Land Development Company Limited. He has worked for the audit departments of various private, public and governmental bodies in Hong Kong and Canada for over 30 years.

Mr. Chan Cheong Tat (Age: 69)

Mr. Chan Cheong Tat was appointed an Independent Non-Executive Director of the Company in March 2006. He is a fellow member of Hong Kong Institute of Certified Public Accountants, Association of Chartered Certified Accountants and CPA Australia. He is also an associate member of The Institute of Chartered Secretaries and Administrators in the United Kingdom and The Hong Kong Institute of Chartered Secretaries. Mr. Chan obtained his master's degree in Financial Management from Central Queensland University. He served in the Inland Revenue Department of the Hong Kong Government for 33 years and retired in early 2005. Mr. Chan is currently a director of a tax consultancy company. He also acts as an independent non-executive director of Medicskin Holdings Limited (the shares of which are listed on GEM of The Stock Exchange of Hong Kong Limited (the "Hong Kong Stock Exchange"). He was appointed as an independent non-executive director of Hyfusin Group Holdings Limited and Dominate Group Holdings Company Limited (the shares of both are listed on GEM of the Hong Kong Stock Exchange) in June 2018 and September 2018 respectively. Mr. Chan also acted as an independent non-executive director of Man Sang International Limited (the shares of which are listed on the Main Board of the Hong Kong Stock Exchange) from January 2015 to November 2016.

(D) SENIOR MANAGEMENT

The senior management of the Group comprises the Executive Director above (namely Mr. Sun Jun) and Ms. Lee Wai Mei, the Chief Financial Officer of the Company.

Ms. Lee Wai Mei (Age: 44)

Ms. Lee Wai Mei was appointed the Chief Financial Officer of the Company in May 2005. She has over 15 years of experience in auditing and accounting. She is an associate member of the Hong Kong Institute of Certified Public Accountants and a fellow member of the Association of Chartered Certified Accountants.

Report of the Directors

The directors (the "Directors") of Guangdong Tannery Limited (the "Company") herein present their report and the audited financial statements of the Company and its subsidiaries (together the "Group") for the year ended 31 December 2018.

PRINCIPAL ACTIVITIES

The Company acts as an investment holding company and provides corporate management services to its subsidiaries. The Group is principally engaged in the processing and sale of semi-finished and finished leather. The activities of the principal subsidiaries of the Company are set out in note 1 to the financial statements on page 46 of this Annual Report. There were no significant changes in the nature of the Group's principal activities during the year.

RESULTS AND DIVIDENDS

The results of the Group for the year ended 31 December 2018 and the financial position of the Group at that date are set out in the financial statements on pages 39 and 112 of this Annual Report.

No interim dividend was paid during the year and the board of Directors do not recommend the payment of a final dividend in respect of the year ended 31 December 2018.

DIVIDEND POLICY

The Company considers stable and sustainable returns to shareholders of the Company to be its goal. In deciding whether to propose a dividend and in determining the dividend amount, the board of directors of the Company takes into account the Group's earnings performance, financial position, investment requirements and future prospects. There can be no assurance that a dividend will be proposed or declared in any given year.

BUSINESS REVIEW

A review of the business of the Group during the year and a discussion on the Group's future business development are provided in the Chairman's Statement on pages 4 to 5 and Management Discussion and Analysis on pages 6 to 9 of this Annual Report.

The financial risk management objective and policies of the Group are shown in note 34 to the financial statements on pages 105 to 110 of this Annual Report.

An analysis of the Group's performance during the year using financial key performance indicators is provided in the Highlights on page 3 of this Annual Report.

Discussion on the Group's environmental issues and compliance with the relevant laws and regulations that have a significant impact on the Company are contained in the Management Discussion and Analysis on pages 6 to 9 and in Corporate Governance Report on page 32 of this Annual Report.

The Company's key relationships with its employees, customers and suppliers and business associates that have a significant impact on the Company and on which the Company's success depends are shown in the Management Discussion and Analysis under "Remuneration Policy for Employees" section on page 9 and in the Corporate Governance Report on page 33 of this Annual Report.

Report of the Directors (Continued)

PRINCIPAL RISKS AND UNCERTAINTIES

The following section lists out the key risks and uncertainties faced by the Group. It is a non-exhaustive list and there may be other risks and uncertainties apart from the key areas outlined below. In addition, this Annual Report is not intended to provide any advice or opinion to any person on making investment in the securities of the Company. Investors should exercise their own judgment or consult their investment advisors before investing in the securities of the Company.

Market Risk

Market risk mainly arose from changes in internal and external environments, such as changes in macroeconomic conditions, market demand and supply, competition and relationships with business partners. The external market condition was ever-changing in recent years, and there was a further enhancement in the de-capacity across the tannery industry and environmental protection requirements in place, resulting in the shutting down or suspension of production of small and medium footwear manufacturers, and the market demand for footwear leather has been trimming down continuously. All these factors brought additional risks and uncertainties to the Group's production, operations and profitability. In this regard, the Group adhered to a market-oriented principle, adjusted product structure and stepped up the strength of marketing effort in view of the changes in the market and the trend of products, in order to achieve higher brand value and stronger competitiveness in the industry.

Environmental Compliance Risk

Environmental compliance risk mainly arose from the prescriptive requirements under the environmental policies, laws and regulation of the PRC. In recent years, the central and local governments constantly stepped up law enforcement in environmental protection, which in turn increased the operating costs and legal risks of the Group. In this regard, the Group took active steps in promoting the application of clean production technology and ramping up the standard of its waste processing technology in conjunction with enhancing communication with local governmental departments to establish long-term, effective and close communication channels in a bid to ensure compliance of laws and regulations.

Cost Fluctuation Risk

The cost elements of the Group mainly include the cost of cowhides, chemicals and labours and the expenses relating to production. Price fluctuation of cowhides, under-development of products and inconsistent quality could possibly increase the likelihood of inventory impairment risk for the Group. In this regard, the Group placed most stringent control on the procurement size, and closely monitored dynamic changes and trends of price, quality and quantity in the market of raw materials, and by factoring in the current inventory status, adopted a targeted inventory replenishment approach that only involved small quantities but multiple batches. In the meantime, the Group focused on developing product type and marketing effort for destocking, in an effort to mitigate inventory risk and alleviate cash flow pressure.

Report of the Directors (Continued)

PRINCIPAL RISKS AND UNCERTAINTIES (CONTINUED)

Liquidity Risk

Insufficient fund availability is a significant constraint for enterprises to carry out necessary activities. When any liability falls due, the contract performance risk may be increased. In recent years, demand in the tannery market witnessed a year-on-year slippage. Downstream footwear manufactures were frequently found encountering difficulties in operations or having shut the operations down, which could possibly result in receivables unable to be recovered. Instability in the financial market may lead to an increase in interest rate and exchange rate risks. In this regard, in managing liquidity risk, the Group has set out higher risk consciousness, timely monitor and analyze interest rate and exchange rate movements in the market, create a model to calculate and forecast cash flows, ensure the formation of a cash flow-oriented production, supply and sales model, take active steps in reducing current inventory level and guarantee cash flows for normal business operations so as to mitigate the impact arising from cash flow fluctuations.

FINANCIAL SUMMARY

The following is a summary of the published results and assets and liabilities of the Group for the last five financial years, as extracted from the audited financial statements. The summary does not form part of the audited financial statements.

Results

	Year ended 31 December				
	2018	2017	2016	2015	2014
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Revenue	**238,317**	322,146	456,722	652,729	767,185
Profit/(loss) from operating activities	**(75,062)**	(92,074)	(34,735)	(28,357)	11,967
Finance costs	**(5,973)**	(6,808)	(5,238)	(10,533)	(6,676)
Profit/(loss) before tax	**(81,035)**	(98,882)	(39,973)	(38,890)	5,291
Income tax credit/(expense)	**(206)**	(741)	(21)	541	(3,293)
Profit/(loss) for the year	**(81,241)**	(99,623)	(39,994)	(38,349)	1,998

Report of the Directors (Continued)

FINANCIAL SUMMARY (CONTINUED)

Assets and liabilities

	As at 31 December				
	2018	2017	2016	2015	2014
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Assets					
Non-current assets	**58,516**	78,200	99,097	116,202	117,999
Current assets	**226,220**	342,715	456,526	490,816	641,054
Total assets	**284,736**	420,915	555,623	607,018	759,053
Liabilities					
Current liabilities	**79,424**	124,610	188,086	175,714	404,909
Non-current liabilities	**146,219**	145,033	142,145	140,689	1,591
Total liabilities	**225,643**	269,643	330,231	316,403	406,500
Net assets	**59,093**	151,272	225,392	290,615	352,553

PROPERTY, PLANT AND EQUIPMENT

Details of movements in the property, plant and equipment of the Group during the year are set out in note 11 to the financial statements.

LOANS FROM A FELLOW SUBSIDIARY AND THE IMMEDIATE HOLDING COMPANY

Details of the loans from a fellow subsidiary and the immediate holding company of the Company as at 31 December 2018 are set out in note 18 to the financial statements.

SHARES ISSUED

Details of the Company's shares issued during the year are set out in note 22 to the financial statements.

EQUITY-LINKED AGREEMENTS

Save as disclosed in the section headed "SHARE OPTIONS OF THE COMPANY" of this report and "SHARE OPTION SCHEME" in note 24 to the financial statements, no equity-linked agreement was entered into by the Company during the year.

Report of the Directors (Continued)

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

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

RESERVES

Details of movements in the reserves of the Group during the year are set out in the consolidated statement of changes in equity.

DISTRIBUTABLE RESERVES

At 31 December 2018, no reserves of the Company, calculated in accordance with the provisions of sections 291, 297 and 299 of the Hong Kong Companies Ordinance, is available for cash distribution.

CHARITABLE CONTRIBUTIONS

The Group did not make any charitable contributions during the year (2017: Nil).

DIRECTORS

The Directors during the year and up to the date of this report were:

Sun Jun *(Chairman and Managing Director)*
Xiao Zhaoyi#
Kuang Hu#
Ding Yatao# *(appointed on 24 March 2018)*
Fung Lak*
Choi Kam Fai, Thomas*
Chan Cheong Tat*
Ran Bo# *(resigned on 24 March 2018)*

Non-Executive Director
* *Independent Non-Executive Director*

In accordance with Articles 82 to 84 of the Articles of Association of the Company, Mr. Kuang Hu and Mr. Fung Lak will retire by rotation at the annual general meeting of the Company to be held on Wednesday, 12 June 2019 (the "2019 AGM") and, being eligible, have offered themselves for re-election.

Mr. Kuang Hu and Mr. Fung Lak, if re-elected, will hold office from the date of re-election to the earlier of (i) the conclusion of the annual general meeting of the Company to be held in 2022, and (ii) 30 June 2022, subject to earlier determination in accordance with the Articles of Association of the Company and/or any applicable laws and regulations.

Report of the Directors (Continued)

DIRECTORS OF SUBSIDIARIES

The names of directors who have served on the boards of the subsidiaries of the Company during the year ended 31 December 2018 and up to the date of this report are set out below (in alphabetical order):

Mr. Ding Yatao, Mr. Fan Chenxiao, Mr. Kuang Hu, Ms. Lee Wai Mei, Mr. Qiao Jiankang, Mr. Ran Bo, Mr. Sun Jun, Mr. Zhou Hao and Mr. Zhuang Xiaobin

DIRECTORS' SERVICE CONTRACT

No Director proposed for re-election at the 2019 AGM has a service contract with the Group which is not determinable within one year without payment of compensation, other than statutory compensation.

DIRECTORS' MATERIAL INTERESTS IN TRANSACTIONS, ARRANGEMENTS OR CONTRACTS

No transactions, arrangements and contracts of significance in relation to the Group's business to which the Company, the Company's subsidiaries, fellow subsidiaries or its parent company was a party and in which a Director or his connected entity had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

PERMITTED INDEMNITY PROVISION

Indemnity provision within the meaning of permitted indemnity provision under the Hong Kong Companies Ordinance for the benefit of the Directors is currently in force and was in force throughout the year ended 31 December 2018. In addition, the Company has taken out and kept in force appropriate directors' and officers' liability insurance coverage for the Directors and officers of the Company.

DIRECTORS' INTERESTS IN COMPETING BUSINESS

As at 31 December 2018, none of the Directors was interested in any business, apart from the Group's business, which competes or is likely to compete, either directly or indirectly, with the business of the Group.

MANAGEMENT CONTRACTS

No contract concerning the management and administration of the whole or any substantial part of the business of the Company was entered into or existed during the year.

Report of the Directors (Continued)

DIRECTORS' INTERESTS AND SHORT POSITIONS IN SECURITIES

As at 31 December 2018, the interests and short positions of the Directors and the chief executive of the Company in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) which were required to be (i) notified to the Company and The Stock Exchange of Hong Kong Limited (the "Hong Kong Stock Exchange") pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which the Directors and the chief executive were taken or deemed to have under such provisions of the SFO); (ii) entered in the register kept by the Company pursuant to section 352 of the SFO; or (iii) notified to the Company and the Hong Kong Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 to the Rules Governing the Listing of Securities on the Hong Kong Stock Exchange (the "Listing Rules"), were as follows:

Interests and Short Positions in the Company

Interests in ordinary shares

Name of Director	Capacity/ nature of interests	Number of ordinary shares held	Long/short position	Approximate percentage of interests held *(Note)*
Sun Jun	Personal	40,000	Long position	0.007%
Fung Lak	Personal	1,380,000	Long position	0.256%
Choi Kam Fai, Thomas	Personal	60,000	Long position	0.011%

Note: The approximate percentage of interests held was calculated on the basis of 538,019,000 ordinary shares of the Company in issue as at 31 December 2018.

Save as disclosed above, as at 31 December 2018, to the knowledge of the Company, none of the Directors or the chief executive of the Company had any interests or short positions in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which are required to be: (i) notified to the Company and the Hong Kong Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which the Directors and the chief executive are taken or deemed to have under such provisions of the SFO); (ii) entered in the register kept by the Company pursuant to Section 352 of the SFO; or (iii) notified to the Company and the Hong Kong Stock Exchange pursuant to the Model Code.

Report of the Directors (Continued)

SUBSTANTIAL SHAREHOLDERS' INTERESTS

As at 31 December 2018, so far as is known to any Director or the chief executive of the Company, the following persons (other than a Director or the chief executive of the Company) had, or were deemed or taken to have interests or short positions in the shares or underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or which were recorded in the register kept by the Company pursuant to section 336 of the SFO:

Name of Shareholder	Capacity/nature of interests	Number of ordinary shares held	Long/short position	Approximate percentage of interests held *(Note 1)*
廣東粵海控股集團有限公司 (Guangdong Holdings Limited) *(Note 2)*	Interest in controlled corporation	383,820,000	Long position	71.34%
GDH Limited	Beneficial owner	383,820,000	Long position	71.34%

Notes:

1. The approximate percentage of interests held was calculated on the basis of 538,019,000 ordinary shares of the Company in issue as at 31 December 2018.

2. The attributable interest which 廣東粵海控股集團有限公司 (Guangdong Holdings Limited) has in the Company is held through its 100% direct interest in GDH Limited.

Save as disclosed above, as at 31 December 2018, so far as is known to any Director or the chief executive of the Company, there were no other persons (other than a Director or the chief executive of the Company) who had, or were deemed or taken to have interests or short positions in the shares or underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or which were recorded in the register kept by the Company pursuant to section 336 of the SFO.

SHARE OPTIONS OF THE COMPANY

During the year ended 31 December 2018, no share options have been granted, exercised, cancelled or lapsed under the share option scheme adopted by the Company on 24 November 2008 (the "2008 Scheme"). As at 31 December 2018 and 31 December 2017, there were no share options outstanding under the 2008 Scheme. The detailed terms of the 2008 Scheme are set out in note 24 to the financial statements.

Report of the Directors (Continued)

SIGNIFICANT CONTRACTS WITH CONTROLLING SHAREHOLDER

Save as disclosed in notes 18 and 29 to the financial statements, the Group and the controlling shareholders of the Company had not entered into any other contracts of significance during the year.

ARRANGEMENTS TO ACQUIRE SHARES OR DEBENTURES

Save as disclosed in the section headed "SHARE OPTIONS OF THE COMPANY" of the report and in note 24 to the financial statements, at no time during the year was the Company, or any of its subsidiaries, its holding companies or its fellow subsidiaries a party to any arrangements to enable the Directors or their spouses or children under 18 years of age to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

RELATED PARTY TRANSACTIONS AND CONNECTED TRANSACTIONS

Details of the related party transactions undertaken in the normal course of business of the Group are provided under note 29 to the financial statements. None of the related party transactions constituted discloseable non-exempted connected transaction or non-exempted continuing connected transaction under the Listing Rules.

MAJOR CUSTOMERS AND SUPPLIERS

For the year ended 31 December 2018, the amount of purchases attributable to the Group's largest supplier represented 19% of the Group's total purchases; and the aggregate amount of purchases (excluding the purchases of items of a capital nature) attributable to the Group's five largest suppliers represented 55% of the Group's total purchases. In addition, the amount of turnover attributable to the Group's largest customer represented 9% of the Group's total turnover; and the aggregate amount of the turnover attributable to the Group's five largest customers represented 29% of the Group's total turnover. None of the Directors or their associates, or any shareholders (which, to the best knowledge of the Directors, owns more than 5% of the Company's issued share capital) had any beneficial interest in the Group's five largest suppliers or customers.

PUBLIC FLOAT

As at the date of this report, the Company has maintained the prescribed public float under the Listing Rules based on the information that is publicly available to the Company and within the knowledge of the Directors.

Report of the Directors (Continued)

CHANGES IN DIRECTORS' INFORMATION

The changes in information of the Directors of the Company are set out below:

(1) With effect from 26 September 2018, Mr. Chan Cheong Tat was appointed an independent non-executive director of Dominate Group Holdings Company Limited, the shares of which have been listed on GEM of the Hong Kong Stock Exchange since 27 March 2019.

(2) Mr. Ding Yatao ceased to act as a director of 徐州南海皮廠有限公司 (Xuzhou Nanhai Leather Factory Co., Ltd.), 徐州港威皮革有限公司 (Xuzhou Gangwei Leather Co., Ltd.) and 粵海制革（徐州）有限公司 (Guangdong Tannery (Xuzhou) Limited) with effect from 30 August 2018.

Save for the above changes in Directors' information, there is no other information that is required to be disclosed pursuant to Rule 13.51B(1) of the Listing Rules.

AUDITOR

A resolution will be proposed at the 2019 AGM for the reappointment of Messrs. Ernst & Young as the auditor of the Company.

By order of the Board
Sun Jun
Chairman and Managing Director

Hong Kong, 28 March 2019

Corporate Governance Report

CORPORATE GOVERNANCE PRACTICES

The Group recognizes the importance of achieving the highest standard of corporate governance consistent with the needs and requirements of its business and the best interest of all of its stakeholders and is fully committed to doing so. It is also with these objectives in mind that the Group has applied the principles of the Corporate Governance Code (the "CG Code") contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules").

In the opinion of the directors of the Company (the "Directors"), the Company had complied with the code provisions and, where appropriate, the applicable recommended best practices in the CG Code throughout the year ended 31 December 2018 except for the following:

The code provision A.2.1 of the CG Code provides that the roles of chairman and chief executive should be separate and should not be performed by the same individual (the Company regards that the term "chief executive" has the same meaning as the Managing Director of the Company).

Mr. Sun Jun serves as both the Chairman and the Managing Director of the Company with effect from 26 February 2016. The Board believes that vesting the roles of both Chairman and Managing Director in the same person provides the Group with strong and consistent leadership and allows for effective and efficient planning and implementation of business strategies and decisions. It also considers that the current structure of vesting the roles of Chairman and Managing Director in the same person will not impair the balance of power and authority between the Board and the management of the Company. The Board will review the current structure from time to time to ensure appropriate and timely action to meet changing circumstances.

DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 to the Listing Rules as its own code of conduct regarding Directors' securities transactions. All Directors confirmed, upon specific enquiry by the Company, that they had complied with the required standard as set out in the Model Code during the year.

BOARD OF DIRECTORS

As at the date of this Annual Report, the Board of Directors (the "Board") comprises one Executive Director, being Mr. Sun Jun, three Non-Executive Directors, being Mr. Xiao Zhaoyi, Mr. Kuang Hu and Mr. Ding Yatao and three Independent Non-Executive Directors, being Mr. Fung Lak, Mr. Choi Kam Fai, Thomas and Mr. Chan Cheong Tat.

The Board is responsible for the leadership and control of the Company and oversees the Group's businesses, strategic decisions and performances. The management is delegated with the authority and responsibility by the Board for the day-to-day management of the Group. Major corporate matters that are specifically delegated by the Board to the management include the preparation of interim and annual reports and announcements for Board approval before publishing, execution of business strategies and initiatives adopted by the Board, implementation of adequate systems of internal controls and risk management procedures, and compliance with relevant statutory and regulatory requirements and rules and regulations.

Corporate Governance Report (Continued)

BOARD OF DIRECTORS (CONTINUED)

The Board members do not have any financial, business, family or other material/relevant relationships with each other. Such balanced Board composition ensures that strong independence exists across the Board. The biographies of the Directors are set out in pages 10 to 12 of this Annual Report, which demonstrate a diversity of skills, expertise, experience and qualifications.

The Board meets regularly to discuss the overall strategy as well as the operation and financial performance of the Company, and to review and approve the Company's annual, interim and quarterly results. During the financial year ended 31 December 2018, four Board meetings were held and attendance of each Director at the Board meetings is set out in the section headed "BOARD AND COMMITTEE MEETINGS" of this report.

CHAIRMAN AND MANAGING DIRECTOR

Mr. Sun Jun serves as the Chairman of the Board and also as the Managing Director of the Company. He has executive responsibilities, provides leadership for the Board and ensures a proper and effective functioning of the Board in discharge of its responsibilities. He is also accountable to the Board for the overall implementation of the Company's strategies and the co-ordination of overall business operations. The Board believes that vesting the roles of both Chairman and Managing Director in the same person provides the Group with strong and consistent leadership and allows for effective and efficient planning and implementation of business strategies and decisions.

The Board considers that the current structure of vesting the roles of Chairman and Managing Director in the same person will not impair the balance of power and authority between the Board and the management of the Company. The Board will review this structure from time to time to ensure appropriate and timely action to meet changing circumstances.

NON-EXECUTIVE DIRECTORS

All Directors, including Non-Executive Directors, appointed to fill a causal vacancy or as an addition to the existing Board, shall hold office only until the first general meeting after his appointment and shall then be eligible for re-election. Moreover, all Non-Executive Directors (including Independent Non-Executive Directors) are appointed for a term of not more than approximately three years expiring on the earlier of either (i) the conclusion of the annual general meeting of the Company in the year of the third anniversary of the appointment or re-election of that Director, or (ii) the expiration of the period within which the annual general meeting of the Company is required to be held in the year of the third anniversary of the appointment or re-election of that Director and in any event, subject to earlier determination in accordance with the Articles of Association of the Company and/or applicable laws and regulations.

INDEPENDENCE OF INDEPENDENT NON-EXECUTIVE DIRECTORS

During the year under review and up to the date of this report, the Company has complied with the requirements under Rule 3.10(1), 3.10(2) and 3.10A of the Listing Rules. The Company has received confirmation of independence from the three Independent Non-Executive Directors, namely Mr. Fung Lak, Mr. Choi Kam Fai, Thomas and Mr. Chan Cheong Tat, in accordance with Rule 3.13 of the Listing Rules. The Company has assessed their independence and concluded that all the Independent Non-Executive Directors are independent within the definition of the Listing Rules.

Corporate Governance Report (Continued)

INDEPENDENCE OF INDEPENDENT NON-EXECUTIVE DIRECTORS (CONTINUED)

Mr. Fung Lak, Mr. Choi Kam Fai, Thomas and Mr. Chan Cheong Tat served the Board for more than nine years. They have clearly demonstrated their willingness to exercise independent judgment and to provide objective challenges to the management. There is no evidence that length of tenure is having an adverse impact on their independence. The Board therefore considers that Mr. Fung, Mr. Choi and Mr. Chan remain independent, notwithstanding the length of their tenure.

DIRECTORS' INDUCTION AND CONTINUOUS PROFESSIONAL DEVELOPMENT

Upon appointment to the Board, each new Director receives an induction package covering business operations, policy and procedures of the Company as well as the general, statutory and regulatory obligations of being a Director to ensure that he is sufficiently aware of his responsibilities under the Listing Rules and other relevant regulatory requirements.

The Directors are briefed on the amendments to or updates on the relevant laws, rules and regulations. In addition, the Company encourages the Directors to enroll in a wide range of professional development courses and seminars relating to the Listing Rules, Hong Kong ordinances and corporate governance practices so that they can continuously update and further improve their relevant knowledge and skills. Some Directors attended seminars and conferences organized by government authorities, professional bodies and industrial organizations in relation to corporate governance, updates on laws, rules and regulations, accounting, financial, management or other professional skills. The Company organized a seminar in October 2018 for the Directors on "Liquidation of PRC Companies". Reading materials have also been provided to the Directors to develop and refresh their professional skill.

According to the records kept by the Company, the Directors attended the following trainings during the year ended 31 December 2018.

Name of Director	Seminar and Conferences	Reading materials
Executive Director		
Sun Jun	✓	✓
Non-Executive Directors		
Xiao Zhaoyi	✓	✓
Kuang Hu	✓	✓
Ding Yatao *(appointed on 24 March 2018)*	✓	✓
Ran Bo *(resigned on 24 March 2018)*	N/A	N/A
Independent Non-Executive Directors		
Fung Lak	✓	✓
Choi Kam Fai, Thomas	✓	✓
Chan Cheong Tat	✓	✓

Corporate Governance Report (Continued)

BOARD DIVERSITY POLICY

The Board has adopted a board diversity policy (the "Board Diversity Policy") on 23 August 2013 which sets out the approach to achieve diversity on the Board.

The Company recognizes and embraces the benefits of having a diversified Board and sees increasing diversity at Board level as an essential element in supporting the attainment of the Company's strategic objectives and sustainable development.

The Company seeks to achieve Board diversity through the consideration of a number of factors, including but not limited to gender, age, cultural and educational background, professional experience, skills, knowledge and length of service. The Company will also take into consideration its own business model and specific needs from time to time. All Board appointments will be based on meritocracy, and candidates will be considered against objective criteria, having due regard to the benefits of diversity on the Board.

The Nomination Committee of the Board has set the measurable objectives based on five focused areas: gender, age, length of service, professional experience and skills and knowledge for the implementation of Board diversity of the Company. The Nomination Committee reviews the Board Diversity Policy, as appropriate, to ensure its continued effectiveness from time to time.

As at the date of this report, the Board comprises seven directors. Three of them are Independent Non-Executive Directors, thereby promoting critical review and control of the management process. The Board has maintained a balanced composition in terms of age, professional experience, skills and knowledge, and has performed effectively.

Having reviewed the implementation of the Board Diversity Policy and the structure, size and composition of the Board, the Nomination Committee considered that the requirement of the Board Diversity Policy had been met.

CORPORATE GOVERNANCE FUNCTIONS

It is the responsibility of the Board to determine the appropriate corporate governance practices applicable to the Company's circumstances and to ensure processes and procedures are in place to achieve the Company's corporate governance objectives.

The duties of the Board performing corporate governance functions are set out below:

1. to develop and review the Company's policies and practices on corporate governance;

2. to review and monitor the training and continuous professional development of Director and senior management of the Company;

3. to review and monitor the Company's policies and practices on compliance with legal and regulatory requirements;

4. to develop, review and monitor the code of conduct and compliance manual (if any) applicable to employees and Directors of the Company; and

5. to review the Company's compliance with the CG Code and disclosure in the Corporate Governance Report.

Corporate Governance Report (Continued)

CORPORATE GOVERNANCE FUNCTIONS (CONTINUED)

During the year under review, the Board considered the following corporate governance issues:

(i) adopted the Nomination Policy (as defined in the section headed "NOMINATION COMMITTEE" of this report below) and the revised terms of reference of the Nomination Committee;

(ii) compiled the Environmental, Social and Governance Reporting for the year of 2018; and

(iii) reviewed the effectiveness of the internal controls and risk management systems of the Company through the Audit Committee.

REMUNERATION COMMITTEE

The Company established the Remuneration Committee in June 2005. The terms of reference of the Remuneration Committee detailing the authorities and duties are available on the Company's website.

The Remuneration Committee comprises three Independent Non-Executive Directors, being Mr. Choi Kam Fai, Thomas, Mr. Fung Lak and Mr. Chan Cheong Tat. Mr. Choi Kam Fai, Thomas is the Chairman of the Remuneration Committee.

During the financial year ended 31 December 2018, the Remuneration Committee held one meeting to approve the annual review of the remuneration package for the Executive Director. The attendance of each member of the Remuneration Committee is set out in the section headed "BOARD AND COMMITTEES MEETINGS" of this report.

Details of the amount of Directors' remuneration for the year 2018 are set out in note 8 to the financial statements.

NOMINATION COMMITTEE

The Company established the Nomination Committee in June 2005. The terms of reference of the Nomination Committee detailing the authority and duties are available on the Company's website.

The Nomination Committee comprises one Executive Director, being Mr. Sun Jun and three Independent Non-Executive Directors, being Mr. Fung Lak, Mr. Choi Kam Fai, Thomas and Mr. Chan Cheong Tat. Mr. Sun Jun is the Chairman of the Nomination Committee.

The Nomination Committee is responsible for reviewing the structure, size and composition of the Board, identifying individuals suitably qualified to become Board members, assessing the independence of its Independent Non-Executive Directors in accordance with the criteria prescribed under the Listing Rules and the CG Code, considering the reappointment of the Directors and succession planning for Directors and making recommendations to the Board in respect of the aforesaid matters.

NOMINATION COMMITTEE (CONTINUED)

The Board adopted a nomination policy (the "Nomination Policy") on 26 October 2018 to formally set out the criteria and process in the nomination and appointment of Directors. According to the Nomination Policy, the ultimate responsibility for selection and appointment of Directors rests with the entire Board or the shareholders in general meeting, as the case may be. The Board has delegated the relevant screening and evaluation process to the Nomination Committee, which identifies suitably qualified Director candidates and recommends them to the Board. In assessing the suitability of a proposed candidate, the Nomination Committee takes into consideration the candidate's character and integrity, qualifications, skills, knowledge, experiences relevant to the Company's business and corporate strategy, his/her commitment to enhancing shareholder value and devoting sufficient time to effectively carry out their duties, fulfilment of the independence requirements as set out in the Listing Rules (for Independent Non-Executive Directors) and diversity on the Board. After reaching its decision, the Nomination Committee nominates relevant Director candidates to the Board for approval and appointment. As said above, all Directors appointed to fill a casual vacancy or as an addition to the existing Board shall hold office until the first general meeting after his or her appointment and shall be eligible for re-election. The Board will make recommendation to shareholders in respect of the proposed re-election of Directors at general meeting.

During the financial year ended 31 December 2018, the Nomination Committee held two meetings (i) to review the structure, size and composition of the Board; (ii) to assess the independence of Independent Non-Executive Directors; (iii) to make recommendations to the Board on the appointment of Director and the re-election of Directors; and (iv) to propose the adoption of the Nomination Policy and the amendment to the terms of reference of the Nomination Committee. The attendance of each member of the Nomination Committee is set out in the section headed "BOARD AND COMMITTEES MEETINGS" of this report.

AUDIT COMMITTEE

The Audit Committee was established in September 1998. The terms of reference of the Audit Committee detailing the authority and duties are available on the Company's website.

The Audit Committee comprises three Independent Non-Executive Directors, being Mr. Fung Lak, Mr. Choi Kam Fai, Thomas and Mr. Chan Cheong Tat who all possess the required experience and knowledge in the accounting profession. Mr. Fung Lak is the Chairman of the Audit Committee.

During the financial year ended 31 December 2018, the Audit Committee held five meetings. It reviewed the 2017 annual results, the 2018 interim results and the 2018 quarterly results of the Company before their submission to the Board and monitored the integrity of such financial statements/financial information. The Audit Committee oversees matters concerning the external auditors including making recommendations to the Board regarding the appointment of the external auditors, reviewing the scope of their audit and work and approving their fees. In addition to the five meetings as aforesaid, the Audit Committee also had a private meeting with the external auditor without the presence of the management to discuss any area of concern. The Audit Committee further ensures that the management has put in place effective systems of risk management and internal control and maintains an overview of the Group's risk assessment, control and management processes. It reviews the adequacy of resources, qualifications and experience of staff of the Group's accounting, internal audit and financial reporting function and their training programmes and budget. In addition, it reviews the internal audit schedules of the Group, considers the Group's internal audit reports and monitors the effectiveness of the internal audit function. The attendance of each member of the Audit Committee is set out in the section headed "BOARD AND COMMITTEES MEETINGS" of this report.

Corporate Governance Report (Continued)

AUDITOR'S REMUNERATION

During the year under review, the remuneration paid/payable to the Company's auditor, Messrs. Ernst & Young, is set out as follows:

Services rendered	**Fee paid/payable** *HK$'000*
Audit of Final Results	1,450
Review of Interim Results	350

BOARD AND COMMITTEES MEETINGS

The individual attendance records of each Director at the meetings of the Board, Remuneration Committee, Nomination Committee, Audit Committee and general meeting during the year ended 31 December 2018 are set out below:

Name of Director	**Board Meeting**	**Remuneration Committee Meeting**	**Nomination Committee Meeting**	**Audit Committee Meeting**	**Annual General Meeting**
Executive Director					
Sun Jun	4/4	—	2/2	—	1/1
Non-Executive Directors					
Xiao Zhaoyi	4/4	—	—	—	1/1
Kuang Hu	4/4	—	—	—	0/1
Ding Yatao *(appointed on 24 March 2018)*	2/3	—	—	—	1/1
Ran Bo *(resigned on 24 March 2018)*	1/1	—	—	—	N/A
Independent Non-Executive Directors					
Fung Lak	4/4	1/1	2/2	5/5	1/1
Choi Kam Fai, Thomas	4/4	1/1	2/2	5/5	1/1
Chan Cheong Tat	4/4	1/1	2/2	5/5	1/1

ACCOUNTABILITY AND AUDIT

The Board is responsible for overseeing the preparation of financial statements for the year ended 31 December 2018, which give a true and fair view of the state of affairs of the Group and of the results and cash flows for that financial year. In preparing the financial statements for the year ended 31 December 2018, the Board has selected appropriate accounting policies, applied them consistently in accordance with the Hong Kong Financial Reporting Standards and Hong Kong Accounting Standards which are pertinent to its operations and relevant to the financial statements and, made judgements and estimates that are prudent and reasonable, and have prepared the financial statements on the going concern basis.

Corporate Governance Report (Continued)

ACCOUNTABILITY AND AUDIT (CONTINUED)

The Company endeavors to present a balanced, clear and comprehensible assessment of the Group's performance, position and prospects. The annual and interim results of the Company are announced in a timely manner within the limit of three months and two months respectively after the end of the relevant periods in accordance with the Listing Rules. To further enhance the Company's level of corporate governance and transparency, the Company has announced its unaudited quarterly financial information during the financial year ended 31 December 2018, and will continue to publish unaudited financial information quarterly in the future.

The Directors have acknowledged their responsibility for preparing all information and representations contained in the financial statements of the Company for the year ended 31 December 2018.

RISK MANAGEMENT AND INTERNAL CONTROL

The Board is responsible for the Group's system of internal controls, risk management and their effectiveness. The internal control system has been designed to mitigate the Group's risk exposure; to facilitate the effectiveness and efficiency of operations; to safeguard the assets against loss and misappropriation; to maintain proper accounting records for producing reliable financial information and ensuring compliance with applicable laws and regulations.

The management under the supervision of the Internal Audit Department and the Board has reviewed, among other things, the profile of the significant risks and identified, evaluated and managed the significant risks faced by the Group including the changes in the nature and extent of significant risks, and the ability to respond to changes in its business and the external environment, the scope and quality of management's ongoing monitoring of the risk management and internal control systems, and updating the systems of risk management and internal control when there are changes to business environment or regulatory guidelines. In addition, the management review the work of internal audit function and other assurance providers, the extent and frequency of communication of monitoring results to the Audit Committee which enables it to assess control of the Group and the effectiveness of risk management, any significant failing or weaknesses in internal control that have been reported, the necessary actions that are being taken promptly to remedy any significant failings or weaknesses, and the effectiveness of the Group's processes for financial reporting and Listing Rules compliance.

The risk management and internal control systems of the Group comprises a well-established organisational structure and comprehensive policies and standards. The Board has clearly defined the authorities and key responsibilities of each operational unit to ensure adequate checks and balances. The management assists the Board in the implementation of the Board's relevant policies and procedures on risk and control by identifying and assessing the risks faced, and involving in the design, operation and monitoring of suitable internal controls to mitigate and control these risks. The key processes that have been established in reviewing the adequacy and integrity of the system of risk management and internal control and assessing the effectiveness of internal control include the following:

A defined management structure is maintained with specified limits of authority and control responsibilities, which is designed to (a) safeguard assets from inappropriate use; (b) maintain proper accounts; (c) ensure compliance with regulations; and (d) identify, manage and mitigate key risks to the Group.

Corporate Governance Report (Continued)

RISK MANAGEMENT AND INTERNAL CONTROL (CONTINUED)

The Audit Committee is established to, inter alia, review the financial controls, risk management and internal control systems of the Group and any significant internal control issues identified by the internal audit department, external auditors, regulatory authorities and management. It also conducts review of the internal audit functions with particular emphasis on the scope and quality of the internal audits and independence of the internal audit department. During its annual review, the Audit Committee also considers the adequacy of resources, qualifications and experience of staff of the Group's accounting, internal audit and financial reporting function, and their training programmes and budgets.

The internal audit department monitors compliance with policies and procedures and the effectiveness of the risk management and internal control systems, and highlight significant findings in respect of any non compliance. It plays an important role in the Group's internal control framework, and provides objective assurance to the Board that a sound internal control system is maintained and operated in compliance with the established processes and standards by performing periodic checking. Using a risk-based approach, the internal audit department plans its internal audit schedules annually with audit resources being focused on higher risk areas. It carried out an entity-level risk assessment which includes identification, evaluation and prioritization of risk factors that the Company is facing. It completed the risk assessment and has submitted the assessment results (including the annual internal audit plan) to the management of the Company for review and reported to the Audit Committee and the Board for approval. The internal audit department issues reports to the Board and relevant management covering various operational and financial processes of the Group and provides summary reports to the Audit Committee together with the status of implementation of their recommendation in each Audit Committee meeting.

The Board has conducted an annual review of the effectiveness of the Group's system of internal control covering all material controls, including financial, operational and compliance controls and risk management system. The Board is satisfied that the systems of risk management and internal control in place for the year under review and up to the date of issuance of the annual report and accounts are reasonably effective and adequate.

There are also procedures including pre-clearance on dealing in the Group's securities by designated Directors, notification of regular blackout period and securities dealing restrictions to Directors and relevant employees, and dissemination of information for specified purposed and on a need-to-know basis have been implemented to guard against possible mishandling of inside information within the Group.

