



Directors' Report

The Directors have pleasure in submitting their report together with the audited accounts for the year ended 31 December 2006.

Principal Activities and Geographical Analysis of Operations

The principal activities of the Company and its subsidiaries (the "Group") consist of manufacture, import, export and sale of carpets, manufacture and sale of yarns, manufacture and sale of mattresses, and property holding.

The discontinued operation comprised sale and leasing of interior furnishings in Hong Kong.

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 37.

The Directors did not declare an interim dividend and the Directors recommend a final dividend of HK 3 cents per share for the year ended 31 December 2006, absorbing a total of HK\$6,366,000 (2005: Nil), to shareholders whose names appear on the register of members as at 15 June 2007.

Five-year Consolidation 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 31 to the accounts.

Donations

During the year, donations made by the Group for charitable purposes amounted to HK\$558,000 (2005: HK\$2,500).

Property, Plant and Equipment

Movements in property, plant and equipment of the Group during the year are set out in Note 16 to the accounts.

Major Investment Properties

Details of major properties held for investment purposes are set out on page 97.

Share Capital

Details of the movements in share capital of the Company are set out in Note 30 to the accounts.

Distributable Reserves

Distributable reserves of the Company as at 31 December 2006, calculated under the Companies Act 1981 of Bermuda (as amended), amounted to HK\$94,292,000 (2005: HK\$98,063,000).

Subsidiaries

Particulars of the principal subsidiaries are set out on pages 95 and 96.

Purchase, Sales 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 was 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 23 May 2002. The details of the Scheme (which fully complies with Chapter 17 of the Listing Rules) are as follows:

1. Purpose

- To provide participants (see the definition below) with the opportunity to acquire proprietary interests in the Company.
- 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.

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).

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

Determined by the Directors being at least the highest of

- the closing price of a share as stated on the daily quotations sheet of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") at the date of grant;
- 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
- 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 23 May 2002.

During 2006, the closing price of the Company's shares immediately before the date on which the share options were exercised was HK\$1.2.

Details of the share options outstanding as at 31 December 2006 are as follows:

Name	Balance as at	Date of grant	Changes during the year			Balance as at	Exercise price	Exercisable period
	1 January 2006		Granted	Lapsed	Exercised	31 December 2006	(HK\$) (Note)	
James H. Kaplan	500,000	10 January 2005	—	246,000	254,000	—	1.21	31 December 2005– 31 January 2006
	500,000	10 January 2005	—	—	—	500,000	1.21	31 December 2006– 31 January 2007
	500,000	10 January 2005	—	—	—	500,000	1.21	31 December 2007– 31 January 2008

Note: 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 in 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 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 significant variables and assumptions used for calculating the fair value of the share options are set out in Note 30 to the accounts.

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 options expense of HK\$51,000 was recognised in 2006, with a corresponding adjustment recognised in the Group's capital reserve.

During the period between 1 January 2007 and the date of this Directors' Report, no share options were exercised by Mr. James H. Kaplan, and 500,000 share options lapsed. As at the date of this Directors' Report, options to subscribe for a total of 500,000 shares are outstanding under the 2002 Share Options Scheme, which represent approximately 0.24% 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 15 and 16.

In accordance with bye-laws 100, 109(A), 189(v) and 189(ix) of the Company's Bye-Laws, Mr. Michael T. H. Lee, Mr. Lincoln K. K. Leong and Mr. David C. L. Tong shall retire, while Mr. Nicholas T. J. Colfer and 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

No 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. Roderic N. A. Sage and Mr. Lincoln C. K. Yung, 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 15 to 16 and 98 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 31 December 2006, 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:

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*	0.943%
Nelson K. F. Leong (Alternate Director to Lincoln K. K. Leong)	—	2,000,000*	0.943%
John J. Ying	—	32,575,875 [#]	15.352%
James H. Kaplan	522,000	—	0.246%

* 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. of which Mr. John J. Ying is the sole shareholder of the general partner of Peak Capital Partners I, L.P. and is deemed to have an 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).

