TAI PING

# Tai Ping Carpets International Limited
# Annual Report 2006

**(Incorporated in Bermuda with Limited Liability)**

(Stock Code: 0146)

## VISION

To build Tai Ping into a modern, global premium brand that is unrivaled in its industry, and to continue to execute an ambitious strategy for the future to ensure the brand remains without peer. Recognised and respected worldwide for quality, artistry, design and outstanding customer service, Tai Ping will continue to post annual growth in sales, market share and operating income.

## VALUES

Integrity applies equally to our high standards for product quality and corporate governance. The Tai Ping brand envisioned can only be achieved with an unwavering Commitment. Excellence is a given; and the foundation on which the brand is built. We distinguish ourselves in everything we do, from design to manufacturing to customer service. We rely on Teamwork—each completed carpet comes from the partnership and passion of countless individuals. Social and Environmental Responsibility is a cornerstone of our philosophy: we are committed to the people who work with us and are stewards of the international lands on which we operate.

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# Tai Ping at a Glance

Tai Ping is Asia's premier carpet manufacturer and is a leader in the international custom carpet industry. The Company was founded in 1956 by a group of visionary businessmen and has been publicly traded since 1973. The Company's shares are traded under stock code 146 on The Stock Exchange of Hong Kong Limited.

The Company has grown from a small cottage industry making traditional Chinese knotted rugs to a vertically integrated, full-service manufacturer of hand tufted, machine woven and tufted carpets with myriad variety and sales in over 100 countries.

Tai Ping offers its customers access to a full range of quality floorcovering products, from luxury to affordable, appropriate for every commercial and residential environment. The Company's global network attends to customer needs with unparallelled attention to detail, providing a full service from custom design through post-installation services. With its superior design and manufacturing capabilities, Tai Ping can transform the most complicated custom design into a work of art for the most discerning buyer.

## Financial Highlights

In thousands of Hong Kong dollars except per share amounts

| | | 2006 | 2005 |
|---|---|---|---|
| **Per share** | Net worth per share (HK$) | **3.80** | 3.36 |
| | Earnings per share (HK cents) | | |
| | - Continuing operations | **17.28** | 4.60 |
| | - Discontinued operation | **(1.87)** | (1.56) |
| | Final dividend declared per share (HK cents) | **3.0** | 0.0 |
| **For the year** | Turnover – Continuing operations | **900,026** | 709,432 |
| | Profit/(loss) for the year | | |
| | - Continuing operations | **40,984** | 37,758 |
| | - Discontinued operation | **(3,964)** | (3,304) |
| | Profit attributable to equity holders of the Company | **32,694** | 27,646 |
| | Earnings before interest, tax, depreciation and amortisation | **114,689** | 96,430 |
| | Additions to property, plant & equipment and construction in progress | **32,661** | 63,818 |
| **At 31 December** | Capital and reserves attributable to the Company's equity holders | **773,861** | 683,607 |
| | Shares in issue (in thousands) | **212,187** | 211,933 |
| **Ratio** | Return on capital and reserves attributable to equity holders | **4.5%** | 4.1% |

# Five-year Consolidated Financial Summary

Year ended 31 December

## Assets and liabilities

| | 2006 | 2005 | 2004 | 2003 | 2002 |
|---|---|---|---|---|---|
| | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 |
| Total assets | **1,047,655** | 990,721 | 891,563 | 840,192 | 824,888 |
| Total liabilities | **240,590** | 279,250 | 204,999 | 151,949 | 175,138 |
| Total equity | **807,065** | 711,471 | 686,564 | 688,243 | 649,750 |

## Profit and loss account

| | 2006 | 2005 | 2004 | 2003 | 2002 |
|---|---|---|---|---|---|
| | HK$'000 | HK$'000 | HK$'000 | HK$'000 | HK$'000 |
| Profit/(loss) attributable to: | | | | | |
| Equity holders of the Company | **32,694** | 27,646 | (3,903) | 16,293 | 17,656 |
| Minority interests | **4,326** | 6,808 | 2,916 | 1,054 | 2,442 |
| | **37,020** | 34,454 | (987) | 17,347 | 20,098 |

# Chairman's Statement

In 2006 we maintained the transformation process that I outlined last year, focusing strongly on relaunching the brand and building sales capabilities.

At the same time, we made considerable efforts to enhance production efficiencies in support of the recent vigorous sales growth while maintaining strict controls on capital expenditure.

Turnover increased by 27% to HK$900 million as a result, with particularly good growth in the USA and Asia. It is a tribute to both sales and production staff that core carpet sales have increased during this transformation period to last year's HK$817 million from HK$410 million in 2003, while the strength of the brand and quality of the product range raised average margins from 38% to 44%.

Tai Ping was recognised with several awards in 2006, including two for Domotex in Germany and one for Most Innovative Products at Hospitality Design in the USA.

On the commercial front, large scale prestigious projects were won in 2006 such as the MGM and Wynn Casinos in Macau. Hospitality projects such as the Crowne Plaza in Prague as well as the luxurious carpet at the Mandarin Oriental Bangkok supplied by Carpets Inter were also completed. In 2006, Tai Ping began installation of our Axminster carpet at the world's largest convention centre at McCormick Place in Chicago.