COMPANY SECRETARY

Ms. Lo Sze Sze, the Company Secretary of the Company, is not a full time employee of the Company. She reports to the Chairman of the Company and is responsible for advising the Board on corporate governance matters of the Company. The primary contact person of the Company with Ms. Lo is Ms. Lee Wai Mei, the Chief Financial Officer of the Company. Ms. Lo has confirmed that she has taken no less than 15 hours of relevant professional training during the year under review.

Corporate Governance Report (Continued)

SHAREHOLDERS' RIGHTS

Shareholders Convening an Extraordinary General Meeting

Pursuant to the Companies Ordinance (Chapter 622 of the Laws of Hong Kong), shareholders of the Company holding not less than 5% of the total voting rights of all the members having a right to vote at general meeting may request the Directors to call a general meeting of the Company. The request must state the general nature of the business to be dealt with at the meeting and may include the text of a resolution that may properly be moved and is intended to be moved at the meeting. The request may be sent to the Company in hard copy form or in electronic form; and must be authenticated by the person or persons making it. Directors of the Company must call a meeting with 21 days after the date on which they become subject to the requirement. The meeting being called must be held on a date not more than 28 days after the date of the notice convening the meeting. If the Directors fail to call the meeting, the shareholders who requested the meeting, or any of them representing more than one half of the total voting rights of all of them, may themselves call a general meeting. The meeting must be called for a date not more than 3 months after the date on which the Directors become subject to the requirement to call a meeting.

Details of the procedures for shareholders to propose a person for election as a Director of the Company are available on the Company's website.

Shareholders' Enquiries and Proposals

Shareholders may direct their enquiries about their shareholdings to the Company's Share Registrar, Tricor Tengis Limited.

Shareholders may also send written enquiries to the Company, for the attention of the Chief Financial Officer or the Company Secretary of the Company by mail or by fax. The contact details of the Company are set out in the "Contact Us" section of the Company's website at www.gdtann.com.hk. In addition, the Company is committed to maximizing the use of its website as a channel to provide updated information in a timely manner and to strengthen the communications with both the shareholders and the public. The Company has formulated the "Shareholders Communication Policy" which enables Shareholders to exercise their rights in an informed manner.

ENVIRONMENTAL PROTECTION AND LEGAL COMPLIANCE

The Group devotes to protect the environment where it operates. Also, it is committed to ensuring compliance of the environmental standards and the relevant laws and regulations that are applicable to its business operation from time to time. The Group has obtained the requisite permits and environmental approvals for its business and production facilities, and has complied with the relevant laws, rules and regulations. For further information on the work done by the Group in respect to environmental protection and legal compliance, please refer to the Management Discussion and Analysis on pages 6 to 9 in this annual report.

Corporate Governance Report (Continued)

RELATIONSHIPS WITH STAKEHOLDERS

The Company recognizes that our employees, customers and suppliers and business associates are key stakeholders to the Company's success. We strive to achieve corporate sustainability through engaging our employees, providing quality services to our customers, collaborating with business partners (including suppliers and contractors) to deliver quality sustainable products and services and supporting our community.

CONSTITUTIONAL DOCUMENTS

During the year under review, there are no changes in the Company's Articles of Association. An up-to-date consolidated version of the Company's Articles of Association is available on the Company's website.

By order of the Board
Sun Jun
Chairman and Managing Director

Hong Kong, 28 March 2019

Independent Auditor's Report

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To the members of **Guangdong Tannery Limited**
(Incorporated in Hong Kong with limited liability)

OPINION

We have audited the consolidated financial statements of Guangdong Tannery Limited (the "Company") and its subsidiaries (the "Group") set out on pages 39 to 112, which comprise the consolidated statement of financial position as at 31 December 2018, and the consolidated statement of profit or loss, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2018, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA") and have been properly prepared in compliance with the Hong Kong Companies Ordinance.

BASIS FOR OPINION

We conducted our audit in accordance with Hong Kong Standards on Auditing ("HKSAs") issued by the HKICPA. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Group in accordance with the HKICPA's *Code of Ethics for Professional Accountants* (the "Code"), and we have fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

KEY AUDIT MATTERS

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

Independent Auditor's Report (Continued)

KEY AUDIT MATTERS (CONTINUED)

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Key audit matter	How our audit addressed the key audit matter
Impairment assessment of plant and equipment	
In view of the operating loss of the Group for the year ended 31 December 2018, management performed an impairment assessment on the Group's cash-generating unit ("CGU") to which the plant and equipment belonged at the end of the reporting period. Based on the results of the impairment assessment, an impairment loss of approximately HK$12.4 million was recognised in the consolidated statement of profit or loss for the year ended 31 December 2018 and represented approximately 15.2% of the consolidated loss. The impairment assessment of the CGU was determined by a value in use approach using a discounted cash flow calculation. This assessment requires the use of significant judgment and assumptions by management to determine the key assumptions including sales growth rate, selling prices, operating expenses and discount rate applied in the discounted cash flows. Relevant disclosures are included in notes 3 and 11 to the consolidated financial statements.	In evaluating management's impairment assessment, our procedures included (i) evaluating the key assumptions used in the discounted cash flow forecast, including sales growth rate, selling prices and operating expenses, with reference to the latest operating performance and historical data; (ii) involving our valuation specialists in evaluating the valuation methodology and discount rate adopted by management by benchmarking comparable companies in similar industries; (iii) performing sensitivity analyses on key inputs in the discounted cash flows for any significant impact on the recoverable amount of the CGU; and (iv) assessing the adequacy of the disclosures of impairment assessment of plant and equipment in the consolidated financial statements.
Provision for inventories	
As at 31 December 2018, the Group's inventories, net of provision, amounted to approximately HK$134.1 million, and represented approximately 59.3% of consolidated current assets of the Group. Significant management judgement and estimates are involved in determining the net realisable values of inventories with reference to, amongst others, the ageing of inventories, historical sales performance, post year-end sales, latest selling prices and expectation of future saleability of the inventories. Relevant disclosures are included in notes 3 and 13 to the consolidated financial statements.	In evaluating management's assessment of provision for inventories, our audit procedures included (i) obtaining an understanding of the basis of inventory provision policy adopted by the Group; (ii) test checking the ageing of inventories balances and past sales/utilisation history; and (iii) evaluating the basis of inventories provision made by management by reviewing the net realisable value of selected samples with reference to the latest selling prices and the estimated costs to be incurred for completion and for sale.

Independent Auditor's Report (Continued)

OTHER INFORMATION INCLUDED IN THE ANNUAL REPORT

The directors of the Company are responsible for the other information. The other information comprises the information included in the Annual Report, other than the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

RESPONSIBILITIES OF THE DIRECTORS FOR THE CONSOLIDATED FINANCIAL STATEMENTS

The directors of the Company are responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with HKFRSs issued by the HKICPA and the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the directors of the Company are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors of the Company either intend to liquidate the Group or to cease operations or have no realistic alternative but to do so.

The directors of the Company are assisted by the Audit Committee in discharging their responsibilities for overseeing the Group's financial reporting process.

AUDITOR'S RESPONSIBILITIES FOR THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Our report is made solely to you, as a body, in accordance with section 405 of the Hong Kong Companies Ordinance, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

Independent Auditor's Report (Continued)

AUDITOR'S RESPONSIBILITIES FOR THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

As part of an audit in accordance with HKSAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.

- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

Independent Auditor's Report (Continued)

AUDITOR'S RESPONSIBILITIES FOR THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

From the matters communicated with the Audit Committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Fok Lai Ching.

Ernst & Young
Certified Public Accountants
Hong Kong

28 March 2019

Consolidated Statement of Profit or Loss

Year ended 31 December 2018

	Notes	2018 HK$'000	2017 HK$'000
REVENUE	5	**238,317**	322,146
Cost of sales		**(273,592)**	(369,583)
Gross loss		**(35,275)**	(47,437)
Other income and gains	5	**3,356**	5,894
Selling and distribution expenses		**(2,081)**	(2,131)
Administrative expenses		**(28,155)**	(28,015)
Impairment on items of plant and equipment	11	**(12,365)**	(21,794)
Other operating income/(expenses), net		**(542)**	1,409
Finance costs	6	**(5,973)**	(6,808)
LOSS BEFORE TAX	6	**(81,035)**	(98,882)
Income tax expense	7	**(206)**	(741)
LOSS FOR THE YEAR		**(81,241)**	(99,623)
LOSS PER SHARE	10		
— Basic		**HK(15.10) cents**	HK(18.52) cents
— Diluted		**HK(15.10) cents**	HK(18.52) cents

Consolidated Statement of Comprehensive Income

Year ended 31 December 2018

	Notes	2018 HK$'000	2017 HK$'000
LOSS FOR THE YEAR		**(81,241)**	(99,623)
OTHER COMPREHENSIVE INCOME/(LOSS)			
Other comprehensive income/(loss) that will not be reclassified to profit or loss in subsequent periods:			
Surplus/(deficits) on revaluation of buildings	*11*	**(219)**	4,185
Income tax effect	*21*	**55**	(1,046)
		(164)	3,139
Other comprehensive income/(loss) that may be reclassified to profit or loss in subsequent periods:			
Exchange differences on translation of foreign operations		**(10,774)**	22,364
OTHER COMPREHENSIVE INCOME/(LOSS) FOR THE YEAR, NET OF TAX		**(10,938)**	25,503
TOTAL COMPREHENSIVE LOSS FOR THE YEAR		**(92,179)**	(74,120)

Consolidated Statement of Financial Position

31 December 2018

	Notes	2018 HK$'000	2017 HK$'000
NON-CURRENT ASSETS			
Property, plant and equipment	*11*	**47,057**	65,887
Prepaid land lease payments	*12*	**11,459**	12,313
Total non-current assets		**58,516**	78,200
CURRENT ASSETS			
Inventories	*13*	**134,131**	218,900
Receivables, prepayments and deposits	*14*	**64,576**	93,641
Pledged bank balances	*15*	**—**	1,066
Cash and bank balances	*15*	**27,513**	29,108
Total current assets		**226,220**	342,715
CURRENT LIABILITIES			
Trade payables	*16*	**38,009**	49,551
Other payables and accruals	*17*	**36,531**	28,902
Tax payable		**113**	33
Loan from a fellow subsidiary	*18*	**—**	41,177
Due to a PRC joint venture partner	*19*	**1,131**	1,131
Provision	*20*	**3,640**	3,816
Total current liabilities		**79,424**	124,610
NET CURRENT ASSETS		**146,796**	218,105
TOTAL ASSETS LESS CURRENT LIABILITIES		**205,312**	296,305

Consolidated Statement of Financial Position (Continued)

31 December 2018

	Notes	2018 HK$'000	2017 HK$'000
NON-CURRENT LIABILITIES			
Loans from the immediate holding company	18	**142,379**	141,138
Deferred tax liabilities	21	**3,840**	3,895
Total non-current liabilities		**146,219**	145,033
Net assets		**59,093**	151,272
EQUITY			
Share capital	22	**75,032**	75,032
Other reserves	23	**(15,939)**	76,240
Total equity		**59,093**	151,272

Sun Jun
Director

Xiao Zhaoyi
Director

Consolidated Statement of Changes in Equity

Year ended 31 December 2018

	Note	Share capital HK$'000	Equity component of convertible notes HK$'000	General reserve fund HK$'000 (Note 23(i))	Reserve funds HK$'000 (Note 23(iii))	Capital reserve HK$'000 (Note 23(iv))	Exchange translation reserve HK$'000	Property revaluation reserve HK$'000	Special capital reserve HK$'000 (Note 23(ii))	Accumulated losses HK$'000	Total HK$'000
At 1 January 2017		75,032	5,545	167,746	20,054	3,639	55,267	7,216	—	(109,107)	225,392
Loss for the year		—	—	—	—	—	—	—	—	(99,623)	(99,623)
Other comprehensive income for the year:											
Changes in fair value of buildings, net of tax		—	—	—	—	—	—	3,139	—	—	3,139
Exchange differences on translation of foreign operations		—	—	—	—	—	22,364	—	—	—	22,364
Total comprehensive loss for the year		—	—	—	—	—	22,364	3,139	—	(99,623)	(74,120)
At 31 December 2017 and 1 January 2018		75,032	5,545*	167,746*	20,054*	3,639*	77,631*	10,355*	—*	(208,730)*	151,272
Loss for the year		—	—	—	—	—	—	—	—	(81,241)	(81,241)
Other comprehensive loss for the year:											
Changes in fair value of buildings, net of tax		—	—	—	—	—	—	(164)	—	—	(164)
Exchange differences on translation of foreign operations		—	—	—	—	—	(10,774)	—	—	—	(10,774)
Total comprehensive loss for the year		—	—	—	—	—	(10,774)	(164)	—	(81,241)	(92,179)
Transfer from accumulated losses in accordance with the undertaking	*23 (ii)*	—	—	—	—	—	—	—	70	(70)	—
At 31 December 2018		75,032	5,545*	167,746*	20,054*	3,639*	66,857*	10,191*	70*	(290,041)*	59,093

* These reserve accounts comprise the consolidated other reserves deficits of HK$15,939,000 (2017: consolidated other reserves of HK$76,240,000) in the consolidated statement of financial position.

Consolidated Statement of Cash Flows

Year ended 31 December 2018

	Notes	2018 HK$'000	2017 HK$'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Loss before tax		**(81,035)**	(98,882)
Adjustments for:			
Finance costs	6	**5,973**	6,808
Finance income	5	**(47)**	(68)
Depreciation	6	**5,849**	11,024
Provision for inventories	6	**987**	24,004
Impairment of trade receivables	6	**514**	1,616
Impairment on items of plant and equipment	11	**12,365**	21,794
Impairment of other receivables	6	**28**	76
Amortisation of prepaid land lease payments	6	**299**	291
Loss on disposal of items of property, plant and equipment	6	**—**	136
Write-off of items of property, plant and equipment	6	**—**	1,567
Reversal of accruals	6	**—**	(4,804)
		(55,067)	(36,438)
Decrease in inventories		**76,533**	31,758
Decrease in receivables, prepayments and deposits		**25,165**	44,114
Decrease in trade payables		**(9,634)**	(15,420)
Increase/(decrease) in other payables and accruals		**5,513**	(98)
Decrease in interest-bearing bank borrowings		**—**	(88,711)
Cash generated from/(used in) operations		**42,510**	(64,795)
Interest received		**47**	68
Interest paid		**(1,635)**	(2,961)
Overseas tax paid		**(121)**	(56)
Net cash flows from/(used in) operating activities		**40,801**	(67,744)
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of items of property, plant and equipment		**(1,430)**	(4,661)
Proceeds from disposal of items of property, plant and equipment		**—**	165
Decrease in pledged bank balances		**1,055**	10,953
Net cash flows from/(used in) investing activities		**(375)**	6,457

Consolidated Statement of Cash Flows (Continued)

Year ended 31 December 2018

	Notes	2018 HK$'000	2017 HK$'000
CASH FLOWS FROM FINANCING ACTIVITIES			
Drawdown of a loan from a fellow subsidiary		—	39,707
Repayment of a loan from a fellow subsidiary		**(40,764)**	—
Net cash flows from/(used in) financing activities		**(40,764)**	39,707
NET DECREASE IN CASH AND CASH EQUIVALENTS		**(338)**	(21,580)
Cash and cash equivalents at beginning of year		**29,108**	48,291
Effect of foreign exchange rate changes, net		**(1,257)**	2,397
CASH AND CASH EQUIVALENTS AT END OF YEAR		**27,513**	29,108
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS			
Cash and bank balances	15	**27,513**	29,108

Notes to Financial Statements

31 December 2018

1. CORPORATE AND GROUP INFORMATION

Guangdong Tannery Limited is a limited liability company incorporated in Hong Kong. The registered office of the Company is located at 29/F, Guangdong Investment Tower, 148 Connaught Road Central, Hong Kong.

During the year, the Group was principally engaged in the processing and sale of semi-finished and finished leather.

GDH Limited ("GDH"), a company incorporated in Hong Kong, is the immediate holding company of the Company. In the opinion of the directors, the ultimate holding company of the Company is 廣東粵海控股集團有限公司, which is established in the People's Republic of China (the "PRC" or "Mainland China").

Information about subsidiaries

Particulars of the Company's principal subsidiaries are as follows:

Name	Place of registration and business	Registered share capital	Percentage of equity attributable to the Company Direct (%)	Principal activities
徐州港威皮革有限公司 (Xuzhou Gangwei Leather Co., Ltd.) +*	PRC/Mainland China	RMB18,000,000	100	Lease of plant and machinery
徐州南海皮廠有限公司 (Xuzhou Nanhai Leather Factory Co., Ltd.) +*	PRC/Mainland China	US$10,450,000	100	Processing of cowhides and leather trading
粵海制革(徐州)有限公司 (Guangdong Tannery (Xuzhou) Limited) +*	PRC/Mainland China	US$9,000,000	100	Lease of plant and machinery

+ Registered as wholly-foreign-owned enterprises under PRC law.

* Subsidiaries of which the financial statements were not audited by Ernst & Young, Hong Kong or another member firm of the Ernst & Young global network.

The above table lists the subsidiaries of the Company which, in the opinion of the directors, principally affected the results for the year and formed a substantial portion of the net assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

Notes to Financial Statements (Continued)

31 December 2018

2.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") (which include all Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), accounting principles generally accepted in Hong Kong and the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for buildings classified as property, plant and equipment and bills receivable which have been measured at fair value as further explained in note 2.4 to the financial statements. These financial statements are presented in Hong Kong dollars ("HK$") and all values are rounded to the nearest thousand (HK$'000) except when otherwise indicated.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries (collectively referred to as the "Group") for the year ended 31 December 2018. A subsidiary is an entity (including a structured entity), directly or indirectly, controlled by the Company. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee (i.e., existing rights that give the Group the current ability to direct the relevant activities of the investee).

When the Company has, directly or indirectly, less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

(a) the contractual arrangement with the other vote holders of the investee;

(b) rights arising from other contractual arrangements; and

(c) the Group's voting rights and potential voting rights.

The financial statements of the subsidiaries are prepared for the same reporting period as the Company, using consistent accounting policies. The results of subsidiaries are consolidated from the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases.

Profit or loss and each component of other comprehensive income are attributed to the owners of the parent of the Group and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

The Group reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control described above. A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction.

Notes to Financial Statements (Continued)

31 December 2018

2.1 BASIS OF PREPARATION (CONTINUED)

Basis of consolidation (Continued)

If the Group loses control over a subsidiary, it derecognises (i) the assets (including goodwill) and liabilities of the subsidiary, (ii) the carrying amount of any non-controlling interest and (iii) the cumulative translation differences recorded in equity; and recognises (i) the fair value of the consideration received, (ii) the fair value of any investment retained and (iii) any resulting surplus or deficit in profit or loss. The Group's share of components previously recognised in other comprehensive income is reclassified to profit or loss or retained profits, as appropriate, on the same basis as would be required if the Group had directly disposed of the related assets or liabilities.

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES

The Group has adopted the following new and revised HKFRSs for the first time for the current year's financial statements.

Amendments to HKFRS 2	*Classification and Measurement of Share-based Payment Transactions*
Amendments to HKFRS 4	*Applying HKFRS 9 Financial Instruments with HKFRS 4 Insurance Contracts*
HKFRS 9	*Financial Instruments*
HKFRS 15	*Revenue from Contracts with Customers*
Amendments to HKFRS 15	*Clarifications to HKFRS 15 Revenue from Contracts with Customers*
Amendments to HKAS 40	*Transfers of Investment Property*
HK(IFRIC)-Int 22	*Foreign Currency Transactions and Advance Consideration*
Annual Improvements 2014–2016 Cycle	Amendments to HKFRS 1 and HKAS 28

Other than as explained below regarding the impact of HKFRS 9 and HKFRS 15, the adoption of the above new and revised standards has had no significant financial effects on these financial statements.

