



The Directors have pleasure in submitting their report together with the audited accounts for the year ended 31st December 2005.

Principal Activities and Geographical Analysis of Operations

The principal activities of the Company and its subsidiaries (the "Group") consist of the manufacture, import, export and sale of carpets, manufacture and sale of yarn, trading and leasing of interior furnishings and property holding.

An analysis of the Group's performance for the year by business and geographical segments is set out in note 5 to the accounts.

Results and Appropriations

The results for the year are set out on page 43.

The Directors did not declare an interim dividend and do not recommend the payment of a final dividend for the year (2004: Nil).

Five-Year Consolidated Financial Summary

A summary of the consolidated results and of the assets and liabilities of the Group for the last five financial years is set out on page 5.

Reserves

Movements in reserves of the Group and the Company during the year are set out in the consolidated statement of changes in equity and Note 28 to the accounts.

Donations

During the year, donations made by the Group for charitable purposes amounted to HK\$ 2,500 (2004: HK\$ 26,000).

Property, Plant and Equipment

Movements in property, plant and equipment of the Group during the year are set out in Note 14 to the accounts.

Major Investment Properties

Details of the major properties held for investment purposes are set out on page 112.

Share Capital

Details of the movements in share capital of the Company are set out in Note 27 to the accounts.

Distributable Reserves

Distributable reserves of the Company at 31st December 2005 calculated under the Companies Act 1981 of Bermuda (as amended) amounted to HK\$ 98,063,000 (2004: HK\$ 98,684,000).

Subsidiaries

Particulars of the principal subsidiaries are set out on pages 110 and 111.

Purchase, Sale or Redemption of the Company's Shares

The Company has not redeemed any of its shares during the year. Neither the Company nor any of its subsidiaries has purchased or sold any of the Company's shares during the year.

Pre-emptive Rights

No shareholder pre-emptive rights exist in the jurisdiction in which the Company is incorporated.

Share Options

The existing share options scheme ("2002 Share Options Scheme" or the "Scheme") was approved by the shareholders of the Company at the Annual General Meeting held on 23rd May 2002. The details of the Scheme (which fully complies with Chapter 17 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") are as follows:

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| 1. Purpose | <p>(a) To provide participants (see the definition below) with the opportunity to acquire proprietary interests in the Company; and</p> <p>(b) To encourage participants to work towards enhancing the value of the Company and its shares for the benefit of the Company and its shareholders as a whole.</p> |
| 2. Participants | Any employee of the Group (whether full time or otherwise, including any Executive Director, Non-executive Director and Independent Non-executive Director of the Group) and any consultant of the Group who has contributed or will contribute to the Group. |
| 3. Maximum number of shares available for issue under the 2002 Share Options Scheme together with the percentage of share capital it represents as at the date of the annual report | 20,401,980 shares (representing 9.6% of issued share capital of the Company as at the date of this Directors' Report). |

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| 4. | Maximum entitlement of each participant | 1% of the shares in issue in any 12-month period up to the date of grant. |
| 5. | The period within which the shares must be taken up under an option | As specified by Directors, which shall not be more than 10 years from the date of grant. |
| 6. | The minimum holding period before an option can be exercised | Generally none, but subject to Directors' discretion on a case-by-case basis. |
| 7. | Amount payable on application or acceptance of the option and the periods within which payments must or may be made or loans made for such purposes must be repaid | HK\$ 10, payable upon acceptance of the option within 30 days of the grant of such option. |
| 8. | Basis of determining the exercise price | <p>Determined by the Directors being at least the highest of</p> <ul style="list-style-type: none"> (i) the closing price of a share as stated on the daily quotation sheet of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") at the date of grant; (ii) the average closing price of a share as stated in the Stock Exchange's daily quotation sheets for the five business days immediately preceding the date of grant; and (iii) the nominal value of a share. |
| 9. | The remaining life of the 2002 Share Options Scheme | The Scheme is valid and effective for a period of 10 years from 23rd May 2002. |

During the year a total of 2,000,000 share options were granted to Mr. James H. Kaplan, the Chief Executive Officer of the Company. Details of the share options outstanding as at 31st December 2005 are as follows:

Name	Balance as at 1st January 2005	Date of grant	Changes during the year			Balance as at 31st December 2005	Exercise price (HK\$) (Note 1)	Exercisable period
			Granted	Lapsed	Exercised			
James H. Kaplan	–	10th January 2005	500,000	270,000	230,000	–	1.21	10th January 2005– 31st January 2005
	–	10th January 2005	500,000	–	–	500,000	1.21	31st December 2005– 31st January 2006
	–	10th January 2005	500,000	–	–	500,000	1.21	31st December 2006– 31st January 2007
	–	10th January 2005	500,000	–	–	500,000	1.21	31st December 2007– 31st January 2008

Note 1: The exercise price of the share options granted to Mr. James H. Kaplan was fixed at the average of the closing prices of the shares of the Company as stated on The Stock Exchange's daily quotation sheets for the five business days before the date of grant. The closing price of the shares at the date on which the options were granted was HK\$ 1.18.