In 2006 we also began to see the positive impact of this strategy on profitability. Our investment to strengthen our global sales capability over the last three years inevitably affected profit adversely in the short term. Now, however, the resultant increased sales at improved margins are at a level to enhance profitability. Thus, operating profit excluding extraordinary items was HK$24 million in 2006, compared with a loss of HK$15 million and HK$21 million in 2005 and 2004 respectively.

Our Weihai joint ventures in China also performed well in 2006, with combined sales up 34% year-on-year. Weihai retains a dominant position in its domestic market, while increasing international sales through our expanding distribution channels. Its large new factory will be operational in 2007, which will increase capacity to support further sales growth.

We continued our programme of disposal of non-core assets, and during the year sold Indigo, the furniture operation. Although Indigo had been a stable contributor, it would have required further investment to develop the business significantly, and it was considered more appropriate to focus resources on the core carpet operations.

During 2007 the Company expects to maintain sales growth in both its existing markets and, after opening distribution channels, in new markets in Asia, Europe and the Americas.

On behalf of the Board, I should like to thank all staff for their considerable efforts during 2006. I am also grateful to the Directors for their valuable support and advice during past year.

**Nicholas T. J. Colfer**
*Chairman*

Hong Kong, 20 April 2007

# Management Discussion and Analysis

The Group's consolidated turnover of continuing operations for the year ended 31 December 2006 totalled HK$900.0 million, a 27% increase from HK$709.4 million in 2005. The gross margin also improved, to 43% in 2006 from 39% in 2005. These significant gains resulted directly from the Group's three-year focus on investing in and growing the carpet operations. In 2006, carpet operations accounted for 91% of the consolidated turnover of the Group's continuing operations (2005: 88%).

The Group recorded a profit attributable to equity holders of HK$32.7 million in 2006, a gain of HK$5.1 million, or 18%, as compared with HK$27.6 million in 2005. The increased profitability in 2006 was mainly attributable to the sustained business growth and margin improvement of carpet operations.

The real improvement in 2006 was in fact greater than the net profit figures reflect. Net profit in 2005 showed a substantial rise of HK$43.9 million before tax, yet the increase was principally due to the disposal of substantial non-core assets and investments, as well as revaluation surpluses of investment properties. Excluding such items, the Group's continuing operations incurred a loss of HK$15.1 million in 2005, compared with an operating profit of HK$24.2 million in 2006 on a similar basis.

## Carpet Operations

Total turnover of carpet operations in 2006 increased by 30%, or HK$189.5 million, to HK$816.9 million. The improvement was mainly attributable to strong growth in the commercial and residential sectors of the USA market.

Turnover in the USA accounted for 44% of total carpet turnover in 2006, while Asia and Europe/Others accounted for 42% and 14% respectively. In 2005, the corresponding shares of total carpet turnover by the USA, Asia and Europe/Others were 35%, 48% and 17%.

Gross margin in 2006 also rose from 40% to 43%, despite increases in fuel costs and labour rates. The gain derived mainly from rising sales of higher-margin residential carpets and improved factory utilisation and efficiencies.

As a result, carpet operations made a segmental profit of HK$15.2 million in 2006, compared with a segmental loss of HK$29.9 million in 2005. The 2005 figures were adversely affected by one-time initial losses incurred that year from the costs of acquiring the business assets and incorporating the operations of Edward Fields, Inc. ("Edward Fields").

In the last quarter of 2006, the Group reorganised sales and support functions into two global business units: Commercial and Residential, Boutique Contract ("RBC"). The restructuring addresses the fact that the commercial and residential businesses have distinct customer bases, markets and distribution channels. Designed to drive the two business units to evaluate and explore new opportunities on a global basis, the initiative is meant to increase management accountability and to improve the transparency of investment and returns so as to prioritise and optimise investment and resource deployment.

### Marketing & Branding

Following the previously established strategy of promoting the brand to a wider audience, Tai Ping opened new and renovated fully branded showrooms in Los Angeles, Hong Kong and New Delhi during 2006. Tai Ping continued to use its fully branded Trade Show booths in Las Vegas, Miami, Monte Carlo and Paris. Fully branded overview brochures were produced for both Commercial and RBC business units with high-quality photography and designed to complement the all-white sales tools introduced into the marketplace in 2005.

Global Marketing provided support and guidance for the commercial unit in the development of new sales tools using the revamped Carpets Inter brand identity in Thailand. Global Marketing also developed additional sales tools under the Tai Ping Contract brand.

To communicate a Tai Ping point of view to the highly sophisticated RBC audience, Global Marketing and Design teams collaborated closely on the development and introduction of distinctive hand-made collections. The teams also worked collegially to produce ancillary support materials for new product launches, including luxurious photography, collection brochures, portfolios and press kits. These efforts aided Tai Ping in obtaining a constant stream of press in a wide variety of media, from significant editorial coverage in international publications to product placement in industry and business publications. As a result, Tai Ping has gained greater brand recognition worldwide through means more cost-effective than advertising.