The nature and the impact of the new and revised HKFRSs are described below:

(a) HKFRS 9 *Financial Instruments* replaces HKAS 39 *Financial Instruments: Recognition and Measurement* for annual periods beginning on or after 1 January 2018, bringing together two aspects of the accounting for financial instruments: classification and measurement, and impairment.

The Group has recognised the transition adjustments against the applicable opening balances in equity at 1 January 2018. Therefore, the comparative information was not restated and continues to be reported under HKAS 39.

Classification and measurement

The following information sets out the impacts of adopting HKFRS 9 on the statement of financial position, including the effect of replacing HKAS 39's incurred credit loss calculations with HKFRS 9's expected credit losses ("ECLs").

Notes to Financial Statements (Continued)

31 December 2018

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES (CONTINUED)

(a) (Continued)

Classification and measurement (Continued)

A reconciliation between the carrying amounts under HKAS 39 and the balances reported under HKFRS 9 as at 1 January 2018 is as follows:

		HKAS 39 measurement			HKFRS 9 measurement	
		Category	Amount	Reclassification	Amount	Category
	Note		*HK$'000*	*HK$'000*	*HK$'000*	
Financial assets						
Trade receivables		L&R[1]	37,313	—	37,313	AC[2]
Bills receivable	*(i)*	L&R[1]	53,223	(53,223)	—	AC[2]
	(i)		—	53,223	53,223	FVOCI[3]
Financial assets included in prepayments, other receivables and deposits		L&R[1]	1,742	—	1,742	AC[2]
Pledged bank balances		L&R[1]	1,066	—	1,066	AC[2]
Cash and bank balances		L&R[1]	29,108	—	29,108	AC[2]
			122,452	—	122,452	
Financial liabilities						
Trade payables		AC[2]	49,551	—	49,551	AC[2]
Financial liabilities included in other payables and accruals		AC[2]	22,646	—	22,646	AC[2]
Due to a PRC joint venture partner		AC[2]	1,131	—	1,131	AC[2]
Loan from the immediate holding company		AC[2]	141,138	—	141,138	AC[2]
Loan from a fellow subsidiary		AC[2]	41,177	—	41,177	AC[2]
			255,643	—	255,643	

1 L&R: Loans and receivables
2 AC: Financial assets or financial liabilities at amortised cost
3 FVOCI: Financial assets at fair value through other comprehensive income

Note:

(i) The objective of the Group of holding the bills receivable is to collect contractual cash flows and to sell before its contractual maturity for working capital management. The Group considered these receivables are managed within a business model to collect contractual cash flows and to sell the financial assets. Accordingly, the Group has reclassified its bills receivable from loans and receivables at amortised cost to financial assets at fair value through other comprehensive income.

Notes to Financial Statements (Continued)

31 December 2018

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES (CONTINUED)

(a) (Continued)

Impairment

There was no significant impact on the financial statements upon transition from the aggregate opening impairment allowances under HKAS 39 to ECL allowances under HKFRS 9 for the financial assets of the Group as at 1 January 2018.

(b) HKFRS 15 and its amendments replace HKAS 11 *Construction Contracts*, HKAS 18 *Revenue* and related interpretations and it applies, with limited exceptions, to all revenue arising from contracts with customers. HKFRS 15 establishes a new five-step model to account for revenue arising from contracts with customers. Under HKFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The principles in HKFRS 15 provide a more structured approach for measuring and recognising revenue. The standard also introduces extensive qualitative and quantitative disclosure requirements, including disaggregation of total revenue, information about performance obligations, changes in contract asset and liability account balances between periods and key judgements and estimates. The disclosures are included in notes 3 and 5 to the financial statements. As a result of the application of HKFRS 15, the Group has changed the accounting policy with respect to revenue recognition in note 2.4 to the financial statements.

The Group has adopted HKFRS 15 using the modified retrospective method of adoption. Under this method, the standard can be applied either to all contracts at the date of initial application or only to contracts that are not completed at this date. The Group has elected to apply the standard to contracts that are not completed as at 1 January 2018. Initial application of HKFRS 15 has no cumulative effect on the timing and measurement of revenue recognition for the sale of processing leather as at 1 January 2018.

The nature of the adjustments as at 1 January 2018 and the reasons for the significant changes in the statement of financial position as at 31 December 2018 are described below:

Presentation of contract assets and liabilities

Under HKFRS 15, a receivable is recognised only if the Group has an unconditional right to consideration. If the Group recognises the related revenue before being unconditionally entitled to the consideration for the promised goods and services in the contract, then the entitlement to consideration is classified as a contract asset. Similarly, a contract liability, rather than a payable, is recognised when a customer pays consideration, or is contractually required to pay consideration and the amount is already due, before the Group recognises the related revenue. For a single contract with the customer, either a net contract asset or a net contract liability is presented. For multiple contracts, contract assets and contract liabilities of unrelated contracts are not presented on a net basis.

Notes to Financial Statements (Continued)

31 December 2018

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES (CONTINUED)

(b) (Continued)

Presentation of contract assets and liabilities (Continued)

(i) Consideration received from customers in advance

Before the adoption of HKFRS 15, the Group recognised consideration received from customers in advance as receipts in advance included in other payables and accruals. Under HKFRS 15, the amount is classified as contract liabilities which is included in other payables and accruals.

Upon adoption of HKFRS 15, the Group reclassified HK$1,308,000 from receipts in advance to contract liabilities which is included in other payables and accruals as at 1 January 2018 in relation to the consideration received from customers in advance as at 1 January 2018.

As at 31 December 2018, under HKFRS 15, HK$4,120,000 was reclassified from receipts in advance to contract liabilities included in other payables and accruals in relation to the consideration received from customers in advance.

2.3 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS

The Group has not applied the following new and revised HKFRSs, that have been issued but are not yet effective, in these financial statements.

Amendments to HKFRS 3	*Definition of a Business*[2]
Amendments to HKFRS 9	*Prepayment Features with Negative Compensation*[1]
Amendments to HKFRS 10 and HKAS 28 (2011)	*Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*[4]
HKFRS 16	*Leases*[1]
HKFRS 17	*Insurance Contracts*[3]
Amendments to HKAS 1 and HKAS 8	*Definition of Material*[2]
Amendments to HKAS 19	*Plan Amendment, Curtailment or Settlement*[1]
Amendments to HKAS 28	*Long-term Interests in Associates and Joint Ventures*[1]
HK(IFRIC)-Int 23	*Uncertainty over Income Tax Treatments*[1]
Annual Improvements 2015–2017 Cycle	Amendments to HKFRS 3, HKFRS 11, HKAS 12 and HKAS 23[1]

1 Effective for annual periods beginning on or after 1 January 2019
2 Effective for annual periods beginning on or after 1 January 2020
3 Effective for annual periods beginning on or after 1 January 2021
4 No mandatory effective date yet determined but available for adoption

Notes to Financial Statements (Continued)

31 December 2018

2.3 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS (CONTINUED)

Further information about those HKFRSs that are expected to be applicable to the Group is described below.

HKFRS 16 replaces HKAS 17 *Leases*, HK(IFRIC)-Int 4 *Determining whether an Arrangement contains a Lease*, HK(SIC)-Int 15 *Operating Leases — Incentives* and HK(SIC)-Int 27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*. The standard sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to recognise assets and liabilities for most leases. The standard includes two elective recognition exemptions for lessees — leases of low-value assets and short-term leases. At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). The right-of-use asset is subsequently measured at cost less accumulated depreciation and any impairment losses unless the right-of-use asset meets the definition of investment property in HKAS 40, or relates to a class of property, plant and equipment to which the revaluation model is applied. The lease liability is subsequently increased to reflect the interest on the lease liability and reduced for the lease payments. Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset. Lessees will also be required to remeasure the lease liability upon the occurrence of certain events, such as change in the lease term and change in future lease payments resulting from a change in an index or rate used to determine those payments. Lessees will generally recognise the amount of the remeasurement of the lease liability as an adjustment to the right-of-use asset. Lessor accounting under HKFRS 16 is substantially unchanged from the accounting under HKAS 17. Lessors will continue to classify all leases using the same classification principle as in HKAS 17 and distinguish between operating leases and finance leases. HKFRS 16 requires lessees and lessors to make more extensive disclosures than under HKAS 17. Lessees can choose to apply the standard using either a full retrospective or a modified retrospective approach. The Group will adopt HKFRS 16 from 1 January 2019. The Group plans to adopt the transitional provisions in HKFRS 16 to recognise the cumulative effect of initial adoption as an adjustment to the opening balance of retained earnings at 1 January 2019 and will not restate the comparatives. In addition, the Group plans to apply the new requirements to contracts that were previously identified as leases applying HKAS 17 and measure the lease liability at the present value of the remaining lease payments, discounted using the Group's incremental borrowing rate at the date of initial application. The right-of-use asset will be measured at the amount of the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to the lease recognised in the statement of financial position immediately before the date of initial application. The Group has assessed that HKFRS 16 is not likely to have significant impact on the financial statements.

Except for the above, the Group is in the process of making an assessment of the impact of these new and revised HKFRSs upon initial application. The Group is not yet in a position to state whether they would have a significant impact on the Group's results of operation and financial position.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Fair value measurement

The Group measures its buildings and bills receivable at fair value at the end of each reporting period. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either in the principal market for the asset or liability, or in the absence of a principal market, in the most advantageous market for the asset or liability. The principal or the most advantageous market must be accessible by the Group. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

Level 1 — based on quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2 — based on valuation techniques for which the lowest level input that is significant to the fair value measurement is observable, either directly or indirectly

Level 3 — based on valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by reassessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Impairment of non-financial assets

Where an indication of impairment exists, or when annual impairment testing for an asset is required (other than inventories, financial assets, and non-current assets), the asset's recoverable amount is estimated. An asset's recoverable amount is the higher of the asset's or cash-generating unit's value in use and its fair value less costs of disposal, and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is charged to the statement of profit or loss in the period in which it arises, unless the asset is carried at a revalued amount, in which case the impairment loss is accounted with the relevant accounting policy for that revalued amount in those expense categories consistent with function of the impaired asset.

An assessment is made at the end of each reporting period as to whether there is an indication that previously recognised impairment losses may no longer exist or may have decreased. If such an indication exists, the recoverable amount is estimated. A previously recognised impairment loss of an asset other than goodwill is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, but not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation) had no impairment loss been recognised for the asset in prior years. A reversal of such an impairment loss is credited to the statement of profit or loss in the period in which it arises, unless the asset is carried at a revalued amount, in which case the reversal of the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

Related parties

A party is considered to be related to the Group if:

(a) the party is a person or a close member of that person's family and that person:

  (i) has control or joint control over the Group;

  (ii) has significant influence over the Group; or

  (iii) is a member of the key management personnel of the Group or of a parent of the Group;

or

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Related parties (Continued)

(b) the party is an entity where any of the following conditions applies:

(i) the entity and the Group are members of the same group;

(ii) one entity is an associate or joint venture of the other entity (or of a parent, subsidiary or fellow subsidiary of the other entity);

(iii) the entity and the Group are joint ventures of the same third party;

(iv) one entity is a joint venture of a third entity and the other entity is an associate of the third entity;

(v) the entity is a post-employment benefit plan for the benefit of employees of either the Group or an entity related to the Group;

(vi) the entity is controlled or jointly controlled by a person identified in (a);

(vii) a person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity); and

(viii) the entity, or any member of a group of which it is a part, provides key management personnel services to the Group or to the parent of the Group.

Property, plant and equipment and depreciation

Plant and equipment, other than construction in progress and buildings, are stated at cost less accumulated depreciation and any impairment losses. The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the statement of profit or loss in the period in which it is incurred. In situations where the recognition criteria are satisfied, the expenditure for a major inspection is capitalised in the carrying amount of the asset as a replacement. Where significant parts of property, plant and equipment are required to be replaced at intervals, the Group recognises such parts as individual assets with specific useful lives and depreciates them accordingly.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Property, plant and equipment and depreciation (Continued)

Buildings are stated at valuation. Valuations are performed frequently enough to ensure that the fair value of a revalued asset does not differ materially from its carrying amount. Changes in the values of property, plant and equipment are dealt with as movements in the property revaluation reserve. If the total of this reserve is insufficient to cover a deficit, on an individual asset basis, the excess of the deficit is charged to the statement of profit or loss. Any subsequent revaluation surplus is credited to the statement of profit or loss to the extent of the deficit previously charged. An annual transfer from the property revaluation reserve to retained profits is made for the difference between the depreciation based on the revalued carrying amount of an asset and the depreciation based on the asset's original cost. On disposal of a revalued asset, the relevant portion of the property revaluation reserve realised in respect of previous valuations is transferred to retained profits as a movement in reserves.

Depreciation is calculated on the straight-line basis to write off the cost or valuation of each item of property, plant and equipment to its residual value over its estimated useful life. The principal annual rates used for this purpose are as follows:

Buildings	2% to 10%
Leasehold improvements	4% to 20%
Plant and machinery	10% to 12.5%
Electronic equipment	20%
Furniture, fixtures and equipment	15% to 20%
Motor vehicles	15% to 20%

Where parts of an item of property, plant and equipment have different useful lives, the cost or valuation of that item is allocated on a reasonable basis among the parts and each part is depreciated separately. Residual values, useful lives and the depreciation method are reviewed, and adjusted if appropriate, at least at each financial year end.

An item of property, plant and equipment including any significant part initially recognised is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss on disposal or retirement recognised in the statement of profit or loss in the year the asset is derecognised is the difference between the net sales proceeds and the carrying amount of the relevant asset.

Construction in progress represents machinery and equipment under construction. It is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction during the period of construction. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Operating leases

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Group is the lessee, rentals payable under operating leases net of incentives received from the lessor are charged to the statement of profit or loss on the straight-line basis over the lease terms.

Prepaid land lease payments under operating leases are initially stated at cost and subsequently recognised on the straight-line basis over the lease terms.

Investments and other financial assets (policies under HKFRS 9 applicable from 1 January 2018)

Initial recognition and measurement

Financial assets of the Group are classified, at initial recognition, as and subsequently measured at amortised cost and fair value through other comprehensive income.

The classification of financial assets at initial recognition depends on the financial asset's contractual cash flow characteristics and the Group's business model for managing them. With the exception of trade receivables that do not contain a significant financing component or for which the Group has applied the practical expedient of not adjusting the effect of a significant financing component, the Group initially measures a financial asset at its fair value, plus in the case of a financial asset not at fair value through profit or loss, transaction costs. Trade receivables that do not contain a significant financing component or for which the Group has applied the practical expedient are measured at the transaction price determined under HKFRS 15 in accordance with the policies set out for "Revenue recognition (applicable from 1 January 2018)" below.

In order for a financial asset to be classified and measured at amortised cost or fair value through other comprehensive income, it needs to give rise to cash flows that are solely payments of principal and interest ("SPPI") on the principal amount outstanding.

The Group's business model for managing financial assets refers to how it manages its financial assets in order to generate cash flows. The business model determines whether cash flows will result from collecting contractual cash flows, selling the financial assets, or both.

All regular way purchases and sales of financial assets are recognised on the trade date, that is, the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Investments and other financial assets (policies under HKFRS 9 applicable from 1 January 2018) (Continued)

Subsequent measurement

The subsequent measurement of financial assets depends on their classification as follows:

Financial assets at amortised cost (debt instruments)

The Group measures financial assets at amortised cost if both of the following conditions are met:

- The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows.

- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

The Group's financial assets measured at amortised cost include trade receivables, other receivables and deposits, pledged bank balances and cash and bank balances.

Financial assets at amortised cost are subsequently measured using the effective interest method and are subject to impairment. Gains and losses are recognised in the statement of profit or loss when the asset is derecognised, modified or impaired.

Financial assets at fair value through other comprehensive income (debt instruments)

The Group measures debt investments at fair value through other comprehensive income if both of the following conditions are met:

- The financial asset is held within a business model with the objective of both holding to collect contractual cash flows and selling.

- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

The Group's financial assets measured at fair value through other comprehensive income includes bills receivable.

For debt investments at fair value through other comprehensive income, finance income, foreign exchange revaluation and impairment losses or reversals are recognised in the statement of profit or loss and computed in the same manner as for financial assets measured at amortised cost. The remaining fair value changes are recognised in other comprehensive income. Upon derecognition, the cumulative fair value change recognised in other comprehensive income is recycled to the statement of profit or loss.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Investments and other financial assets (policies under HKAS 39 applicable before 1 January 2018)

Initial recognition and measurement

Financial assets are classified, at initial recognition, as loans and receivables. When financial assets are recognised initially, they are measured at fair value plus transaction costs that are attributable to the acquisition of the financial assets.

The Group's financial assets include trade and bills receivables, deposits and other receivables, pledged bank balances and cash and bank balances.

All regular way purchases and sales of financial assets are recognised on the trade date, that is, the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Subsequent measurement

The subsequent measurement of loans and receivables is as follows:

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, such assets are subsequently measured at amortised cost using the effective interest rate method less any allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and includes fees or costs that are an integral part of the effective interest rate. The effective interest rate amortisation is included in other income and gains in the statement of profit or loss. The loss arising from impairment is recognised in the statement of profit or loss in finance costs for loans and in other operating expenses for receivables.

Derecognition of financial assets (policies under HKFRS 9 applicable from 1 January 2018 and policies under HKAS 39 applicable before 1 January 2018)

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is primarily derecognised (i.e., removed from the Group's consolidated statement of financial position) when:

- the rights to receive cash flows from the asset have expired; or
- the Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a "pass-through" arrangement; and either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Derecognition of financial assets (policies under HKFRS 9 applicable from 1 January 2018 and policies under HKAS 39 applicable before 1 January 2018) (Continued)

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, it evaluates if, and to what extent, it has retained the risk and rewards of ownership of the asset. When it has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the Group continues to recognise the transferred asset to the extent of the Group's continuing involvement. In that case, the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Impairment of financial assets (policies under HKFRS 9 applicable from 1 January 2018)

The Group recognises an allowance for ECLs for all debt instruments not held at fair value through profit or loss. ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Group expects to receive, discounted at an approximation of the original effective interest rate. The expected cash flows will include cash flows from the sale of collateral held or other credit enhancements that are integral to the contractual terms.

General approach

ECLs are recognised in two stages. For credit exposures for which there has not been a significant increase in credit risk since initial recognition, ECLs are provided for credit losses that result from default events that are possible within the next 12 months (a 12-month ECLs). For those credit exposures for which there has been a significant increase in credit risk since initial recognition, a loss allowance is required for credit losses expected over the remaining life of the exposure, irrespective of the timing of the default (a lifetime ECLs).

At each reporting date, the Group assesses whether the credit risk on a financial instrument has increased significantly since initial recognition. When making the assessment, the Group compares the risk of a default occurring on the financial instrument as at the reporting date with the risk of a default occurring on the financial instrument as at the date of initial recognition and considers reasonable and supportable information that is available without undue cost or effort, including historical and forward-looking information.

For debt investments at fair value through other comprehensive income, the Group applies the low credit risk simplification. At each reporting date, the Group evaluates whether the debt investments are considered to have low credit risk using all reasonable and supportable information that is available without undue cost or effort. In making that evaluation, the Group reassesses the external credit ratings of the debt investments. In addition, the Group considers that there has been a significant increase in credit risk when contractual payments are more than 30 days past due.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Impairment of financial assets (policies under HKFRS 9 applicable from 1 January 2018) (Continued)

General approach (Continued)

The Group considers a financial asset other than trade and bills receivables in default when contractual payments are 90 days past due. However, in certain cases, the Group may also consider a financial asset to be in default when internal or external information indicates that the Group is unlikely to receive the outstanding contractual amounts in full before taking into account any credit enhancements held by the Group. A financial asset is written off when there is no reasonable expectation of recovering the contractual cash flows.