Apart from the above, the Company had not granted any share option under the 2002 Share Options Scheme to any other persons as required to be disclosed under Rule 17.07 of the Listing Rules.

The Company uses the Black Scholes option pricing model (the "Model") to value the share options granted during the year. The Model is one of the commonly used models to estimate the fair value of an option. The value of an option varies with different variables of certain subjective assumptions. Any change in such variables so adopted may materially affect the estimation of the fair value of an option.

The aggregate fair value of the options determined at the date of grant using the Model was HK\$ 341,000. Such value is expensed through the Group's profit and loss account over the respective vesting periods of each batch of options. Share option expense of HK\$ 176,000 was recognised in 2005, with a corresponding adjustment recognised in the Group's capital reserves.

The fair value of the share options are determined based on the following significant variables and assumptions:

Date of grant	10th January 2005
Closing price at the date of grant	HK\$ 1.18
Risk free rate (Note 1)	0.58% – 1.63%
Expected life of options	1 – 3 years
Expected volatility (Note 2)	38.65%
Expected dividend per annum (Note 3)	HK\$ 0.0218

Notes:

1. Risk free rate: being the approximate yields of Exchange Fund Notes and Bills traded on the date of grant, matching the expected life of each batch of options.
2. Expected volatility: being the approximate volatility of closing prices of the share of the Company in the past one year immediately before the date of grant.
3. Expected dividend per annum: being the approximate average annual cash dividend for the past five financial years.

During the period between 1st January 2006 and the date of this Directors' Report, Mr. James H. Kaplan further exercised 254,000 share options, and 246,000 share options lapsed. As at the date of this Directors' Report, options to subscribe for a total of 1,000,000 shares were still outstanding under the 2002 Share Options Scheme, which represent approximately 0.47% of the issued share capital of the Company.

Directors

The names of the Directors at the date of this Report are set out on pages 19 and 20.

On 13th May 2005, Mr. James S. Dickson Leach resigned as Chairman and Non-executive Director of the Company due to his retirement. Mr. Nicholas T. J. Colfer was appointed Chairman while Mr. David C.L. Tong was appointed Non-executive Director of the Company.

On 8th September 2005, Mr. Anthony Y. C. Yeh and Mr. Kent M. C. Yeh resigned as Non-executive Directors of the Company due to personal reasons.

On 1st November 2005, Ms. Alison S. Bailey resigned as Chief Operating Officer and Executive Director of the Company due to personal reasons.

On 15th November 2005, Mr. Roderic N. A. Sage was appointed Independent Non-executive Director of the Company.



In accordance with Bye-laws 100, 109(A), 189(v) and 189(ix) of the Company's Bye-laws, Mr. Roderic N. A. Sage, Mr. David C. L. Tong, Mr. Ian D. Boyce, Mr. John J. Ying shall retire, while Mr. James H. Kaplan shall retire voluntarily. All retiring Directors shall offer themselves for re-election on the forthcoming Annual General Meeting.

Directors' Service Contracts

None of the Directors who are proposed for re-election at the forthcoming Annual General Meeting has a service contract with the Company which is not determinable within one year without payment of compensation, other than statutory compensation.

Directors' Interests in Contracts

The Company and Hong Kong Carpet (Holdings) Limited, an indirect wholly-owned subsidiary of the Company, entered into a severance agreement (the "Agreement") on 30th July 2003 with Mr. Kent M. C. Yeh ("Mr. Yeh") pursuant to which Mr. Yeh's employment by Hong Kong Carpet (Holdings) Limited as the Managing Director of the Company would be terminated with effect from 31st August 2003. Mr. Yeh remained as Non-executive Director of the Company until the resignation of his directorship on 8th September 2005.