For Edward Fields, 2006 brought the development of a brand strategy to ensure future growth. Implementation of the Edward Fields branding effort is slated for 2007, beginning with the creation of an updated corporate identity and a newly branded showroom in New York. The launch of a company-wide newsletter and intranet helped sales and design teams access marketing tools, improve internal communications and knit together teams around the world.

**USA**

The USA continues to be the primary growth market. Both the commercial and residential businesses recorded strong sales growth during the year, and significantly improved operating results.

Investments made in prior years for long-term expansion in the commercial market, including the addition of experienced sales representatives and field designers and the provision of effective sales and marketing tools, have already yielded measurable results. Despite fierce competition in certain sectors of the commercial market, turnover in the commercial business increased by more than 40% to HK$208.3 million in 2006, with particular focus maintained on the booming hospitality and gaming sectors. The operating results of the commercial carpet business showed significant improvement in 2006 as the Group began to benefit from an effective leveraging of the growth, with lower incremental costs and expenses and stable gross profit margin percentages.

The residential sector's first full operational year in the USA was 2006. For this area of operations, 2005 was occupied with opening the flagship Tai Ping showroom in New York and the acquisition of the business assets of Edward Fields, Inc., including its nation-wide distribution network.

Turnover of the residential business was HK$144.3 million in 2006, an increase of more than 140% over sales in 2005. The average gross profit margin was significantly higher than the commercial business. Also, the related operating costs and expenses in 2006 were relatively lower than the 2005 level, which included one-time initial expenses for business launch and additional post-acquisition costs associated with the incorporation of the Edward Fields operations.

During the year, Tai Ping opened a second showroom in Los Angeles, relocating and converting an old Edward Fields showroom. This was branded as a Tai Ping showroom with dedicated display space and sales staff reserved for Edward Fields products. A programme was developed to renovate or re-locate, as appropriate, the other Edward Fields showrooms over the next few years.

The Group expects that the residential business will be a principal target for both revenue and profit growth over the next few years because of its higher margin and the Group's competitive edge in product quality, customer service, design support, and branding.

**Hong Kong, Macau and China**

In the Hong Kong, Macau and China region, turnover rose to HK$80.4 million, a 26% improvement over 2005. Hong Kong and Macau's booming casino and resort markets, Tai Ping's primary segments in this region, buoyed the commercial businesses. Despite intense competition from Chinese manufacturers, the Group's sales increases did not compromise profitability. The average gross margin percentage decreased only slightly in 2006 because the Group's strategy was to compete with premium product quality and strong service commitment and design support, rather than price.

The Group also exercised tight control of incremental selling expenses, while cost management at the Foshan Nanhai factory in mainland China benefited from improved utilisation and factory efficiencies. Operating results continued to improve in 2006.

**Thailand and South East Asia**

Thailand's strong economy as well as the rebranding with new, improved sales tools benefited Carpets International Thailand Public Company Limited, the dominant player in the Thai domestic market selling under the "Carpets Inter" brand. Sales in 2006 increased in this region by 7% to HK$232.9 million, due to the overall growth of the commercial sector both in Thailand and throughout South East Asia.

The gross margin percentages remained relatively flat in 2006 as increases in raw material prices and energy costs offset the savings from improved factory utilisation and efficiencies.

The environmentally friendly felt-backed modular carpet tile, which was developed in-house and branded "Eco-Soft", was launched during the year. It is expected to boost sales in new markets.

**Europe**

Total turnover generated by the European subsidiaries amounted to HK$74.3 million, a 14% increase over 2005.

The relatively moderate increase in sales was mainly attributable to a management change in the Germany subsidiary, Tai Ping Carpets Interieur GmbH, and the postponement of several orders to 2007 at the request of customers.

The Group implemented a number of strategic initiatives in 2006 to expand its future market share of the commercial and residential businesses throughout Europe. In the past, it focused on niche markets. For the residential business, it targeted the high-end interior design community. For the commercial business, it concentrated on certain medium-scale, lower-margin projects, mainly in France and Germany. In 2007, the Group plans to explore further expanding distribution channels and establishing residential operations in key new markets.

In targeting commercial business in the UK, Middle East and other parts of Europe, the Group established a UK-based sales and design team in 2005, with a resulting sales increase to HK$18.0 million in 2006 from HK$4.4 million in 2005. The UK team remains the driving force for aggressive growth in the commercial business in Europe and Middle East.

Despite stable gross profit margin percentages, the European subsidiaries increased operating losses from 2005 to 2006. This was due both to planned personnel changes and to investments made to prepare for future business growth.

**Jointly Controlled Entities and Associate**

The Weihai group encompasses three jointly controlled entities : Weihai Shanhua Huabao Carpet Co. Ltd. and Weihai Shanhua Premier Carpet Co. Ltd. (both 49% owned), plus Weihai Shanhua Floorcovering Products Co. Ltd. (42% owned). Due to strong market demand and the dominant market position of its products within China, the Weihai group's combined turnover totalled HK$716.8 million, a 34% increase over the 2005 total of HK$534.1 million. Assisted by the Group in global marketing and distribution, these companies also sell Weihai "Shanhua" products outside the PRC. The complementary arrangement expands the Group's range of existing products and price points. The Group's share of profit after income tax expenses of the jointly controlled entities in 2006 amounted to HK$28.0 million, a 15% increase over the 2005 results (HK$24.3 million).