Debt investments at fair value through other comprehensive income and financial assets at amortised cost are subject to impairment under the general approach and they are classified within the following stages for measurement of ECLs except for trade receivables which apply the simplified approach as detailed below.

Stage 1 — Financial instruments for which credit risk has not increased significantly since initial recognition and for which the loss allowance is measured at an amount equal to 12-month ECLs

Stage 2 — Financial instruments for which credit risk has increased significantly since initial recognition but that are not credit-impaired financial assets and for which the loss allowance is measured at an amount equal to lifetime ECLs

Stage 3 — Financial assets that are credit-impaired at the reporting date (but that are not purchased or originated credit-impaired) and for which the loss allowance is measured at an amount equal to lifetime ECLs

Simplified approach

For trade receivables that do not contain a significant financing component or when the Group applies the practical expedient of not adjusting the effect of a significant financing component, the Group applies the simplified approach in calculating ECLs. Under the simplified approach, the Group does not track changes in credit risk, but instead recognises a loss allowance based on lifetime ECLs at each reporting date. The Group has established a provision matrix that is based on its historical credit loss experience, adjusted for forward-looking factors specific to the debtors and the economic environment.

For trade receivables that contain a significant financing component and lease receivables, the Group chooses as its accounting policy to adopt the simplified approach in calculating ECLs with policies as described above.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Impairment of financial assets (policies under HKAS 39 applicable before 1 January 2018)

The Group assesses at the end of each reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired. An impairment exists if one or more events that occurred after the initial recognition of the asset have an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that a debtor or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and observable data indicating that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Financial assets carried at amortised cost

For financial assets carried at amortised cost, the Group first assesses whether impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

The amount of any impairment loss identified is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not yet been incurred). The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition).

The carrying amount of the asset is reduced through the use of an allowance account and the loss is recognised in the statement of profit or loss. Finance income continues to be accrued on the reduced carrying amount using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. Loans and receivables together with any associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Group.

If, in a subsequent period, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a write-off is later recovered, the recovery is credited to other operating income in the statement of profit or loss.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Financial liabilities (policies under HKFRS 9 applicable from 1 January 2018 and HKAS 39 applicable before 1 January 2018)

Initial recognition and measurement

Financial liabilities are classified, at initial recognition, as loans and borrowings, or payables, as appropriate.

All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings and payables, net of directly attributable transaction costs.

The Group's financial liabilities include trade and other payables, accruals, an amount due to a PRC joint venture partner, loans from the immediate holding company and a loan from a fellow subsidiary.

Subsequent measurement

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost, using the effective interest rate method unless the effect of discounting would be immaterial, in which case they are stated at cost. Gains and losses are recognised in the statement of profit or loss when the liabilities are derecognised as well as through the effective interest rate amortisation process.

Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the effective interest rate. The effective interest rate amortisation is included in finance costs in the statement of profit or loss.

Derecognition of financial liabilities (policies under HKFRS 9 applicable from 1 January 2018 and HKAS 39 applicable before 1 January 2018)

A financial liability is derecognised when the obligation under the liability is discharged or cancelled, or expires.

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and a recognition of a new liability, and the difference between the respective carrying amounts is recognised in the statement of profit or loss.

Offsetting of financial instruments (policies under HKFRS 9 applicable from 1 January 2018 and HKAS 39 applicable before 1 January 2018)

Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position if there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liabilities simultaneously.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on the weighted average basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour and an appropriate proportion of overheads. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

Cash and cash equivalents

For the purpose of the consolidated statement of cash flows, cash and cash equivalents comprise cash on hand and demand deposits, and short term highly liquid investments that are readily convertible into known amounts of cash, are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired, less bank overdrafts which are repayable on demand and form an integral part of the Group's cash management.

For the purpose of the consolidated statement of financial position, cash and cash equivalents comprise cash on hand and at banks, and assets similar in nature to cash, which are not restricted as to use.

Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the end of the reporting period of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in the statement of profit or loss.

Provisions for staff redundancy payments and compensation to a PRC joint venture partner for early termination of a joint venture agreement are determined based on the relevant employment contracts and the terms of the joint venture agreement.

Income tax

Income tax comprises current and deferred tax. Income tax relating to items recognised outside the profit or loss is recognised outside profit or loss, either in other comprehensive income or directly in equity.

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period, taking into consideration interpretations and practices prevailing in the countries in which the Group operates.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Income tax (Continued)

Deferred tax is provided, using the liability method, on all temporary differences at the end of the reporting period between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences, except:

- when the deferred tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of taxable temporary differences associated with interests in subsidiaries, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, the carryforward of unused tax credits and any unused tax losses. Deferred tax assets are recognised to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, the carryforward of unused tax credits and unused tax losses can be utilised, except:

- when the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of deductible temporary differences associated with interests in subsidiaries, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at the end of each reporting period and are recognised to the extent that it has become probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Income tax (Continued)

Deferred tax assets and deferred tax liabilities are offset if and only if the Group has a legally enforceable right to set off current tax assets and current tax liabilities and the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities which intend either to settle current tax liabilities and assets on a net basis, or to realise the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

Government grants

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income on a systematic basis over the periods that the costs, which it is intended to compensate, are expensed.

Where the grant relates to an asset, the fair value is deducted from the carrying amount of the asset and released to the statement of profit or loss by way of a reduced depreciation charge.

Revenue recognition (applicable from 1 January 2018)

Revenue from contracts with customers

Revenue from contracts with customers is recognised when control of goods or services is transferred to the customers at an amount that reflects the consideration to which the Group expects to be entitled in exchange for those goods or services.

When the consideration in a contract includes a variable amount, the amount of consideration is estimated to which the Group will be entitled in exchange for transferring the goods or services to the customer. The variable consideration is estimated at contract inception and constrained until it is highly probable that a significant revenue reversal in the amount of cumulative revenue recognised will not occur when the associated uncertainty with the variable consideration is subsequently resolved.

When the contract contains a financing component which provides the customer a significant benefit of financing the transfer of goods or services to the customer for more than one year, revenue is measured at the present value of the amount receivable, discounted using the discount rate that would be reflected in a separate financing transaction between the Group and the customer at contract inception. When the contract contains a financing component which provides the Group a significant financial benefit for more than one year, revenue recognised under the contract includes the interest expense accreted on the contract liability under the effective interest method. For a contract where the period between the payment by the customer and the transfer of the promised goods or services is one year or less, the transaction price is not adjusted for the effects of a significant financing component, using the practical expedient in HKFRS 15.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Revenue recognition (applicable from 1 January 2018) (Continued)

Revenue from contracts with customers (Continued)

Sale of goods

Revenue from the sale of goods is recognised at the point in time when control of the asset is transferred to the customer, generally on delivery of the goods.

Other income

Finance income is recognised on an accrual basis using the effective interest method by applying the rate that exactly discounts the estimated future cash receipts over the expected life of the financial instrument or a shorter period, when appropriate, to the net carrying amount of the financial asset.

Revenue recognition (applicable before 1 January 2018)

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

(a) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold; and

(b) finance income, on an accrual basis using the effective interest method by applying the rate that exactly discounts the estimated future cash receipts over the expected life of the financial instrument or a shorter period, when appropriate, to the net carrying amount of the financial asset.

Contract liabilities (applicable from 1 January 2018)

A contract liability is the obligation to transfer goods or services to a customer for which the Group has received a consideration (or an amount of consideration that is due) from the customer. If a customer pays the consideration before the Group transfers goods or services to the customer, a contract liability is recognised when the payment is made or the payment is due (whichever is earlier). Contract liabilities are recognised as revenue when the Group performs under the contract.

Share-based payments

The Company operates a share option scheme for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. Employees (including directors) of the Group receive remuneration in the form of share-based payments, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Share-based payments (Continued)

The cost of equity-settled transactions with employees for grants after 7 November 2002 is measured by reference to the fair value at the date at which they are granted. The fair value is determined by an external valuer using a binomial model, further details of which are given in note 24 to the financial statements.

The cost of equity-settled transactions is recognised in employee benefit expense, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled. The cumulative expense recognised for equity-settled transactions at the end of each reporting period until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The charge or credit to the statement of profit or loss for a period represents the movement in the cumulative expense recognised as at the beginning and end of that period.

Service and non-market performance conditions are not taken into account when determining the grant date fair value of awards, but the likelihood of the conditions being met is assessed as part of the Group's best estimate of the number of equity instruments that will ultimately vest. Market performance conditions are reflected within the grant date fair value. Any other conditions attached to an award, but without an associated service requirement, are considered to be non-vesting conditions. Non-vesting conditions are reflected in the fair value of an award and lead to an immediate expensing of an award unless there are also service and/or performance conditions.

For awards that do not ultimately vest because non-market performance and/or service conditions have not been met, no expense is recognised. Where awards include a market or non-vesting condition, the transactions are treated as vesting irrespective of whether the market or non-vesting condition is satisfied, provided that all other performance and/or service conditions are satisfied.

Where the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified, if the original terms of the award are met. In addition, an expense is recognised for any modification that increases the total fair value of the share-based payments, or is otherwise beneficial to the employee as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. This includes any award where non-vesting conditions within the control of either the Group or the employee are not met. However, if a new award is substituted for the cancelled award, and is designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of earnings/loss per share.

Notes to Financial Statements (Continued)

31 December 2018

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Other employee benefits

Pension schemes

The Group operates a defined contribution Mandatory Provident Fund retirement benefit scheme (the "MPF Scheme") under the Mandatory Provident Fund Schemes Ordinance for those employees who are eligible to participate in the MPF Scheme. Contributions are made based on a percentage of the employees' basic salaries and are charged to the statement of profit or loss as they become payable in accordance with the rules of the MPF Scheme. The assets of the MPF Scheme are held separately from those of the Group in an independently administered fund. The Group's employer contributions vest fully with the employees when contributed into the MPF Scheme, except for the Group's employer voluntary contributions, which are proportionally refunded to the Group upon employee's termination of services in accordance with the vesting scales of the MPF Scheme.

The employees of the Group's subsidiaries which operate in Mainland China are required to participate in a central pension scheme (the "PRC Scheme") operated by the local municipal government. These subsidiaries are required to contribute a certain percentage of their payroll costs to the PRC Scheme. The contributions are charged to the statement of profit or loss as they become payable in accordance with the rules of the PRC Scheme.

Borrowing costs

Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds. Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e., assets that necessarily take a substantial period of time to get ready for their intended use or sale, are capitalised as part of the cost of those assets. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs capitalised. All other borrowing costs are expensed in the period in which they are incurred.

Foreign currencies

These financial statements are presented in Hong Kong dollars, which is the Company's functional and presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Foreign currency transactions recorded by the entities in the Group are initially recorded using their respective functional currency rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rates of exchange ruling at the end of the reporting period. Differences arising on settlement or translation of monetary items are recognised in the statement of profit or loss.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Foreign currencies (Continued)

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was measured. The gain or loss arising on translation of a non-monetary item measured at fair value is treated in line with the recognition of the gain or loss on change in fair value of the item (i.e., translation difference on the item whose fair value gain or loss is recognised in other comprehensive income or profit or loss is also recognised in other comprehensive income or profit or loss, respectively).

In determining the exchange rate on initial recognition of the related asset, expense or income on the derecognition of a non-monetary asset or non-monetary liability relating to an advance consideration, the date of initial transaction is the date on which the Group initially recognises the non-monetary asset or non-monetary liability arising from the advance consideration. If there are multiple payments or receipts in advance, the Group determines the transaction date for each payment or receipt of the advance consideration.

The functional currencies of certain overseas subsidiaries are currencies other than the Hong Kong dollar. As at the end of each reporting period, the assets and liabilities of these entities are translated into the Hong Kong dollars at the exchange rates prevailing at the end of each reporting period and their statements of profit or loss are translated into Hong Kong dollars at the weighted average exchange rates for the year.

The resulting exchange differences are recognised in other comprehensive income and accumulated in the exchange translation reserve. On disposal of a foreign operation, the component of other comprehensive income relating to that particular foreign operation is recognised in the statement of profit or loss.

For the purpose of the consolidated statement of cash flows, the cash flows of overseas subsidiaries are translated into Hong Kong dollars at the exchange rates ruling at the dates of the cash flows. Frequently recurring cash flows of overseas subsidiaries which arise throughout the year are translated into Hong Kong dollars at the weighted average exchange rates for the year.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

The preparation of the Group's financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and their accompanying disclosures, and the disclosure of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that could require a material adjustment to the carrying amounts of the assets or liabilities affected in the future.

Estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below.

Notes to Financial Statements (Continued)

31 December 2018

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (CONTINUED)

Estimation uncertainty (Continued)

Provision for inventories

Management reviews the condition of inventories of the Group at the end of each reporting period and makes provision for obsolete and slow-moving inventory items. Management also estimates the net realisable value for such inventories based primarily on the ageing of inventories, historical sales performances, post year-end sales, latest selling price and expectation of future saleability of the inventories. Management reassesses the estimation at the end of each reporting period. The carrying amount of inventories as at 31 December 2018 was HK$134,131,000 (2017: HK$218,900,000).

Provision for expected credit losses on trade receivables

The Group uses a provision matrix to calculate ECLs for trade receivables. The provision rates are based on days past due for groupings of various customer segments that have similar loss patterns (i.e., by geography and customer type).

The provision matrix is initially based on the Group's historical observed default rates. The Group will calibrate the matrix to adjust the historical credit loss experience with forward-looking information. At each reporting date, the historical observed default rates are updated and changes in the forward-looking estimates are analysed.

The application of forward-looking adjustment is a significant estimate. The amount of ECLs is sensitive to changes in circumstances and forecast economic conditions. The Group's historical credit loss experience and forecast of economic conditions may also not be representative of customer's actual default in the future. The information about the ECLs on the Group's trade receivables is disclosed in note 14 to the financial statements. The carrying amount of trade receivables was HK$32,037,000 (2017: HK$37,313,000).

Useful lives and residual values of items of property, plant and equipment

In determining the useful lives and residual values of items of property, plant and equipment, the Group periodically reviews the changes in market conditions, expected physical wear and tear, and the maintenance of the assets. The estimation of the useful life of the asset is based on experience of the Group with similar assets that are used in a similar way. Additional depreciation is made if the estimated useful lives and/or the residual values of items of property, plant and equipment are different from previous estimation. Useful lives and residual values are reviewed, at the end of each reporting period, based on changes in circumstances. The carrying amount of property, plant and equipment, excluding construction in progress, as at 31 December 2018 was HK$47,057,000 (2017: HK$64,207,000).

Notes to Financial Statements (Continued)

31 December 2018

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (CONTINUED)

Estimation uncertainty (Continued)

Deferred tax assets

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits together with future tax planning strategies. The amount of unrecognised tax losses at 31 December 2018 was HK$243,915,000 (2017: HK$178,360,000). Further details are set out in note 21 to the financial statements.

Impairment of plant and equipment

The Group assesses at the end of each reporting period whether there is any indication that plant and equipment may be impaired. If any indication exists, the Group estimates the recoverable amount of the Group's cash-generating unit ("CGU") to which plant and equipment belong to. The Group measures the recoverable amount of the CGU with reference to its value in use. The value in use calculation requires the Group to estimate the future cash flows expected to arise from the plant and equipment and apply a suitable discount rate in order to calculate their present value. As at 31 December 2018, the carrying amount of plant and equipment was nil (2017: HK$15,128,000). Further details are set out in note 11 to the financial statements.

4. OPERATING SEGMENT INFORMATION

No separate analysis of operating segment information is presented by the Group as over 90% of the Group's revenue, results and assets related to the processing and sale of semi-finished and finished leather in Mainland China during the year.

Information about a major customer

Revenue of approximately HK$21,068,000 (2017: HK$34,726,000) was derived from sales to a single customer, which constituted less than 10% (2017: 10.8%) of the total revenue during the year ended 31 December 2018.

Notes to Financial Statements (Continued)

31 December 2018

5. REVENUE, OTHER INCOME AND GAINS

Revenue

An analysis of revenue is as follows:

	2018 HK$'000	2017 HK$'000
Revenue from contracts with customers		
Sale of processed leather	**238,317**	322,146

(i) Disaggregated revenue information

Revenue is recognised when goods are transferred at a point in time to customers. The amount of revenue recognised in the current reporting period that was included in the contract liabilities at the beginning of the reporting period was HK$896,000.

(ii) Performance obligations

Information about the Group's performance obligations is summarised below:

Sale of goods

The performance obligation is satisfied upon delivery of the goods at a point in time and payment is generally due within 90 to 180 days from date of delivery, except for new customers, where payment in advance is normally required.

Other income and gains

	2018 HK$'000	2017 HK$'000
Finance income	**47**	68
Sale of scrap materials	**1,914**	1,240
Government grants*	**865**	15
Foreign exchange gains, net	**—**	3,648
Others	**530**	923
	3,356	5,894

* During the year ended 31 December 2018, the Group received HK$865,000 (2017: HK$15,000) from the PRC local government as a support to the Group's PRC operations.

Notes to Financial Statements (Continued)

31 December 2018

6. LOSS BEFORE TAX

The Group's loss before tax is arrived at after charging/(crediting):

	Notes	2018 HK$'000	2017 HK$'000
Cost of inventories sold		272,605	345,579
Auditor's remuneration		1,450	1,375
Depreciation	11	5,849	11,024
Interests on:			
Bank loans and discounting bills receivable to banks		994	2,556
Loans from the immediate holding company		4,337	3,847
Loan from a fellow subsidiary		642	405
		5,973	6,808
Employee benefit expense (excluding directors' remuneration *(note 8)*):			
Wages and salaries		24,606	29,032
Pension scheme contributions (defined contribution schemes)*		3,503	3,347
		28,109	32,379
Foreign exchange differences, net		536	(3,648)
Provision for inventories**		987	24,004
Minimum lease payments under operating leases in respect of land and buildings		960	900
Amortisation of prepaid land lease payments	12	299	291
Impairment of financial assets, net			
Impairment of trade receivables#	14	514	1,616
Impairment of financial assets included in prepayments, other receivables and deposits, net#	14	28	76
		542	1,692
Write-off of items of property, plant and equipment#	11	—	1,567
Loss on disposal of items of property, plant and equipment#		—	136
Reversal of accruals#		—	(4,804)

* At 31 December 2018 and 2017, the Group had no forfeited contributions available to reduce its contributions to the pension schemes in future years.

** This item is included in the "Cost of sales" on the face of the consolidated statement of profit or loss.

\# These items are included in the "Other operating income/(expenses), net" on the face of the consolidated statement of profit or loss.

Notes to Financial Statements (Continued)

31 December 2018

7. INCOME TAX

No provision for Hong Kong profits tax has been made as the Group did not generate any assessable profits arising in Hong Kong during the year (2017: Nil). Taxes on profits assessable in Mainland China have been calculated at the rate of tax prevailing in Mainland China in which the Group operates.