The major terms of the Agreement include:

1. a "non-compete" clause whereby Mr. Yeh undertook not to compete with the Company or any members of the Group in any business connected with the sale, marketing, manufacturing, trading, retailing, export or distribution of carpets anywhere in the world for a period of two years from the employment termination date; and
2. a "consultancy" undertaking whereby Mr. Yeh undertook to provide such consultancy services as were required by the Group (including but not limited to assisting the Group in developing and maintaining relationships with existing and potential customers and suppliers and providing information regarding the Group's business) for a two-year period following 31st August 2003.

The consideration of the Agreement was HK\$ 5,400,000, payable in three yearly instalments. The first and second instalments of HK\$ 2,700,000 and HK\$ 1,350,000 were paid in August 2003 and August 2004 respectively, and the third instalment of HK\$ 1,350,000 was paid in August 2005.

Apart from the above, no other contracts of significance in relation to the Group's business to which the Company and its subsidiaries was a party and in which a Director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

Independent Non-executive Directors

The Company has received from Mrs. Yvette Y. H. Fung, Mr. Michael T. H. Lee, Mr. Lincoln C. K. Yung and Mr. Roderic N. A. Sage, Independent Non-executive Directors, written confirmations of independence pursuant to Rule 3.13 of the Listing Rules.

The Company considers all the Independent Non-executive Directors to be independent.

Biographical Details of Directors and Senior Management

Brief biographical details of Directors and senior management are set out on pages 19 to 20, and page 113 to 114 respectively.

Directors' Interests in Competing Business

None of the Directors of the Company have any interest in any business which may compete with the business of the Group.

Directors' Interests in Equity Securities

As at 31st December 2005, the interests of the Directors in the shares of the Company and its associated corporations (within the meaning of the Part XV of Securities and Futures Ordinance ("SFO")) as recorded in the register maintained by the Company under Section 352 of the SFO or as notified to the Company were as follows:

(a) Ordinary shares of HK\$ 0.10 each in the Company

No. of ordinary shares held (long position)

Name	Personal interests	Corporate interests	Aggregate % to the share capital
Ian D. Boyce	214,371	–	0.101%
David C. L. Tong	431,910	–	0.204%
Lincoln C. K. Yung	30,000	–	0.014%
Lincoln K. K. Leong	–	2,000,000*	0.944%
Nelson K. F. Leong	–	2,000,000*	0.944%
(Alternate Director to Lincoln K.K. Leong)			
John J. Ying	–	32,575,875#	15.371%
James H. Kaplan	268,000	–	0.126%

* Mr. Nelson K. F. Leong is interested in the same shares as disclosed by Mr. Lincoln K. K. Leong. The shares are held through a company which is controlled by Mr. Lincoln K. K. Leong and Mr. Nelson K.F. Leong.

The shares are held through Peak Capital Partners I, L.P. (formerly known as iVentures I, L.P.) of which Mr. John J. Ying is interested in more than one-third of the voting shares.

Save for the Directors' interests as disclosed above, at no time during the year was the Company or any of its subsidiaries a party to any arrangements to enable the Directors and Chief Executives of the Company to hold any interests in the shares in, or debentures of, the Company or any other body corporate.

Substantial Shareholders

As at 31st December 2005, the register of substantial shareholders required to be kept under Section 336 of part XV of the SFO showed that the Company had been notified of the following interests, being 5% or more in the issued ordinary share capital of the Company. These interests are in addition to those disclosed above in respect of the Directors.

Name	No. of ordinary shares held in the Company of HK\$ 0.10 each (long position)	Aggregate % to the share capital
Bermuda Trust Company Limited	117,688,759*	55.531%
HWR Trustees Limited	117,688,759*	55.531%
Esko Limited	117,688,759*	55.531%
Hesko Limited	117,688,759*	55.531%
Lawrencium Corporation	117,688,759*	55.531%
Acorn Holdings Corporation	117,688,759*	55.531%
New Holmium Holding Corporation	117,688,759*	55.531%
Peak Capital Partners I, L.P. (formerly known as iVentures I, L.P.)	32,575,875#	15.371%

* Bermuda Trust Company Limited and HWR Trustees Limited are deemed to be interested in the 117,688,759 shares in which Esko Limited and Hesko Limited are deemed to be interested. Esko Limited and Hesko Limited are deemed to be interested in the 117,688,759 shares in which Lawrencium Corporation and Acorn Holdings Corporation are deemed to be interested. Lawrencium Corporation and Acorn Holdings Corporation are deemed to be interested in the 117,688,759 shares in which New Holmium Holding Corporation is interested. The 117,688,759 shares are owned by New Holmium Holding Corporation.