Philippine Carpet Manufacturing Corporation ("PCMC"), the 33% owned associate, recorded a small profit for the Group of HK$0.2 million in 2006 despite slightly lower sales, compared with a small net loss in 2005.

## Other Operations

**Yarn Dyeing**

Premier Yarn Dyers, Inc. ("PYD"), which operates the Group's US-based yarn-dyeing facilities, posted lower turnover and segmental results for 2006, at HK$48.5 million (2005: HK$57.6 million) and HK$6.0 million (2005: HK$8.7 million), respectively.

**Interior Furnishings**

Indigo Living Limited ("Indigo") and Banyan Tree Limited ("Banyan Tree"), the Group's interior furnishings operations in Hong Kong, have been subjected to intense market competition during the last few years. Overall profitability and returns on assets deployed have been relatively low. In addition, the interior furnishings business requires significant working capital to carry substantial inventories with a relatively high risk of obsolescence.

In view of this, the Group sold its interests in Indigo and Banyan Tree in July 2006 at a consideration of HK$19.2 million. Their operating results for 2005 and 2006 were reclassified and presented as discontinued operation.

As a result, the segmental turnover and operating results for interior furnishings under continuing operations in both 2006 and 2005 represented that of Suzhou Shuilian Mattress Co. Ltd. only. Turnover and profit before tax in 2006 grew by HK$11.1 million and HK$1.0 million, respectively, as compared with 2005. This was mainly attributable to the booming hospitability industry in China and Hong Kong.

**Property Holding**

The Group disposed of an investment property in Thailand during the year for an aggregate sum of HK$43.7 million, which produced a net gain on disposal of HK$1.3 million. Rental income decreased in 2006 as a result, to HK$4.7 million (2005: HK$5.6 million).

Revaluation of investment properties held on 31 December 2006 generated for the Group a net surplus of HK$6.5 million (2005: HK$15.6 million), included in the consolidated profit and loss account.

## Group Capital Expenditure

Capital expenditure in the form of property, plant, equipment and construction in progress incurred by the Group totalled HK$32.7 million in 2006 (2005: HK$63.8 million). As at 31 December 2006, the aggregate net book value of the Group's property, plant and equipment, investment properties, leasehold and land use rights, and construction in progress amounted to HK$383.5 million (2005: HK$410.6 million).

It is expected that the capital expenditure will increase in 2007 to expand factory capacities and renovate residential showrooms to support the sales growth.

## Liquidity and Financial Resources

The Group coordinates its financing and cash management activities at the corporate level, and usually funds its business with internally generated cash flows and through banking facilities at various subsidiaries.

As at 31 December 2006, the Group had total bank borrowings of HK$11.0 million (2005: HK$109.3 million). Total cash and bank balances amounted to HK$59.0 million (2005: HK$87.1 million). The net cash balance was HK$48.0 million as at 31 December 2006. The gearing ratio, calculated as net bank borrowings (total bank borrowings net of cash and bank balances) divided by total equity, was 0% (2005: 3%).

As at 31 December 2006, the Group also held financial assets at fair value through profit or loss of HK$23.8 million.

The bank loans outstanding on 31 December 2006 were unsecured and carried interest at fixed interest rates throughout their terms. The currency denomination of the loans and their maturity dates as at 31 December 2006 were as follows:

| | **2006**<br>**HK$'000** | 2005<br>HK$'000 |
|---|---|---|
| Within 1 year | | |
| Thai Baht | **11,000** | 55,859 |
| United States Dollar | — | 16,977 |
| Hong Kong Dollar | — | 27,000 |
| | **11,000** | 99,836 |
| Between 1 and 2 years | | |
| Thai Baht | — | 9,500 |
| Total borrowings | **11,000** | 109,336 |

## Exposure to Foreign Exchange Risks and Related Hedges

The Group has overseas operations in the PRC, Thailand, Singapore, the USA and Europe. The Group treats its investments in these foreign operations as permanent equity, so exchange differences from translating the net investments in these foreign operations do not affect cash flows and are dealt with in the reserves.

The European and Singaporean operations are not significant in terms of the Group's results. The Chinese Renminbi gradually appreciated against the Hong Kong dollar during 2006. The major exchange differences arising from overseas operations relate mostly to Thailand. The effect of these exchange differences, however, has been partly reduced because borrowings are in local currency and by hedging against some of its foreign currency exposure (including accounts receivable from export sales).

The Group's export sales are denominated primarily in US dollar, and to a much lesser extent in Euro.

The Group, therefore, considers its exposure to exchange rate movements in 2006 managed and will continue to monitor exchange rate movements closely to ascertain if any material exposure may arise.

## Employee and Remuneration Policies

As at 31 December 2006, the Group employed 3,200 employees (2005: 3,100 employees). Employees are remunerated according to the nature of the job and market trends, with built-in merit components incorporated as an annual incentive to reward and motivate individual performance. Staff costs and retirement benefit costs for 2006 totalled HK$270.6 million (2005: HK$221.5 million) and HK$5.9 million (2005: HK$4.6 million) respectively.