	2018 *HK$'000*	2017 *HK$'000*
Current — Mainland China		
Charge for the year	**206**	74
Underprovision in prior years	**—**	17
Deferred *(note 21)*	**—**	650
Total tax charge for the year	**206**	741

A reconciliation of the tax expense applicable to loss before tax at the statutory rates for the jurisdictions in which the Company and the majority of its subsidiaries are domiciled to the tax expense at the effective tax rates is as follows:

2018

	Hong Kong *HK$'000*	**Mainland China** *HK$'000*	**Total** *HK$'000*
Loss before tax	**(11,132)**	**(69,903)**	**(81,035)**
Tax at the statutory tax rate	**(1,837)**	**(17,476)**	**(19,313)**
Income not subject to tax	**(149)**	**(6,465)**	**(6,614)**
Expenses not deductible for tax	**1,081**	**8,778**	**9,859**
Tax losses utilised from previous periods	**—**	**(62)**	**(62)**
Tax losses not recognised	**905**	**15,431**	**16,336**
Tax charge at the Group's effective rate	**—**	**206**	**206**

2017

	Hong Kong *HK$'000*	Mainland China *HK$'000*	Total *HK$'000*
Loss before tax	(5,311)	(93,571)	(98,882)
Tax at the statutory tax rate	(876)	(23,393)	(24,269)
Adjustments in respect of current tax of previous periods	—	(17)	(17)
Income not subject to tax	(6,582)	(1,256)	(7,838)
Expenses not deductible for tax	6,636	15,246	21,882
Tax losses not recognised	822	10,161	10,983
Tax charge at the Group's effective rate	—	741	741

Notes to Financial Statements (Continued)

31 December 2018

8. DIRECTORS' REMUNERATION

Directors' remuneration for the year, disclosed pursuant to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"), section 383(1)(a), (b), (c) and (f) of the Hong Kong Companies Ordinance and Part 2 of the Companies (Disclosure of Information about Benefits of Directors) Regulation, is as follows:

	2018 ***HK$'000***	2017 *HK$'000*
Fees	**450**	450
Other emoluments:		
Salaries, allowances and benefits in kind	**641**	604
Pension scheme contributions	**178**	153
	819	757
	1,269	1,207

(a) Independent non-executive directors

The fees paid to independent non-executive directors during the year were as follows:

	2018 ***HK$'000***	2017 *HK$'000*
Mr. Fung Lak	**150**	150
Mr. Choi Kam Fai, Thomas	**150**	150
Mr. Chan Cheong Tat	**150**	150
	450	450

There were no other emoluments payable to the independent non-executive directors during the year (2017: Nil).

Notes to Financial Statements (Continued)

31 December 2018

8. DIRECTORS' REMUNERATION (CONTINUED)

(b) Executive directors and non-executive directors

	Fees *HK$'000*	Salaries, allowances and benefits in kind *HK$'000*	Pension scheme contributions *HK$'000*	Total remuneration *HK$'000*
2018				
Executive director:				
Mr. Sun Jun	—	641	178	819
	—	641	178	819
Non-executive directors:				
Mr. Ran Bo*	—	—	—	—
Mr. Xiao Zhaoyi	—	—	—	—
Mr. Ding Yatao^	—	—	—	—
Mr. Kuang Hu	—	—	—	—
	—	—	—	—
	—	641	178	819

	Fees *HK$'000*	Salaries, allowances and benefits in kind *HK$'000*	Pension scheme contributions *HK$'000*	Total remuneration *HK$'000*
2017				
Executive director:				
Mr. Sun Jun	—	604	153	757
	—	604	153	757
Non-executive directors:				
Mr. Ran Bo*	—	—	—	—
Mr. Xiao Zhaoyi	—	—	—	—
Mr. Kuang Hu	—	—	—	—
	—	—	—	—
	—	604	153	757

There was no arrangement under which a director waived or agreed to waive any remuneration during the year.

* Mr. Ran Bo resigned as a non-executive director of the Company on 24 March 2018.

^ Mr. Ding Yatao was appointed as a non-executive director of the Company on 24 March 2018.

Notes to Financial Statements (Continued)

31 December 2018

9. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees of the Group during the year included one (2017: one) director, details of whose remuneration are set out in note 8 above. Details of the remuneration for the year of the remaining four (2017: four) highest paid employees who are not directors of the Company are as follows:

	2018 *HK$'000*	2017 *HK$'000*
Salaries and allowances	1,782	1,696
Pension scheme contributions	206	258
	1,988	1,954

The number of non-director highest paid employees whose remuneration fell within the following band is as follows:

	Number of employees	
	2018	2017
Nil to HK$1,000,000	4	4

10. LOSS PER SHARE

The calculation of the basic loss per share amount is based on the loss for the year and the weighted average number of ordinary shares of 538,019,000 (2017: 538,019,000) in issue during the year.

The calculations of basic and diluted loss per share are based on:

	2018 *HK$'000*	2017 *HK$'000*
Loss		
Loss for the year, used in the basic loss per share calculation	81,241	99,623

	Number of shares	
	2018	2017
Shares		
Weighted average number of ordinary shares in issue during the year used in the basic loss per share calculation	538,019,000	538,019,000

No adjustment has been made to the basic loss per share amount presented for the years ended 31 December 2018 and 2017 in the calculation of diluted loss per share as there was no dilutive events during the years ended 31 December 2018 and 2017.

Notes to Financial Statements (Continued)

31 December 2018

11. PROPERTY, PLANT AND EQUIPMENT

	Buildings HK$'000	Leasehold improve-ments HK$'000	Plant and machinery HK$'000	Electronic equipment HK$'000	Furniture, fixtures and equipment HK$'000	Motor vehicles HK$'000	Construction in progress HK$'000	Total HK$'000
31 December 2018								
At 1 January 2018:								
Cost or valuation	50,759	24,179	125,027	3,507	497	5,969	1,680	211,618
Accumulated depreciation and impairment	—	(21,856)	(114,125)	(3,421)	(493)	(5,836)	—	(145,731)
Net carrying amount	50,759	2,323	10,902	86	4	133	1,680	65,887
At 1 January 2018, net of accumulated depreciation and impairment	50,759	2,323	10,902	86	4	133	1,680	65,887
Additions	—	257	46	12	—	203	912	1,430
Deficit on revaluation *(note (a))*	(219)	—	—	—	—	—	—	(219)
Impairment *(note (b))*	—	(837)	(9,339)	(123)	—	(171)	(1,895)	(12,365)
Depreciation provided during the year	(1,989)	(1,629)	(2,056)	(28)	(4)	(143)	—	(5,849)
Transfer	—	—	627	53	—	—	(680)	—
Exchange realignment	(1,494)	(114)	(180)	—	—	(22)	(17)	(1,827)
At 31 December 2018, net of accumulated depreciation and impairment	47,057	—	—	—	—	—	—	47,057
At 31 December 2018:								
Cost or valuation	47,057	23,316	120,584	3,415	497	5,993	1,826	202,688
Accumulated depreciation and impairment	—	(23,316)	(120,584)	(3,415)	(497)	(5,993)	(1,826)	(155,631)
Net carrying amount	47,057	—	—	—	—	—	—	47,057
Analysis of cost or valuation:								
At cost	—	23,316	120,584	3,415	497	5,993	1,826	155,631
At 31 December 2018 valuation	47,057	—	—	—	—	—	—	47,057
	47,057	23,316	120,584	3,415	497	5,993	1,826	202,688

Notes to Financial Statements (Continued)

31 December 2018

11. PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

	Buildings	Leasehold improve-ments	Plant and machinery	Electronic equipment	Furniture, fixtures and equipment	Motor vehicles	Construction in progress	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
31 December 2017								
At 1 January 2017:								
Cost or valuation	47,434	23,338	116,947	4,175	497	6,073	325	198,789
Accumulated depreciation and impairment	—	(16,409)	(84,946)	(3,800)	(483)	(5,843)	—	(111,481)
Net carrying amount	47,434	6,929	32,001	375	14	230	325	87,308
At 1 January 2017, net of accumulated depreciation and impairment	47,434	6,929	32,001	375	14	230	325	87,308
Additions	106	1,206	105	—	—	—	3,244	4,661
Surplus on revaluation *(note (a))*	4,185	—	—	—	—	—	—	4,185
Impairment *(note (b))*	—	(3,955)	(17,530)	(133)	—	(176)	—	(21,794)
Write-off	(1,179)	(388)	—	—	—	—	—	(1,567)
Depreciation provided during the year	(2,169)	(1,901)	(6,698)	(130)	(10)	(116)	—	(11,024)
Transfer	—	—	1,784	—	—	194	(1,978)	—
Disposals	—	—	(222)	(42)	—	(37)	—	(301)
Exchange realignment	2,382	432	1,462	16	—	38	89	4,419
At 31 December 2017, net of accumulated depreciation and impairment	50,759	2,323	10,902	86	4	133	1,680	65,887
At 31 December 2017:								
Cost or valuation	50,759	24,179	125,027	3,507	497	5,969	1,680	211,618
Accumulated depreciation and impairment	—	(21,856)	(114,125)	(3,421)	(493)	(5,836)	—	(145,731)
Net carrying amount	50,759	2,323	10,902	86	4	133	1,680	65,887
Analysis of cost or valuation:								
At cost	—	24,179	125,027	3,507	497	5,969	1,680	160,859
At 31 December 2017 valuation	50,759	—	—	—	—	—	—	50,759
	50,759	24,179	125,027	3,507	497	5,969	1,680	211,618

Notes to Financial Statements (Continued)

31 December 2018

11. PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

Notes:

(a) The Group's buildings were revalued individually at 31 December 2018 based on the valuations performed by Vigers Appraisal & Consulting Limited, independent professionally qualified valuers, at an aggregate open market value of HK$47,057,000 (2017: HK$50,759,000) based on their existing use, with a revaluation deficit of HK$219,000 (2017: revaluation surplus of HK$4,185,000) debited to other comprehensive income.

Had these buildings been carried at historical cost less accumulated depreciation and impairment losses, their carrying amounts as at 31 December 2018 would have been approximately HK$32,272,000 (2017: HK$35,783,000).

Each year, the Group appoints an external valuer to be responsible for external valuations of the Group's properties. Selection criteria include market knowledge, reputation, independence and whether professional standards are maintained. Management has discussion with the valuers on the valuation assumptions and valuation results when the valuation is performed at each interim and annual reporting date.

Fair value hierarchy

The following table illustrates the fair value measurement hierarchy of the Group's buildings:

	Fair value measurement as at 31 December 2018 using		
	Quoted prices in active markets (Level 1)	**Significant observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**
	HK$'000	***HK$'000***	***HK$'000***
Recurring fair value measurement for properties held for own use	**—**	**—**	**47,057**

	Fair value measurement as at 31 December 2017 using		
	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)
	HK$'000	*HK$'000*	*HK$'000*
Recurring fair value measurement for properties held for own use	—	—	50,759

During the year, there were no transfers of fair value measurements between Level 1 and Level 2 and no transfers into or out of Level 3 (2017: Nil).

Notes to Financial Statements (Continued)

31 December 2018

11. PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

Notes: (Continued)

(a) (Continued)

Fair value hierarchy (Continued)

Reconciliation of fair value measurements categorised within Level 3 of the fair value hierarchy:

	Properties held for own use *HK$'000*
Carrying amount at 1 January 2017	47,434
Additions for the year	106
Depreciation charge for the year	(2,169)
Gain from fair value measurement recognised in other comprehensive income	4,185
Write-off during the year	(1,179)
Exchange realignment	2,382
Carrying amount at 31 December 2017 and 1 January 2018	**50,759**
Depreciation charge for the year	**(1,989)**
Loss from fair value measurement recognised in other comprehensive income	**(219)**
Exchange realignment	**(1,494)**
Carrying amount at 31 December 2018	**47,057**

Below is a summary of the valuation techniques used and the key inputs to the valuation:

	Valuation technique	**Significant unobservable inputs**	**2018 Range**	2017 Range
Properties held for own use	Market approach	Market price per square metre	**RMB150 per square metre**	RMB150 per square metre
	Depreciated replacement cost method	Estimated hard cost of construction per square metre	**RMB400 to RMB900 per square metre**	RMB400 to RMB900 per square metre
		Estimated construction period	**1 year**	1 year
		Estimated soft cost of construction	**3% to 4.35% on estimated hard cost of construction**	3% to 4.35% on estimated hard cost of construction

Notes to Financial Statements (Continued)

31 December 2018

11. PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

Notes: (Continued)

(a) (Continued)

Fair value hierarchy (Continued)

A combination of the market and depreciated replacement cost approaches was adopted in assessing the land portions of the properties and the buildings and structures standing on the land, respectively. The sum of the two results represents the market value of the properties as a whole. In the valuation of the land portions, reference has been made to the sales comparables in the locality. Due to the fact that the nature of the buildings and structures cannot be valued on the basis of market value; they have therefore been valued on the basis of their depreciated replacement cost. The depreciated replacement cost approach considers the cost to reproduce or replace in new condition the property appraised in accordance with current construction costs for similar properties in the locality, with allowance for accrued depreciation as evidenced by an observed condition or obsolescence percent, whether arising from physical, functional or economic causes. The depreciated replacement cost approach generally furnishes the most reliable indication of value for properties in the absence of a known market based on comparable sales.

A significant increase in the market land price per square metre in isolation would result in a significant increase in fair value of the properties, and vice versa. A significant increase in hard and soft costs of construction in isolation would result in a significant increase in the fair value of the properties, and vice versa.

(b) During the year ended 31 December 2017, the consolidation of factories for production capacity integration and temporary production suspension for compliance of environmental regulations led to a decline in the sales and production activities of the Group. The weakening demand and keen competition in the tannery market persisted during the year ended 31 December 2018. As a result, the Group's operating results for the years ended 31 December 2018 and 2017 have been adversely affected.

In light of the performance of the manufacture and sale of leather business, the directors of the Company reassessed the recoverable amounts of plant and equipment as at 31 December 2018 and 31 December 2017 by reference to their value in use (the "VIU") as at 31 December 2018 and 31 December 2017. Based on the VIU, impairment losses of HK$12,365,000 (2017: HK$21,794,000) were recognised in the consolidated statement of profit or loss for the year ended 31 December 2018.

According to the VIU, the recoverable amounts of nil (2017: HK$15,128,000) as at 31 December 2018 were determined based on discounted cash flow calculations which were derived from the present value of expected future cash flows to be generated from the sale of semi-finished and finished leather. The pre-tax discount rate applied to the projected cash flows was 16.5% for 2018 (2017: 20.1%).

Notes to Financial Statements (Continued)

31 December 2018

12. PREPAID LAND LEASE PAYMENTS

	2018	2017
	HK$'000	*HK$'000*
Carrying amount at 1 January	**12,616**	12,071
Recognised during the year *(note 6)*	**(299)**	(291)
Exchange realignment	**(570)**	836
Carrying amount at 31 December	**11,747**	12,616
Current portion included in receivables, prepayments and deposits	**(288)**	(303)
Non-current portion	**11,459**	12,313

The Group's leasehold land is held under medium term leases and is situated in Mainland China.

13. INVENTORIES

	2018	2017
	HK$'000	*HK$'000*
Raw materials	**11,678**	9,639
Work in progress	**83,686**	169,766
Finished goods	**38,767**	39,495
	134,131	218,900

In light of the deteriorating sales demand and declining selling prices during the year, management reassessed the net realisable value of inventories and a provision of HK$987,000 was made for the year ended 31 December 2018 (2017: HK$24,004,000).

14. RECEIVABLES, PREPAYMENTS AND DEPOSITS

		2018	2017
	Notes	***HK$'000***	*HK$'000*
Trade receivables	*(i)*	**32,037**	37,313
Bills receivable	*(i)*	**26,031**	53,223
Prepayments, deposits and other receivables	*(ii)*	**6,508**	3,105
		64,576	93,641

Notes to Financial Statements (Continued)

31 December 2018

14. RECEIVABLES, PREPAYMENTS AND DEPOSITS (CONTINUED)

Notes:

(i) The Group's trading terms with customers are mainly on credit, except for new customers, where payment in advance is normally required. Invoices are normally payable within 60 days of issuance, except for certain well-established customers, where the terms are extended to 150 days. Each customer has a maximum credit limit. The Group seeks to maintain tight control over its outstanding receivables in order to minimise credit risk. Overdue balances are reviewed regularly by senior management. In view of the aforementioned and the fact that the Group's trade receivables relate to a large number of diversified customers, there is no significant concentration of credit risk. The Group does not hold any collateral or other credit enhancements over its trade receivable balances. Trade receivables are non-interest-bearing. The carrying amounts of trade and bills receivables approximate their fair values.

An ageing analysis of the trade and bills receivables as at the end of the reporting period, based on the settlement due date, is as follows:

	2018	2017
	HK$'000	*HK$'000*
Current	**53,964**	89,618
Less than 3 months	**2,932**	2,085
3 to 6 months	**1,543**	510
More than 6 months	**1,724**	—
	60,163	92,213
Impairment	**(2,095)**	(1,677)
	58,068	90,536

Movements in the loss allowance for impairment of trade receivables are as follows:

	2018	2017
	HK$'000	*HK$'000*
At 1 January	**1,677**	—
Impairment losses *(note 6)*	**514**	1,616
Exchange realignment	**(96)**	61
At 31 December	**2,095**	1,677

Notes to Financial Statements (Continued)

31 December 2018

14. RECEIVABLES, PREPAYMENTS AND DEPOSITS (CONTINUED)

Notes: (Continued)

(i) (Continued)

Impairment under HKFRS 9 for the year ended 31 December 2018

The Group has applied the simplified approach to provide impairment of ECLs prescribed by HKFRS 9, which permits the use of the lifetime expected loss provision for all trade receivables. An impairment analysis is performed at each reporting date for trade receivables using a provision matrix to measure ECLs. To measure the ECLs, trade receivables have been grouped based on shared credit risk characteristics and the days past due. The calculation of ECLs considered reasonable and supportable information that is available at the reporting date about past events, current conditions and forward-looking information.

Set out below is the information about the credit risk exposure on the Group's trade receivables using a provision matrix:

As at 31 December 2018

		Past due		
	Current	Less than 6 months	Over 6 months	Total
Expected credit loss rate	**0%**	**8.4%**	**100%**	**6.1%**
Gross carrying amount (HK$'000)	**27,990**	**4,418**	**1,724**	**34,132**
Expected credit losses (HK$'000)	**—**	**371**	**1,724**	**2,095**

An impairment analysis is performed at each reporting date for bills receivable by applying a loss rate approach with reference to the historical loss record of the Group. The loss rate is adjusted to reflect the current conditions and forecasts of future economic conditions, as appropriate. The Group estimated the expected loss rate of bills receivable was minimal and no ECLs in respect of the balance as at 31 December 2018 was made.

Impairment under HKAS 39 for the year ended 31 December 2017

Included in the above provision for impairment of trade and bills receivables which was measured based on incurred credit losses under HKAS 39 as at 31 December 2017 was a provision for individually impaired trade and bills receivables of HK$1,677,000 with a carrying amount before provision of HK$1,826,000. The individually impaired trade and bills receivables as at 31 December 2017 related to a debtor that was in default or delinquency payments and only a portion of the receivables was expected to be recovered.

Notes to Financial Statements (Continued)

31 December 2018

14. RECEIVABLES, PREPAYMENTS AND DEPOSITS (CONTINUED)

Notes: (Continued)

(i) (Continued)

Impairment under HKAS 39 for the year ended 31 December 2017 (Continued)

The ageing analysis of the trade and bills receivables as at 31 December 2017 that were not individually nor collectively considered to be impaired under HKAS 39 is as follows:

	2017 *HK$'000*
Neither past due nor impaired	89,478
Less than 3 months past due	839
3 to 6 months past due	70
	90,387

Receivables that were neither past due nor impaired related to a large number of diversified customers for which there was no recent history of default.

Receivables that were past due but not impaired related to a number of independent customers that had a good track record with the Group. Based on past experience, the directors of the Company were of the opinion that no provision for impairment under HKAS 39 was necessary in respect of these balances as there has not been a significant change in credit quality and the balances were still considered fully recoverable.

(ii) As at 31 December 2018, a provision of HK$394,000 (2017: HK$385,000) was made for other receivables with a gross carrying amount of HK$394,000 (2017: HK$385,000).