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 executive 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 31 December 2006, 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*	55.465%
Harneys Trustees Limited	117,688,759*	55.465%
Lawrencium Holdings Limited	117,688,759*	55.465%
Acorn Holdings Corporation	117,688,759*	55.465%
New Holmium Holding Corporation	117,688,759*	55.465%
The Hon. Sir Michael Kadoorie	117,688,759*	55.465%
Peak Capital Partners I, L.P.	32,575,875 [#]	15.352%

* Bermuda Trust Company Limited are deemed to be interested in the same 117,688,759 shares in which Lawrencium Holdings Limited and Acorn Holdings Corporation are deemed to be interested. Lawrencium Holdings Limited, Acorn Holdings Corporation and Harneys Trustees Limited are deemed to be interested in the same 117,688,759 shares in which New Holmium Holding Corporation is interested. These shares are held by New Holmium Holding Corporation. For the purpose of the SFO, the spouse of the Hon. Sir Michael Kadoorie has a duty of disclosure in Hong Kong in relation to the 117,688,759 shares. The interest disclosed by the spouse of the Hon. Sir Michael Kadoorie is that of the Hon. Sir Michael Kadoorie attributed to her under the SFO. Except the above, she has no interest, legal or beneficial in those shares.

[#] Mr. John J. Ying (a Non-executive Director of the Company) is the sole shareholder of the general partner of Peak Capital Partners I, L.P. and is deemed to have an 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 31 December 2006, which did not constitute connected transactions and were not required to be disclosed under the Listing Rules, are disclosed in Note 40 to the accounts.
- (b) Other related party transactions entered into by the Group in 2006 and up to the date of this Directors' Report, which fall under the definition of "connected transactions" or "continuing connected transactions" and not exempted under 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 ("HSH") 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 HSH. In accordance with the requirements of the Listing Rules, the Company entered into a master supply agreement with HSH on 22 March 2005 for the supply of carpets and floor coverings and provision of ancillary services to HSH 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 22 March 2005. For the year ended 31 December 2006, the total order amount and invoiced value of these transactions ("HSH Transactions") amounted to HK\$5,887,000 and HK\$5,898,000 respectively.

The Directors, including all the Independent Non-executive Directors, have reviewed the HSH Transactions and confirmed that they 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 HSH Transactions have been approved by the Company's Board of Directors;
2. the HSH 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
3. the amounts on the HSH Transactions in 2006 have not exceeded the relevant cap amounts.

- (ii) Carpets International Thailand Public Company Limited ("CIT", a non-wholly owned subsidiary of the Company) has been from time to time purchasing underlay, felt polyester fibres and other products from Feltech Manufacturing Company Limited ("Feltech"). These transactions fall under the definition of continuing connected transactions under the Listing Rules by virtue of the fact that Feltech is 61.75% owned by Mr. Wan Tabtiang, a director of CIT. In accordance with the requirements of the Listing Rules, CIT entered into a master supply agreement with Feltech on 25 January 2006 for the purchase of such products from Feltech on normal commercial terms for a period of three years subject to an annual cap of HK\$9,800,000. An announcement in this respect was made on 25 January 2006. For the year ended 31 December 2006, the total order amount and invoiced value of these transactions ("Feltech Transactions") amounted to HK\$1,562,000 and HK\$1,408,000 respectively.

The Directors, including all the Independent Non-executive Directors, have reviewed the Feltech Transactions and confirmed that they 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 Feltech Transactions have been approved by the Company's Board of Directors;
2. the Feltech Transactions have been entered into in accordance with the terms of the relevant agreements or order contracts governing such transactions; and
3. the amounts on the Feltech Transactions in 2006 have not exceeded the relevant cap amounts.

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

PricewaterhouseCoopers did not seek for re-appointment as the Company's auditors upon their retirement in the Annual General Meeting held on 16 June 2006 and BDO McCabe Lo Limited was appointed auditors of the Company.

The accounts have been audited by BDO McCabe Lo Limited who will retire, and being eligible, offer themselves for re-appointment.

By order of the Board

James H. Kaplan

Chief Executive Officer

Hong Kong, 20 April 2007