## Contingent Liabilities

As at 31 December 2006, the Group's total contingent liabilities amounted to HK$12.9 million (see Note 39 to the accounts for full disclosure) (2005: HK$8.5 million).

**James H. Kaplan**
*Chief Executive Officer*

Hong Kong, 20 April 2007

# Board of Directors

## Chairman and Non-executive Director

**Nicholas T. J. Colfer**: aged 47; Chairman since 2005; Non-executive Director since 2003.

Mr. Colfer is a Director of Sir Elly Kadoorie & Sons Limited and serves on several other corporate boards in Hong Kong. He holds a Master of Arts Degree from the University of Oxford.

## Chief Executive Officer and Executive Director

**James H. Kaplan**: aged 51; Executive Director and Chief Executive Officer since 2003.

Prior to joining the Company, Mr. Kaplan was Divisional Vice-President of the high-end global furniture manufacturer Knoll International. He holds a Bachelor of Arts Degree from Lafayette College.

## Non-executive Directors

**Ian D. Boyce**: aged 62; Non-executive Director since 1999.

Mr. Boyce is Chairman of Sir Elly Kadoorie & Sons Limited, a Non-executive Director of CLP Holdings Limited and Deputy Chairman of The Hongkong & Shanghai Hotels, Limited. He is a Chartered Accountant with extensive investment banking experience.

**Lincoln K. K. Leong**: aged 46; Non-executive Director since 1997.

Mr. Leong is the Finance Director of MTR Corporation Limited and a Non-executive Director of Hong Kong Aircraft Engineering Limited. He is a Chartered Accountant and holds a Master of Arts Degree from the University of Cambridge. He is the elder brother of Mr. Nelson K. F. Leong.

**Nelson K. F. Leong**: aged 43; Alternate Director to his brother Lincoln K. K. Leong since 1997.

Mr. Leong is a Director of a number of companies involved in real estate in Hong Kong and North America. He holds a Master of Business Administration Degree from the University of Toronto and a Bachelor of Arts Degree from Brown University.

**David C. L. Tong**: aged 36; Non-executive Director since 1997. Remuneration Committee.

Mr. Tong is a Director of Sir Elly Kadoorie & Sons Limited and serves on several other corporate boards in Hong Kong. He is a Chartered Engineer and holds a Bachelor of Engineering Degree from the University of London.

**John J. Ying**: aged 44; Non-executive Director since 1999. Audit Committee.

Mr. Ying is the Managing Director of Peak Capital, an established private equity firm focused on investments in Greater China, a member of the Graduate Executive Board of the Wharton School, Chairman of the Hong Kong Ballet, and Vice Chairman of the Hong Kong International School. He holds a Master of Business Administration Degree from the Wharton School, a Master of Arts Degree from the University of Pennsylvania, and a Bachelor of Science Degree from the Massachusetts Institute of Technology.

## Independent Non-executive Directors

**Yvette Y. H. Fung**: aged 45; Independent Non-executive Director since 2004. Remuneration Committee.
Mrs. Fung is Deputy Chairman of Synergis Holdings Limited, Non-executive Director of Fountain Set (Holdings) Limited, Independent Non-executive Director of Hong Kong Catering Management Limited, Executive Director of Hsin Chong Holdings (HK) Limited, Court Member of the Hong Kong University of Science and Technology and a Board member of the Hong Kong International School. She holds a Juris Doctor Degree from Stanford Law School, a Master of Business Administration Degree from the University of California Los Angeles, and a Bachelor of Arts Degree from Stanford University.

**Michael T. H. Lee**: age 45; Independent Non-executive Director since 1998. Audit Committee.
Mr. Lee is the Managing Director of Hysan Development Company Limited, a member of the Main Board Listing Committee of The Stock Exchange of Hong Kong Limited, a member of the SFC (HKEC Listing) Committee, a member of the Executive Committee of Hong Kong Housing Society, President of Hong Kong Society for the Protection of Children and Vice-Chairman of Helping Hand. He holds a Bachelor of Arts Degree from Bowdoin College and a Master of Business Administration Degree from Boston University.

**Roderic N. A. Sage**: aged 54; Independent Non-executive Director since 2005. Chairman of Remuneration Committee and Chairman of Audit Committee.
Mr. Sage is Chief Executive Officer of a specialist tax, corporate services and trust consultancy. He is a Chartered Accountant and was until 2003 a Senior Partner and member of the management board of KPMG in Hong Kong.

**Lincoln C. K. Yung**, JP: aged 61; Independent Non-executive Director since 2004, and previously a Non-executive Director (1980-2004).
Mr. Yung has extensive experience in the textile industry, banking and investment, and has served on various community and government committees. He is currently Deputy Managing Director of Nanyang Holdings Limited and a Director of Shanghai Commercial Bank Limited, The Shanghai Commercial & Savings Bank, Limited, Shanghai Sung Nan Textile Company Limited and Paofoong Insurance Company (Hong Kong) Limited. He is an economics graduate from the Cornell University and received a Master of Business Administration Degree in accounting and finance from the University of Chicago.