Movements in the provision for impairment of other receivables are as follows:

	2018 ***HK$'000***	2017 *HK$'000*
At 1 January	**385**	288
Impairment losses, net *(note 6)*	**28**	76
Exchange realignment	**(19)**	21
At 31 December	**394**	385

The ECLs as at 31 December 2018 are estimated by applying a loss rate approach with reference to the historical loss record of the Group as at 31 December 2018. The loss rate is adjusted to reflect the current conditions and forecasts of future economic conditions, as appropriate. The loss rate applied as at 31 December 2018 was 16.9%.

Notes to Financial Statements (Continued)

31 December 2018

14. RECEIVABLES, PREPAYMENTS AND DEPOSITS (CONTINUED)

Notes: (Continued)

(ii) (Continued)

Included in the above provision for other receivables, which was measured based on incurred credit losses under HKAS 39, as at 31 December 2017 was a provision for individually impaired other receivables of HK$385,000 with a gross carrying amount of HK$385,000. The individually impaired other receivables as at 31 December 2017 related to debtors who were in default in payments and were not considered recoverable.

The carrying amounts of other receivables approximate their carrying values.

15. CASH AND BANK BALANCES, AND PLEDGED BANK BALANCES

	2018 ***HK$'000***	2017 *HK$'000*
Cash and bank balances	**27,513**	30,174
Less: Pledged bank balances*	**—**	(1,066)
Cash and bank balances	**27,513**	29,108

* As at 31 December 2018, there were nil (2017: HK$1,066,000) bank balances pledged to banks for banking facilities granted to the Group (note 18).

At the end of the reporting period, the cash and bank balances of the Group denominated in Renminbi ("RMB") amounted to HK$25,456,000 (2017: HK$29,006,000). The RMB is not freely convertible into other currencies; however, under Mainland China's Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange RMB for other currencies through banks authorised to conduct foreign exchange business.

Cash at banks earns interest at floating rates based on daily bank deposit rates. Short term time deposits are made for varying periods of between one day and three months depending on the immediate cash requirements of the Group, and earn interest at the respective short-term time deposit rates. The bank balances and pledged bank balances are deposited with creditworthy banks with no recent history of default. The carrying amounts of cash and bank balances approximate their fair values.

Notes to Financial Statements (Continued)

31 December 2018

16. TRADE PAYABLES

An ageing analysis of the trade payables as at the end of the reporting period, based on the date of receipt of goods, is as follows:

	2018	2017
	HK$'000	*HK$'000*
Within 3 months	**28,127**	32,104
3 to 6 months	**5,670**	14,266
Over 6 months	**4,212**	3,181
	38,009	49,551

The trade payables of the Group are non-interest-bearing and are normally settled on terms of 90 days. The carrying amounts of trade payables approximate their fair values.

17. OTHER PAYABLES AND ACCRUALS

		2018	2017
	Notes	***HK$'000***	*HK$'000*
Other payables and accruals	*(a)*	**32,411**	27,594
Contract liabilities	*(b)*	**4,120**	—
Receipts in advance		**—**	1,308
		36,531	28,902

Notes:

(a) Included in the other payables is accrued interest of HK$10,537,000 (2017: HK$7,441,000) due to the immediate holding company which is repayable on demand, and arose from loans from the immediate holding company.

Details of the loans from the immediate holding company are included in note 18 to the financial statements.

Other payables of the Group are non-interest-bearing and have an average term of three months. The carrying amounts of other payables approximate their fair values.

(b) Contract liabilities include short-term advances received from customers for the sale of processed leather. The increase in contract liabilities in 2018 was mainly due to the increase in short-term advances received from customers in relation to the sale of leather at the end of the year.

As a practical expedient under HKFRS 15, the transaction prices allocated to the remaining performance obligations (unsatisfied or partially unsatisfied) as at 31 December 2018 are not disclosed as all the remaining performance obligations in relation to the sale of processed leather are part of contracts that have an original expected duration of one year or less.

Notes to Financial Statements (Continued)

31 December 2018

18. LOANS FROM A FELLOW SUBSIDIARY AND THE IMMEDIATE HOLDING COMPANY

		2018			2017		
	Notes	Effective interest rate (%)	Maturity	Amount HK$'000	Effective interest rate (%)	Maturity	Amount HK$'000
Current							
Loan from a fellow subsidiary	(a)	—	—	—	4.35	2018	41,177
Non-current							
Loans from the immediate holding company	(b)	**3.44–3.97**	**2021**	**142,379**	2.78–3.34	2021	141,138
				142,379			182,315

	2018 HK$'000	2017 HK$'000
Analysed into:		
Other borrowings repayable		
Within one year	**—**	41,177
In the third to fifth years, inclusive	**142,379**	141,138
	142,379	182,315

Notes:

(a) Last year's balance represented an unsecured loan from a fellow subsidiary of RMB34,420,000, which bore interest at 4.35% p.a.. The balance was fully repaid during the year ended 31 December 2018.

Notes to Financial Statements (Continued)

31 December 2018

18. LOANS FROM A FELLOW SUBSIDIARY AND THE IMMEDIATE HOLDING COMPANY (CONTINUED)

Notes: (Continued)

(b) The following table illustrates the loans from GDH, the Company's immediate holding company:

Notes	2018 HK$'000	2017 HK$'000
(i)	**22,779**	22,779
(ii)	**65,000**	65,000
(iii)	**54,600**	53,359
	142,379	141,138

Notes:

(i) The balance represents an unsecured loan from GDH of US$2,920,000 (2017: US$2,920,000), which bears interest ranging from 3-month LIBOR + 1.17% to 3-month LIBOR + 2% for the year ended 31 December 2018 (2017: 3-month LIBOR + 2%) and is repayable on 31 July 2021 (2017: repayable on 31 July 2021).

(ii) The balance represents an unsecured loan from GDH of HK$65,000,000 (2017: HK$65,000,000), which bears interest ranging from 3-month HIBOR + 1.17% to 3-month HIBOR + 2% for the year ended 31 December 2018 (2017: 3-month HIBOR + 2%) and is repayable on 9 August 2021 (2017: repayable on 9 August 2021).

(iii) The balance represents an unsecured loan from GDH of US$7,000,000 (2017: US$7,000,000), which bears no interest on or before 30 December 2018 and bears interest at 3-month LIBOR + 1.17% starting from 31 December 2018 (2017: no interest) and is repayable on 30 December 2021 (2017: repayable on 30 December 2021).

As at 31 December 2017, the Group's trust receipt loan facilities which were denominated in RMB and amounted to HK$119,630,000 were secured by the pledge of certain of the Group's bank balances and supported by corporate guarantees executed by the Company. None had been utilised at 31 December 2017. During the year ended 31 December 2018, the Group's trust receipt loan facilities were expired and the pledge of the Group's bank balances was released.

Details of the pledge of assets are included in note 30 to the financial statements.

The carrying values of the loans approximate their fair values.

19. DUE TO A PRC JOINT VENTURE PARTNER

The amount due to a PRC joint venture partner is unsecured, interest-free and has no fixed terms of repayment. The carrying amount approximates its fair value.

Notes to Financial Statements (Continued)

31 December 2018

20. PROVISION

	Early termination of a joint venture agreement *HK$'000*
At 1 January 2018	3,816
Exchange realignment	(176)
At 31 December 2018	3,640

With respect to the Group's decision in August 2001 to curtail the operations of 青島南海皮廠有限公司 (Qingdao Nanhai Tannery Co., Ltd.) ("Qingdao Tannery"), a subsidiary of the Group, due to its continuous losses, provisions of RMB3,000,000 were made for (a) staff redundancy payments of RMB2,000,000; and (b) compensation of RMB1,000,000 to the PRC joint venture partner for early termination of the joint venture agreement with Qingdao Tannery. These provisions were determined based on the relevant employment contracts and the terms of the joint venture agreement.

Qingdao Tannery is a Sino-foreign co-operative joint venture. Pursuant to the joint venture agreement, the registered capital of Qingdao Tannery was solely contributed by the Company. The PRC joint venture partner contributed its plant and equipment for the operations of Qingdao Tannery. The Company is entitled to all its distributable profits after the payment of an agreed annual fee to the PRC joint venture partner.

During the year ended 31 December 2004, the arbitration proceedings undertaken by the Group and the PRC joint venture partner were concluded by the China International Economic and Trade Arbitration Commissions in Shenzhen and Beijing. These proceedings determined that (i) the joint venture agreement of Qingdao Tannery was terminated with effect from 23 August 2001; (ii) Qingdao Tannery should be liquidated in accordance with the joint venture agreement and the relevant laws and regulations in the PRC; and (iii) the PRC joint venture partner's claim against the Company for an economic loss of RMB15 million due to the termination of the joint venture agreement was revoked.

As the liquidation of Qingdao Tannery has not been completed, no payment for the provision, additional provision or reversal of provision was made during the year.

Notes to Financial Statements (Continued)

31 December 2018

21. DEFERRED TAX LIABILITIES

Movements in deferred tax liabilities/(assets) of the Group during the year are as follows:

	Depreciation in excess of related tax depreciation *HK$'000*	Revaluation of properties *HK$'000*	Total *HK$'000*
At 1 January 2017	(629)	2,849	2,220
Deferred tax debited to the property revaluation reserve	—	1,046	1,046
Deferred tax debited to the statement of profit or loss during the year *(note 7)*	650	—	650
Exchange realignment	(21)	—	(21)
At 31 December 2017 and 1 January 2018	**—**	**3,895**	**3,895**
Deferred tax credited to property revaluation reserve	**—**	**(55)**	**(55)**
At 31 December 2018	**—**	**3,840**	**3,840**

The Group has tax losses arising in Hong Kong of HK$87,225,000 (2017: HK$81,741,000) that are available for offsetting against future taxable profits of the companies in which the losses arose. As at 31 December 2018, the Group had tax losses arising in Mainland China of HK$156,690,000 (2017: HK$96,619,000) that would expire in one to five years for offsetting against future taxable profits of the companies in which the losses arose. As at 31 December 2018, the Group has deductible temporary differences of HK$38,306,000 (2017: HK$31,528,000). Deferred tax assets have not been recognised in respect of these losses and deductible temporary differences as they have arisen in subsidiaries that have been loss-making for some time and the directors considered it is not probable that taxable profits will be available against which the tax losses can be utilised.

Pursuant to the PRC Corporate Income Tax Law, a 10% withholding tax is levied on dividends declared to foreign investors from the foreign investment enterprises established in Mainland China. The requirement is effective from 1 January 2008 and applies to earnings after 31 December 2007. A lower withholding tax rate may be applied if there is a tax treaty between Mainland China and the jurisdiction of the foreign investors. For the Group, the applicable rate is 5%. The Group is therefore liable for withholding taxes on dividends distributed by those subsidiaries established in Mainland China in respect of earnings generated from 1 January 2008.

At 31 December 2018, no deferred tax has been recognised for withholding taxes that would be payable on the unremitted earnings that are subject to withholding taxes of the Group's subsidiaries established in Mainland China. In the opinion of the directors, it is not probable that these subsidiaries will distribute such earnings in the foreseeable future. The unremitted earnings of the subsidiaries in Mainland China which represented the aggregate amount of the temporary differences for which deferred tax liabilities have not been recognised was nil at 31 December 2018 (2017: Nil).

Notes to Financial Statements (Continued)

31 December 2018

22. SHARE CAPITAL

Shares

	2018	2017
	HK$'000	*HK$'000*
Issued and fully paid:		
538,019,000 (2017: 538,019,000) ordinary shares	**75,032**	75,032

23. RESERVES

The amounts of the Group's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity of the financial statements.

(i) The general reserve fund of the Group is an undistributable reserve and may not be treated as realised profits.

On 25 November 1996, a court order confirming the reduction of the share premium account by HK$133,349,000 was registered by the Registrar of Companies in Hong Kong and the credit arising therefrom was transferred to the general reserve fund against which goodwill arising on the acquisition of a subsidiary was eliminated in the consolidated financial statements. In the year ended 31 December 2002, there was a release of goodwill of HK$133,349,000 in respect of impairment of an investment in a subsidiary relating to the goodwill arising from the acquisition of that subsidiary in 1996.

Pursuant to a special resolution passed in the Group's extraordinary general meeting held on 23 January 1998 and confirmed by the Order of the High Court of the Hong Kong Special Administrative Region of the PRC (the "Court") dated 2 March 1998, the share premium account was reduced by the amount of HK$34,397,000 and, as undertaken by the Group, a general reserve fund was credited in the books of accounts of the Group in the same amount for the purpose of setting off, in the consolidated financial statements of the Group and its subsidiaries, goodwill arising on consolidation in 1997. In 2000 and 2001, there was a release of goodwill of HK$12,478,000 and HK$21,919,000, respectively, in respect of impairment of investments in subsidiaries relating to the goodwill arising from the acquisition of the subsidiaries in 1997.

Notes to Financial Statements (Continued)

31 December 2018

23. RESERVES (CONTINUED)

(ii) On 1 February 2011, a special resolution was passed by the shareholders of the Company for approving the reduction in share premium of the Company (the "Share Premium Reduction"). The purpose of the Share Premium Reduction is to reduce the credit standing to the share premium account of the Company to the extent of HK$393,345,845 and to apply the credit arising from such reduction to eliminate the accumulated losses of the Company by the same amount.

On 22 March 2011, the Court made an order (the "Order") confirming the Share Premium Reduction. An office copy of the Order was registered with the Registrar of the Companies on 29 March 2011 (the "Effective Date") in accordance with Section 61 of the Hong Kong Companies Ordinance. Accordingly, the Share Premium Reduction became effective immediately following the registration of the Order of the Court and the accumulated losses of the Company of HK$393,345,845 were eliminated against the Company's share premium account.

In connection with the application for the Share Premium Reduction (the "Application"), the Company undertakes that in the event of the Company making any future recoveries of the assets identified in the Application for which provision for impairment in value or amortisation was made in the accounts of the Company between 31 December 2000 and 30 June 2010 (the "Assets"), beyond their written down values in the Company's accounts as at 30 June 2010, all such recoveries beyond that written down values up to an amount of HK$150,345,170 (the "Limit"), will be credited to a special capital reserve in the accounting records of the Company (the "Special Capital Reserve") and that so long as there shall remain outstanding any debt of or claim against the Company which, if the Effective Date was the date of the commencement of the winding up of the Company, would be admissible to proof in such winding up and the persons entitled to the benefit of such debts or claims shall not have agreed otherwise, such reserve shall not be treated as realised profits for the purposes of ss291, 297 and 299 of the new Companies Ordinance (Cap.622 of the Laws of Hong Kong) and shall (for so long as the Company shall remain a listed company) be treated as an undistributable reserve of the Company for the purposes of ss290 and 298 of the new Companies Ordinance (Cap. 622 of the Laws of Hong Kong), or any statutory re-enactments or modifications thereof provided that:

(1) the Company shall be at liberty to apply the Special Capital Reserve for the same purposes as a share premium account may be applied;

(2) the Limit in respect of the Special Capital Reserve may be reduced by the amount of any increase, after the Effective Date, in the amount standing to the credit of the share premium account of the Company as a result of the paying up of shares by the receipt of new consideration or the capitalisation of distributable profits;

(3) the Limit in respect of the Special Capital Reserve may be reduced upon the disposal or other realisation, after the Effective Date, of the Assets by the amount of the impairment in value and amortisation made in relation to such asset as at 30 June 2010 less such amount (if any) as is credited to the Special Capital Reserve as a result of such disposal or realisation; and

Notes to Financial Statements (Continued)

31 December 2018

23. RESERVES (CONTINUED)

(ii) (Continued)

(4) in the event that the amount standing to the credit of the Special Capital Reserve exceeds the Limit thereof after any reduction of such Limit pursuant to provisions (2) and/or (3) above, the Company shall be at liberty to transfer the amount of any such excess to the general reserves of the Company and the same shall become available for distribution.

During the year ended 31 December 2018, a reversal of provision for impairment of HK$70,000 was made for the Assets. This resulted in a transfer of HK$70,000 from the accumulated losses to the Special Capital Reserve.

The Limit as at 31 December 2018 was HK$150,273,970 (2017: HK$150,273,970) and the amount standing to the credit of the Group's Special Capital Reserve as at 31 December 2018 was HK$70,000 (2017: Nil).

(iii) Pursuant to the relevant PRC laws and regulations, a portion of the profits of the Group's subsidiaries which are established in Mainland China has been transferred to reserve funds which are restricted as to use.

(iv) Capital reserve represents the capital contribution from the immediate holding company.

24. SHARE OPTION SCHEME

On 24 November 2008, the Company adopted a new share option scheme (the "2008 Scheme").

The purpose of the 2008 Scheme is to provide incentives to selected employees, officers and directors who contribute to the Group and to provide the Company with a flexible means of retaining, incentivising, rewarding, remunerating, compensating and/or providing benefits to such employees, officers and directors or to serve such other purposes as the board of directors of the Company (the "Board") may approve from time to time. Eligible persons of the 2008 Scheme include the employees, officers or directors of the members of the Group. The 2008 Scheme, unless otherwise terminated or amended, will remain in force for 10 years from 24 November 2008.

The total number of ordinary shares which may be issued upon exercise of all share options to be granted under the 2008 Scheme (excluding any which has lapsed) and any other schemes of the Company must not, in aggregate, exceed 10% of the ordinary shares in issue as at the date of the adoption of the 2008 Scheme.

The total number of ordinary shares issued and to be issued upon exercise of the share options granted and to be granted under the 2008 Scheme to each eligible person (including exercised, cancelled and outstanding options) in any 12-month period up to and including the date of grant of share options must not exceed 1% of the ordinary shares in issue at such date. Any further grant of share options under the 2008 Scheme in excess of this limit is subject to shareholders' approval in a general meeting of the Company.

Notes to Financial Statements (Continued)

31 December 2018

24. SHARE OPTION SCHEME (CONTINUED)

Share options granted to a director or chief executive of the Company, or any of their respective associates, under the 2008 Scheme must be approved by the independent non-executive directors of the Company. In addition, for any share options granted to an independent non-executive director of the Company, or any of their respective associates, which would result in the ordinary shares issued and to be issued upon exercise of all share options already granted or to be granted under the 2008 Scheme (including options exercised, cancelled and outstanding) to such person in the 12-month period up to and including the date of such grant (i) representing in aggregate over 0.1% of the ordinary shares in issue; and (ii) having an aggregate value (based on the closing price of the ordinary shares at the date of grant) in excess of HK$5 million, such grant of options by the Board must be approved by shareholders in a general meeting.

An offer of grant of a share option under the 2008 Scheme may be accepted by the grantee within the period of the time stipulated by the Board, but no later than 14 days from the date of such offer. All share options under the 2008 Scheme will be unvested share options upon grant which will, subject to a grantee continuing to be an eligible person, vest with the grantee in accordance with the vesting schedules specified in their respective offer of grant. Subject to the rules of the 2008 Scheme and the relevant offer of the grant of a share option, a vested share option may be exercised in accordance with the terms of the rules of the 2008 Scheme at any time during the period to be determined and notified by the directors to each grantee, which period may commence on the date which is 2 years from the date of grant of the share option but shall end in any event no later than 10 years from the aforesaid date of grant. The exercise of any share option under the 2008 Scheme may be subject to the achievement of performance targets which may be determined by the Board, at its absolute discretion, on a case by case basis upon the grant of the relevant share option and stated in the offer of grant of such share option.

The exercise price of the share options under the 2008 Scheme is determinable by the Board and shall not be less than the highest of (i) the closing price of the ordinary shares as stated in the daily quotation sheet of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") on the date of grant of the share options; (ii) the average closing price of the Company's ordinary shares as stated in the Stock Exchange's daily quotation sheets for the five business days immediately preceding the date of grant of the share options; and (iii) the nominal value of the ordinary shares.

No dividends (including distributions made upon the liquidation of the Company) will be payable and no voting rights will be exercisable in relation to any share option that has not been exercised.