Mr. John J. Ying (a Director of the Company) is the sole shareholder of the general partner of Peak Capital Partners I, L.P. and is deemed to have interest in the shares held by Peak Capital Partners I, L.P. (the Company is advised that the term "general partner" commonly refers to the entity liable for all the debts and obligations of a limited partnership and has power to bind a limited partnership).

Management Contracts

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

Major Customers and Suppliers

During the year, the Group sold less than 30% of its goods and services to its five largest customers and purchased less than 30% of its goods and services from its five largest suppliers.

Connected Transactions

- (a) Significant related party transactions entered into by the Group during the year ended 31st December 2005, which do not constitute connected transactions and are not required to be disclosed under the Listing Rules, are disclosed in Note 37 to the accounts.
- (b) Other related party transactions entered into by the Group in 2005 and up to the date of this Directors' Report, which fall under the definition of "connected transactions" or "continuing connected transactions" and are not exempted under the Rule 14A.31 and Rule 14A.45 of the Listing Rules, are as follows:
 - i) The Company's subsidiaries have been from time to time supplying products, and providing related ancillary services to The Hongkong and Shanghai Hotels, Limited ("HKS Hotels") and its subsidiaries. These transactions fall under the definition of continuing connected transactions under the Listing Rules by virtue of the fact that Bermuda Trust Company Limited, a substantial shareholder of the Company, is also interested in more than 30% voting power of HKS Hotels. In accordance with the requirements of the Listing Rules, the Company entered into a master supply agreement with HKS Hotels on 22nd March 2005 for the supply of carpets and floor coverings and provision of ancillary services to HKS Hotels and its subsidiaries on normal commercial terms for a period of three years subject to an annual cap of HK\$ 8,500,000. An announcement in this respect was made on 22nd March 2005. During the year, the total order amount and invoiced value of these transactions amounted to HK\$ 6,790,000 and HK\$ 7,007,000 respectively.

The Directors, including all the Independent Non-executive Directors, have reviewed these transactions and confirmed that these transactions have been entered into:

1. in the ordinary and usual course of business of the Group;
2. either on normal commercial terms or, if there are not sufficient comparable transactions to judge whether they are on normal commercial terms, on terms no less favourable to the Group than terms available to independent third parties; and
3. in accordance with the master supply agreement governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

The Company's auditors have reported to the Directors in their letter that based on their work performed:

1. the continuing connected transactions have been approved by the Company's Board of Directors;
2. such transactions have been entered into in accordance with the pricing policies of the Group and the relevant agreements or order contracts governing the transactions; and

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3. the amounts on such transactions in 2005 have not exceeded the relevant cap amounts.
- ii) On 22nd August 2005, CII Cement Limited ("CIIC"), a non-wholly owned subsidiary of the Company, entered into an agreement to transfer its entire 54.54% stake in Changzhou Nantai Construction Materials Company Limited ("Nantai Construction", a Sino-foreign joint venture company incorporated in The People's Republic of China) to Changzhou Nanyang Construction Materials Company ("CNCMC") which held 40.31% interests in Nantai Construction. As CNCMC was a substantial shareholder of Nantai Construction at that moment, the transfer was therefore a connected transaction under the Listing Rules and an announcement of the transaction was made on 22nd August 2005. The aggregate consideration for the transaction of RMB 8,000,000 (approximately HK\$ 7,700,000) was arrived at after arm's length negotiation and on normal commercial terms.
- iii) On 25th January 2006, Carpets International Thailand Public Company Limited ("CIT"), a non-wholly owned subsidiary of the Company, entered into an agreement with Feltech Manufacturing Company Limited ("FMCL") to purchase underlay, compressed polyester felt, bi-component polyester fibers and such other products as may be supplied by FMCL from time to time. The agreement constitutes continuing connected transactions by virtue of the fact that Mr. Wan Tabtiang, a Director of CIT, is interested in 61.75% of the voting power at the general meeting of FMCL.

The Company confirms that it has complied with the disclosure requirements in accordance with Chapter 14A of the Listing Rules in respect of connected transactions and continuing connected transactions.

PUBLIC FLOAT

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

AUDITORS

The accounts have been audited by PricewaterhouseCoopers who retire and, being eligible, offer themselves for re-appointment.

By order of the Board
James H. Kaplan
Chief Executive Officer

Hong Kong, 24th April 2006