# Corporate Governance

## Corporate Governance Practices

The Board and the Management are committed to promoting good corporate governance to safeguard the interests of shareholders. The Company codified its corporate governance practices by reference to the Code on Corporate Governance Practices (the "Code") as set out in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Listing Rules"). The Company has applied the principles in the Code and complied with the code provisions set out in the Code throughout the year ended 31 December 2006.

## Directors' Securities Transactions

The Company has adopted a code of conduct regarding the Directors' transactions in the securities of the Company on terms no less exacting than the Model Code for Securities Transactions by Directors of Listed Issuers set out in Appendix 10 of the Listing Rules (the "Model Code"). Specific enquiry has been made of all the Directors of the Company and they have confirmed their compliance with the required standard set out in the Model Code and the Company's code of conduct in this respect throughout the year ended 31 December 2006 and up to the date of publication of this Annual Report.

## Board of Directors

The Board of Directors is accountable to the shareholders for the leadership and management and control of the business of the Company. The Board delegates to the Chief Executive Officer and his management team day-to-day management of the Company's business, including the preparation of annual and interim accounts and implementation of internal controls, in accordance with the strategy, policies and programs approved by the Board.

The members of the Board and their attendances at the four formal Board meetings scheduled during the financial year are set out as follows:

| | No. of meetings attended |
|---|---|
| **Chairman and Non-executive Director** | |
| Nicholas T. J. Colfer | 4/4 |
| **Chief Executive Officer and Executive Director** | |
| James H. Kaplan | 4/4 |
| **Non-executive Directors** | |
| Ian D. Boyce | 4/4 |
| Lincoln K. K. Leong | 2/4 |
| Nelson K. F. Leong<br>(Alternate Director to Lincoln K. K. Leong) | 3/4 |
| David C. L. Tong | 4/4 |
| John J. Ying | 3/4 |
| **Independent Non-executive Directors** | |
| Yvette Y. H. Fung | 3/4 |
| Michael T. H. Lee | 3/4 |
| Roderic N. A. Sage | 3/4 |
| Lincoln C. K. Yung | 3/4 |

## Chairman and Chief Executive Officer

The Chairman of the Board is Mr. Nicholas T. J. Colfer and the Chief Executive Officer is Mr. James H. Kaplan. To comply with code provision A.2.1 of the Code, the division of responsibilities between the Chairman and the Chief Executive Officer was formally set out in writing at the Board meeting on 23 September 2005. Essentially, the Chairman takes the lead to oversee the Board functions while the Chief Executive Officer, supported by his management team, is responsible for the day-to-day management of the business of the Company.

## Non-executive Directors

The Company's Non-executive Directors are not appointed for specific terms as required by code provision A.4.1 of the Code. However, at the Company's Annual General Meeting on 10 June 2005, in order to be more consistent with code provision A.4.1, the relevant Bye-law of the Company was amended to ensure that every director other than any Executive Chairman or Managing Director retire by rotation at least once every three years. The Executive Chairman or Managing Director cannot be required to retire by rotation in the Bye-laws as pursuant to section 2(e) of the Tai Ping Carpets International Limited Company Act 1990 of Bermuda. Notwithstanding this, the Directors intend to comply with code provision A.4.1 by asking any Executive Chairman or Managing Director to voluntarily retire by rotation at least once every three years.

Mr. Lincoln K. K. Leong and Mr. Nelson K. F. Leong (being Alternate Director to Mr. Lincoln K. K. Leong) are brothers. Save for this relationship, to the best knowledge of the Company, there are no other business, family or other material/relevant relationships among members of the Board.

The Company considers that its Non-executive Directors and Independent Non-executive Directors bring to the Board a good mix of expertise and experience in the fields of accounting, investment and business. At least one of the Independent Non-executive Directors has appropriate accounting or related financial management expertise as required under rule 3.10(2) of the Listing Rules. Pursuant to the requirements of the Listing Rules, each Independent Non-executive Director has given the Company an annual confirmation of his/her independence. The Company considers all the Independent Non-executive Directors to be independent with due regard to the guidelines as set out in rule 3.13 of the Listing Rules.

## Board Committees

Currently the Company has set up three board committees, namely, Executive Committee, Remuneration Committee, and Audit Committee.

### 1. Executive Committee

The Executive Committee was established in August 2005 and operates as an executive management committee under the Board to monitor and control the financial and operational performance of the Group. During the year under review, it held seven meetings and the attendances of the members were:

| | No. of meetings attended |
|---|---|
| Nicholas T. J. Colfer | 7/7 |
| James H. Kaplan | 7/7 |
| David C. L. Tong | 5/7 |
| John J. Ying | 6/7 |
| Nelson K. F. Leong | 5/7 |

**2. Remuneration Committee**

Written terms of reference for the Remuneration Committee in line with code provision B.1.3 of the Code were adopted at the Board meeting on 23 September 2005 and the majority of its members of the Committee are Independent Non-executive Directors, as required by code provision B.1.1 of the Code.