The 2008 Scheme expired during the year ended 31 December 2018. As at 31 December 2017 and 2018, there were no share options outstanding under the 2008 Scheme.

Notes to Financial Statements (Continued)

31 December 2018

25. CONTINGENT LIABILITIES

At the end of the reporting period, the Group did not have any contingent liabilities which had not been provided for in the financial statements.

26. OPERATING LEASE ARRANGEMENTS

As lessee

The Group leases certain of its office properties under operating lease arrangements. Leases for properties are negotiated for terms ranging from two to three years (2017: two to three years).

At 31 December 2018, the Group had total future minimum lease payments under non-cancellable operating leases falling due as follows:

	2018	2017
	HK$'000	*HK$'000*
Within one year	**960**	589
In the second to fifth years, inclusive	**776**	633
	1,736	1,222

27. COMMITMENTS

In addition to the operating lease commitments detailed in note 26 above, the Group had the following capital commitments at the end of the reporting period:

	2018	2017
	HK$'000	*HK$'000*
Contracted, but not provided for:		
Buildings	**20**	20
Leasehold improvements	**294**	503
Plant and machinery	**513**	657
	827	1,180

Notes to Financial Statements (Continued)

31 December 2018

28. NOTE TO THE CONSOLIDATED STATEMENT OF CASH FLOWS

Changes in liabilities arising from a financing activity

	Loan from a fellow subsidiary HK$'000
At 1 January 2017	—
Changes from financing cash flows	39,707
Foreign exchange movement	1,470
At 31 December 2017 and 1 January 2018	**41,177**
Changes from financing cash flows	**(40,764)**
Foreign exchange movement	**(413)**
At 31 December 2018	**—**

29. RELATED PARTY TRANSACTIONS

(a) In addition to the transactions detailed elsewhere in these financial statements, the Group had the following material transactions with related parties during the year:

	Notes	2018 HK$'000	2017 HK$'000
Office rental paid to a fellow subsidiary	*(i)*	**534**	485
Computer system maintenance service fees paid to a fellow subsidiary	*(ii)*	**246**	198
Interest expense to the immediate holding company	*(iii)*	**4,337**	3,847
Interest expense to a fellow subsidiary	*(iv)*	**642**	405

Notes:

(i) The office rental was charged by a fellow subsidiary at HK$44,500 per month for the year ended 31 December 2018 (2017: HK$44,500 per month) in accordance with the terms of the rental agreement between the Group and the fellow subsidiary. As at 31 December 2018, the Group had a rental deposit of HK$150,819 (2017: HK$150,819) with the fellow subsidiary.

(ii) The fellow subsidiary charged maintenance service fees of HK$245,710 for the year ended 31 December 2018 (2017: HK$197,553) for the computer system used by the Group based on contractual terms.

(iii) The interest expense to the immediate holding company arose from the loans advanced from GDH. Further details of the loan, including the terms, are disclosed in note 18 to the financial statements.

Notes to Financial Statements (Continued)

31 December 2018

29. RELATED PARTY TRANSACTIONS (CONTINUED)

(a) (Continued)

Notes: (Continued)

(iv) The interest expense to a fellow subsidiary arose from the loan advanced from a fellow subsidiary. Further details of the loan, including the terms, are disclosed in note 18 to the financial statements.

(b) Commitments with related parties:

On 28 November 2016, the Group entered into a three-year office rental agreement commencing 6 February 2017 and ending 5 February 2020 with Global Head Developments Limited, a fellow subsidiary of the Group, with a monthly rent of HK$44,500. The total operating lease commitments due within one year and in the second to fifth years as at 31 December 2018 were approximately HK$534,000 (2017: HK$534,000) and HK$45,000 (2017: HK$579,000), respectively.

(c) Outstanding balances with related parties:

(i) Details of the Group's loans from the immediate holding company and a fellow subsidiary as at the end of the reporting period are included in note 18 to the financial statements.

(ii) Details of the Group's accrued interest arising from loans from the immediate holding company as at the end of the reporting period are included in note 17(a) to the financial statements.

(d) Compensation of key management personnel of the Group:

The key management personnel are the directors. Details of their remuneration are disclosed in note 8 to the financial statements.

The related party transactions in respect of items in note 29(a), 29(b) and 29(c) above constituted continuing connected transactions as defined in Chapter 14A of the Listing Rules. However, these transactions are exempt from reporting, announcement and shareholders' approval requirements under Chapter 14A of the Listing Rules.

30. PLEDGE OF ASSETS

As at 31 December 2018, assets of the Group pledged to banks to secure general banking facilities granted to the Group were as follows:

	Note	**2018** ***HK$'000***	2017 *HK$'000*
Bank balances	*15*	—	1,066

Notes to Financial Statements (Continued)

31 December 2018

31. FINANCIAL INSTRUMENTS BY CATEGORY

The carrying amounts of each of the categories of financial instruments as at the end of the reporting period are as follows:

2018

Financial assets

	Financial assets at fair value through other comprehensive income *HK'000*	Financial assets at amortised cost *HK$'000*	Total *HK$'000*
Trade receivables	—	32,037	32,037
Bills receivable	26,031	—	26,031
Financial assets included in prepayments, other receivables and deposits	—	1,936	1,936
Cash and bank balances	—	27,513	27,513
	26,031	61,486	87,517

Financial liabilities

	Financial liabilities at amortised cost *HK$'000*
Trade payables	38,009
Financial liabilities included in other payables and accruals *(note 17)*	32,411
Due to a PRC joint venture partner	1,131
Loans from the immediate holding company	142,379
	213,930

Notes to Financial Statements (Continued)

31 December 2018

31. FINANCIAL INSTRUMENTS BY CATEGORY (CONTINUED)

The carrying amounts of each of the categories of financial instruments as at the end of the reporting period are as follows: (Continued)

2017

Financial assets

	Loans and receivables *HK$'000*
Trade and bills receivables	90,536
Financial assets included in prepayments, other receivables and deposits	1,742
Pledged bank balances	1,066
Cash and bank balances	29,108
	122,452

Financial liabilities

	Financial liabilities at amortised cost *HK$'000*
Trade payables	49,551
Financial liabilities included in other payables and accruals	22,646
Due to a PRC joint venture partner	1,131
Loans from the immediate holding company	141,138
Loan from a fellow subsidiary	41,177
	255,643

Notes to Financial Statements (Continued)

31 December 2018

32. TRANSFERS OF FINANCIAL ASSETS

Transferred financial assets that are not derecognised in their entirety

At 31 December 2018, the Group endorsed certain bills receivable accepted by banks in Mainland China (the "Endorsed Bills") with a carrying amount of RMB5,738,000 (equivalent to HK$6,549,000) (2017: RMB9,770,000 (equivalent to HK$11,688,000)) to certain of its suppliers in order to settle the trade payables due to such suppliers (the "Endorsement"). In the opinion of the directors, the Group has retained the substantial risks and rewards, which include default risks relating to such Endorsed Bills, and accordingly, it continued to recognise the full carrying amounts of the Endorsed Bills and the associated trade payables settled. Subsequent to the Endorsement, the Group does not retain any rights on the use of the Endorsed Bills, including the sale, transfer or pledge of the Endorsed Bills to any other third parties. The aggregate carrying amount of the trade payables settled by the Endorsed Bills to which the suppliers have recourse was RMB5,738,000 (equivalent to HK$6,549,000) (2017: RMB9,770,000 (equivalent to HK$11,688,000)) as at 31 December 2018.

Transferred financial assets that are derecognised in their entirety

At 31 December 2018, the Group endorsed certain bills receivable accepted by banks in Mainland China (the "Derecognised Bills") to certain of its suppliers in order to settle the trade payables due to such suppliers with a carrying amount of RMB23,488,000 (equivalent to HK$26,807,000) (2017: RMB13,728,000 (equivalent to HK$16,423,000). The Derecognised Bills had a maturity from one to six months at the end of the reporting period. In accordance with the Law of Negotiable Instruments in the PRC, the holders of the Derecognised Bills have a right of recourse against the Group if the banks default (the "Continuing Involvement"). In the opinion of the directors, the Group has not retained substantially all risks and rewards but transferred control relating to the Derecognised Bills. Accordingly, it has derecognised the full carrying amounts of the Derecognised Bills and the associated trade payables. The maximum exposure to loss from the Group's Continuing Involvement in the Derecognised Bills and the undiscounted cash flows to repurchase these Derecognised Bills is equal to their carrying amounts. In the opinion of the directors, the fair values of the Group's Continuing Involvement in the Derecognised Bills are not significant.

During the year ended 31 December 2018, the Group has not recognised any gain or loss on the date of transfer of the Derecognised Bills. No gains or losses were recognised from the Continuing Involvement, both during the year or cumulatively. The endorsement has been made evenly throughout the years ended 31 December 2018 and 2017.

33. FAIR VALUE AND FAIR VALUE HIERARCHY OF FINANCIAL INSTRUMENTS

Management has assessed that the fair values of cash and bank balances, pledged bank balances, trade and bills receivables, trade payables, financial assets included in prepayments, other receivables and deposits, financial liabilities included in other payables and accruals, a loan from a fellow subsidiary and an amount due to a PRC joint venture partner approximate their carrying amounts largely due to the short term maturities of these instruments.

The fair values of bills receivable and loans from the immediate holding company have been calculated by discounting the expected future cash flows using rates currently available for instruments with similar terms, credit risk and remaining maturities. The Group's own non-performance risk for borrowings as at 31 December 2018 and 2017 was assessed to be insignificant.

The head of the finance department of the Group is responsible for determining the policies and procedures for the fair value measurement of financial instruments. The head of the finance department reports directly to the chief financial officer and the audit committee. At each reporting date, the finance department analyses the movements in the values of financial instruments and determines the major inputs applied in the valuation. The valuation is reviewed and approved by the chief financial officer. The valuation process and results are discussed with the audit committee twice a year for interim and annual financial reporting.

The fair values of the financial assets and liabilities are included at the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. The following methods and assumptions were used to estimate the fair values:

Fair value hierarchy

The following tables illustrate the fair value measurement hierarchy of the Group's financial instruments:

Assets measured at fair value:

As at 31 December 2018

	Fair value measurement using			
	Quoted prices in active markets (Level 1)	**Significant observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**	**Total**
	HK$'000	***HK$'000***	***HK$'000***	***HK$'000***
Bills receivable	—	**26,031**	—	**26,031**

The Group did not have any financial assets measured at fair value as at 31 December 2017. During the year, there were no transfers of fair value measurement between Level 1 and Level 2 and no transfer into or out of Level 3 for financial assets (2017: Nil).

34. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments comprise interest-bearing unsecured other borrowings from the immediate holding company and a fellow subsidiary, and cash and bank balances. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets and liabilities such as trade and bills receivables, and trade payables, which arise directly from its operations.

The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk, credit risk and liquidity risk. The board of directors reviews and agrees policies for managing each of these risks and they are summarised below.

Interest rate risk

The Group's exposure to the risk of changes in market interest rates relates primarily to certain of the Group's debt obligations with floating interest rates.

The Group's policy is to manage its interest cost using an appropriate mix of fixed and floating rate borrowings. Despite the fact that the Group had its debt obligations at floating interest rates, in the opinion of the directors, the Group had no significant concentration of interest rate risk.

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the Group's loss before tax (through the impact on floating rate borrowings).

	Increase/ (decrease) in basis points	**Decrease/ (increase) in loss before tax** *HK$'000*
2018		
Hong Kong dollar	**100**	**(650)**
United States dollar ("US$")	**100**	**(229)**
Hong Kong dollar	**(10)**	**65**
US$	**(10)**	**23**
2017		
Hong Kong dollar	100	(650)
US$	100	(228)
Hong Kong dollar	(10)	65
US$	(10)	23

Notes to Financial Statements (Continued)

31 December 2018

34. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

Foreign currency risk

The Group has transactional currency exposures. Such exposures arise from purchases by operating units in currencies other than the units' functional currencies. Approximately 56% (2017: 71%) of the Group's purchases were denominated in currencies other than the functional currencies of the operating units making the purchases, whilst all sales were denominated in the units' functional currency.

The following table demonstrates the sensitivity at the end of the reporting period to a reasonably possible change in the US$-RMB exchange rate, with all other variables held constant, of the Group's loss before tax (due to changes in the fair value of monetary assets and liabilities). There is no impact on the equity of the Group.

	Increase/ (decrease) in exchange rate *%*	Decrease/ (increase) in loss before tax *HK$'000*
2018		
If RMB weakens against US$	**(3)**	**(2,656)**
If RMB strengthens against US$	**3**	**2,656**
2017		
If RMB weakens against US$	(3)	(6,227)
If RMB strengthens against US$	3	6,227

Notes to Financial Statements (Continued)

31 December 2018

34. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

Credit risk

The Group trades only with recognised and creditworthy third parties. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis and the Group's exposure to bad debts is not significant.

Maximum exposure and year-end staging as at 31 December 2018

The table below shows the credit quality and the maximum exposure to credit risk based on the Group's credit policy, which is mainly based on past due information unless other information is available without undue cost or effort, and year-end staging classification as at 31 December 2018. The amounts presented are gross carrying amounts for financial assets and the exposure to credit risk.

	12-month ECLs	Lifetime ECLs			
	Stage 1 *HK$'000*	**Stage 2** *HK$'000*	**Stage 3** *HK$'000*	**Simplified approach** *HK$'000*	*HK$'000*
Trade receivables*	—	—	—	34,132	34,132
Bills receivable	26,031	—	—	—	26,031
Financial assets included in prepayments, other receivables and deposits					
— Normal**	1,936	—	—	—	1,936
— Doubtful**	—	394	—	—	394
Cash and bank balances					
— Not yet past due	27,513	—	—	—	27,513
	55,480	394	—	34,132	90,006

* For trade receivables to which the Group applies the simplified approach for impairment, information based on the provision matrix is disclosed in note 14 to the financial statements.

** The credit quality of the financial assets included in prepayments, other receivables and deposits is considered to be "normal" when they are not past due and there is no information indicating that the financial assets had a significant increase in credit risk since initial recognition. Otherwise, the credit quality of the financial assets is considered to be "doubtful".

Notes to Financial Statements (Continued)

31 December 2018

34. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

Credit risk (Continued)

Maximum exposure as at 31 December 2017

The credit risk of the financial assets, which comprise cash and bank balances, pledged bank balances, trade and bills receivables and other receivables, arises from default of the counterparty, with a maximum exposure equal to the carrying amounts of these instruments.

Since the Group trades only with recognised and creditworthy third parties, there is no requirement for collateral. Concentrations of credit risk are managed by customer. As the Group's exposure spreads over a diversified portfolio of customers, there are no significant concentrations of credit risk within the Group.

Further details of the credit policy and quantitative data in respect of the Group's exposure to credit risk arising from trade and bills receivables are disclosed in note 14 to the financial statements.

Liquidity risk

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of bank loans and other interest-bearing loans.

The Group's policy is to regularly monitor its liquidity to ensure it maintains sufficient reserves of cash and cash equivalents and adequate committed lines of funding from major financial institutions, the immediate holding company and a fellow subsidiary to meet its liquidity requirements in the short and longer term.

The maturity profile of the Group's financial liabilities as at the end of the respective reporting period, based on the contractual undiscounted payments, is as follows:

2018

	On demand *HK$'000*	Less than 3 months *HK$'000*	3 to less than 12 months *HK$'000*	1 to 5 years *HK$'000*	Total *HK$'000*
Trade payables	9,882	28,127	—	—	38,009
Other payables and accruals	32,411	—	—	—	32,411
Due to a PRC joint venture partner	1,131	—	—	—	1,131
Loans from the immediate holding company	—	—	—	157,204	157,204
	43,424	28,127	—	157,204	228,755

Notes to Financial Statements (Continued)

31 December 2018

34. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

Liquidity risk (Continued)

2017

	On demand	Less than 3 months	3 to less than 12 months	1 to 5 years	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Trade payables	17,447	32,104	—	—	49,551
Other payables and accruals	22,646	—	—	—	22,646
Due to a PRC joint venture partner	1,131	—	—	—	1,131
Loans from the immediate holding company	—	—	—	153,148	153,148
Loan from a fellow subsidiary	—	—	42,499	—	42,499
	41,224	32,104	42,499	153,148	268,975

Capital management

The primary objectives of the Group's capital management are to safeguard the Group's ability to continue as a going concern and to maintain healthy capital ratios in order to support its business and maximise shareholders' value.

The Group manages its capital structure and makes adjustments to it in light of changes in economic conditions. To maintain or adjust the capital structure, the Group may return capital to shareholders or issue new shares. The Group is not subject to any externally imposed capital requirements. No changes were made in the objectives, policies or processes for managing capital during the years ended 31 December 2018 and 2017.

Notes to Financial Statements (Continued)

31 December 2018

34. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

Capital management (Continued)

The Group monitors capital using a gearing ratio, which is total debt divided by the equity attributable to equity holders of the Company plus total debt. Total debt includes loans from the immediate holding company and a fellow subsidiary. The gearing ratios as at the end of the respective reporting periods were as follows:

	2018	2017
	HK$'000	*HK$'000*
Loans from the immediate holding company	**142,379**	141,138
Loan from a fellow subsidiary	**—**	41,177
Total debt	**142,379**	182,315
Equity attributable to equity holders of the Company	**59,093**	151,272
Total debt and equity	**201,472**	333,587
Gearing ratio	**71%**	55%

Notes to Financial Statements (Continued)

31 December 2018

35. STATEMENT OF FINANCIAL POSITION OF THE COMPANY

Information about the statement of financial position of the Company at the end of the reporting period is as follows:

	2018	2017
	HK$'000	*HK$'000*
NON-CURRENT ASSETS		
Property, plant and equipment	**—**	3
Interests in subsidiaries	**173,353**	233,960
Total non-current assets	**173,353**	233,963
CURRENT ASSETS		
Prepayments, other receivables and deposits	**215**	214
Cash and bank balances	**1,719**	852
Total current assets	**1,934**	1,066
CURRENT LIABILITIES		
Amount due to a subsidiary	**31,858**	—
Other payables and accruals	**11,310**	7,763
Total current liabilities	**43,168**	7,763
NET CURRENT LIABILITIES	**(41,234)**	(6,697)
TOTAL ASSETS LESS CURRENT LIABILITIES	**132,119**	227,266
NON-CURRENT LIABILITY		
Loans from the immediate holding company	**87,779**	87,779
Total non-current liability	**87,779**	87,779
Net assets	**44,340**	139,487
EQUITY		
Share capital	**75,032**	75,032
Other reserves *(note)*	**(30,692)**	64,455
Total equity	**44,340**	139,487

Sun Jun
Director

Xiao Zhaoyi
Director

Notes to Financial Statements (Continued)

31 December 2018

35. STATEMENT OF FINANCIAL POSITION OF THE COMPANY (CONTINUED)

Note:

A summary of the Company's reserves is as follows:

	Equity component of convertible notes *HK$'000*	General reserve fund *HK$'000*	Special capital reserve *HK$'000*	Accumulated losses *HK$'000*	Total *HK$'000*
At 1 January 2017	5,545	167,746	—	(64,121)	109,170
Total comprehensive loss for the year	—	—	—	(44,715)	(44,715)
At 31 December 2017 and 1 January 2018	**5,545**	**167,746**	**—**	**(108,836)**	**64,455**
Total comprehensive loss for the year	**—**	**—**	**—**	**(95,147)**	**(95,147)**
Transfer from accumulated losses in accordance with the undertaking	**—**	**—**	**70**	**(70)**	**—**
At 31 December 2018	**5,545**	**167,746**	**70**	**(204,053)**	**(30,692)**

36. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 28 March 2019.

粵海制革有限公司
GUANGDONG TANNERY LIMITED