The roles and functions of the Remuneration Committee under its terms of reference are to:

- Make recommendation on the Company's policy and structure for remuneration of the Directors and senior executives
- Determine remuneration of all Executive Directors and senior executives
- Review and approve performance-based remuneration
- Review and approve compensation in connection with any loss or termination of office or appointment of any Executive Directors and senior executives

The members of the Remuneration Committee and their attendances at the meetings of the committee are set out below:

| | No. of meetings attended |
|---|---|
| Roderic N. A. Sage (Chairman) | 1/1 |
| Yvette Y. H. Fung | 1/1 |
| David C. L. Tong | 1/1 |

During the year under review, the Remuneration Committee held a meeting to determine the remuneration of the Executive Director, authorise the discretionary bonus payments to senior management, and approve the adoption of performance-based incentive plans for the Executive Director and senior management.

**3. Audit Committee**

Written terms of reference of the Audit Committee in line with code provision C.3.3 of the Code were adopted at the Board meeting on 23 September 2005.

Under these terms of reference, the responsibilities of the Audit Committee include overseeing the relationship with the Company's external auditors (including making recommendation to the Board on the appointment, re-appointment and removal of the external auditors, and approving the audit fee and reviewing the audit scope), review of financial information of the Group, oversight of the Group's financial reporting system and internal controls.

During the year under review, the Audit Committee held 3 meetings with management and the external auditors for reviewing the interim and annual reports before submission to the Board for consideration and approval, reviewing the annual audit plan and scope of work of both external auditors and internal auditors, and discussing issues arising from the audits including internal controls and financial reporting.

The composition of the Audit Committee and the attendances of the members are as follows:

| | No. of meetings attended |
|---|---|
| Roderic N. A. Sage (Chairman) | 2/3 |
| Michael T. H. Lee | 3/3 |
| John J. Ying | 2/3 |

## Nomination of Directors

The Company has not established a Nomination Committee for the time being. By virtue of the Company's Bye-laws, the Board has power from time to time to appoint any person as a Director. However, any Director so appointed shall hold office until the next General Meeting and shall then be eligible for re-election. In considering the nomination of a new Director, the Board will review the Board composition and evaluate the candidate's qualifications and experience before appointing him/her as a member of the Board.

During the year, there was no change in the composition of the Board.

## Auditors' Remuneration

For the year under review, the fees charged to the accounts of the Company and its subsidiaries by the Group's external auditors, BDO McCabe Lo Limited for services provided are analysed as follows:

| | (HK$'000) |
|---|---|
| Audit services | 2,082 |
| Non-audit services | 16 |

## Financial Reporting and Internal Controls

The consolidated accounts of the Company for the year ended 31 December 2006 have been reviewed by the Audit Committee and audited by the external auditor, BDO McCabe Lo Limited. The Directors acknowledge their responsibilities for preparing the consolidated accounts of the Company and they are not aware of any events or conditions that may cast significant doubt upon the Company's ability to continue as a going concern.

The independent auditor's report is on page 36.

The Board is responsible for maintaining an adequate system of internal control and for reviewing its effectiveness. The internal control system of the Group is designed to facilitate the effectiveness and efficiency of operations, safeguard assets against unauthorised use and disposition, ensure the maintenance of proper accounting records and the truth and fairness of the financial statements, and ensure compliance with relevant legislation and regulations. It provides reasonable, but not absolute, assurance against material misstatement or loss and manages rather than eliminates risks associated with its business activities.

During the year, an independent internal audit function was established, which has written terms of reference and reports directly to the Audit Committee. Internal Audit conducts reviews of the effectiveness of the Group's internal control system based on the internal audit plan and ad hoc requests from the Audit Committee and senior management. The annual internal audit plan is developed based on an assessment of the various business and operational risks of the Group and is approved by the Audit Committee. The Audit Committee reviews the findings and opinion of Internal Audit in respect of the effectiveness of the Group's internal control system periodically, and reports annually to the Board the key findings of such reviews.

# 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 1 January 2006 | Date of grant | Changes during the year Granted | Lapsed | Exercised | Balance as at 31 December 2006 | Exercise price (HK$) (Note) | Exercisable period |
|---|---|---|---|---|---|---|---|---|
| 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

# Financial Section



## Notes to the Accounts

# Independent Auditor's Report

**To the shareholders of Tai Ping Carpets International Limited**
(Incorporated in Bermuda with limited liability)

We have audited the financial statements of Tai Ping Carpets International Limited set out on pages 37 to 94, which comprise the consolidated and company balance sheet as at 31 December 2006, and the consolidated profit and loss account, the consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

## Directors' responsibility for the financial statements

The directors are responsible for the preparation and the true and fair presentation of these financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the disclosure requirements of Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

## Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. This report is made solely to you, as a body, in accordance with Section 90 of the Companies Act 1981 of Bermuda, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## Opinion

In our opinion, the financial statements give a true and fair view of the state of the affairs of the Company and of the Group as at 31 December 2006 and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

**BDO McCabe Lo Limited**
*Certified Public Accountants*

**Yip Li Yuet Fong, Jennifer**
*Practising Certificate no. P01039*
25th Floor, Wing On Centre
111 Connaught Road Central, Hong Kong

Hong Kong, 20 April 2007

# Consolidated Profit and Loss Account

For the year ended 31 December

| | Note | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|---|
| Continuing Operations | | | |
| Turnover | 5 | **900,026** | 709,432 |
| Cost of sales | | **(514,937)** | (432,587) |
| Gross profit | | **385,089** | 276,845 |
| Interest income | 6 | **1,643** | 1,101 |
| Gain/(loss) on disposal of investment properties | | **1,294** | (470) |
| Gain on liquidation of an available-for-sale financial asset | | **—** | 21,084 |
| Gain on disposal of a jointly controlled entity | | **—** | 7,692 |
| Surplus on revaluation of investment properties | 17 | **6,486** | 15,648 |
| Distribution costs | | **(74,648)** | (60,409) |
| Administrative expenses | | **(286,389)** | (228,510) |
| Other operating income | | **3,557** | 1,729 |
| Other operating expenses | | **(5,024)** | (5,920) |
| Operating profit | 5, 7 | **32,008** | 28,790 |
| Finance costs | 8 | **(3,912)** | (3,578) |
| Share of profits/(losses) of | | | |
| an associate | | **220** | (69) |
| jointly controlled entities | | **27,959** | 24,343 |
| add: Reversal of impairment of jointly controlled entities | | **2,900** | — |
| Profit before income tax expenses | | **59,175** | 49,486 |
| Income tax expenses | 10 | **(18,191)** | (11,728) |
| Profit after income tax expenses from continuing operations | | **40,984** | 37,758 |
| Discontinued Operation | | | |
| Loss after income tax expenses from discontinued operation | 11 | **(3,964)** | (3,304) |
| Profit after income tax expenses | | **37,020** | 34,454 |
| | | | |
| Attributable to: | | | |
| Equity holders of the Company | 12 | **32,694** | 27,646 |
| Minority interests | | **4,326** | 6,808 |
| | | **37,020** | 34,454 |
| Dividend | | | |
| - Interim | | **—** | — |
| - Final, proposed | 13 | **6,366** | — |
| | | **6,366** | — |
| Earnings/(loss) per share of profit/(loss) attributable to equity holders of the Company (expressed in HK cents) | | | |
| From continuing and discontinued operations | | | |
| - Basic | 14 | **15.41** | 13.04 |
| - Diluted | 14 | **15.41** | 13.04 |
| From continuing operations | | | |
| - Basic | 14 | **17.28** | 14.60 |
| - Diluted | 14 | **17.28** | 14.60 |
| From discontinued operation | | | |
| - Basic | 14 | **(1.87)** | (1.56) |
| - Diluted | 14 | **(1.87)** | (1.56) |

# Consolidated Balance Sheet

As at 31 December

| | Note | 2006<br>HK$'000 | 2005<br>HK$'000 |
|---|---|---|---|
| **Assets** | | | |
| **Non-current assets** | | | |
| Leasehold land and land use rights | 15 | **21,588** | 21,739 |
| Property, plant and equipment | 16 | **317,092** | 303,440 |
| Investment properties | 17 | **36,800** | 73,130 |
| Construction in progress | 18 | **7,993** | 12,282 |
| Interest in an associate | 21 | **21,682** | 21,166 |
| Interests in jointly controlled entities | 22 | **157,705** | 133,318 |
| Available-for-sale financial assets | | **—** | 134 |
| Net investment in finance leases | 24 | **—** | 210 |
| Deferred tax assets | 33 | **6,631** | 1,983 |
| | | **569,491** | 567,402 |
| **Current assets** | | | |
| Inventories | 25 | **211,858** | 173,847 |
| Trade and other receivables | 26 | **178,404** | 161,658 |
| Current portion of net investment in finance leases | 24 | **—** | 735 |
| Derivative financial instruments | 27 | **681** | — |
| Properties held for sale | 28 | **4,436** | — |
| Financial assets at fair value through profit or loss | 23 | **23,809** | — |
| Cash and cash equivalents | 29 | **58,976** | 87,079 |
| | | **478,164** | 423,319 |
| **Total assets** | | **1,047,655** | 990,721 |

| | Note | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|---|
| **Equity** | | | |
| **Capital and reserves attributable to equity holders of the Company** | | | |
| Share capital | 30 | **21,219** | 21,193 |
| Reserves | 31 | **746,276** | 662,414 |
| Proposed final dividend | 13 | **6,366** | — |
| | | **773,861** | 683,607 |
| **Minority interests** | | **33,204** | 27,864 |
| **Total equity** | | **807,065** | 711,471 |
| **Liabilities** | | | |
| **Non-current liabilities** | | | |
| Bank borrowings – unsecured | 32 | — | 9,500 |
| Deferred tax liabilities | 33 | **2,602** | 5,632 |
| Other long-term liabilities | 34 | **1,601** | 1,991 |
| | | **4,203** | 17,123 |
| **Current liabilities** | | | |
| Bank borrowings – unsecured | 32 | **11,000** | 99,836 |
| Trade and other payables | 35 | **201,520** | 153,016 |
| Other long-term liabilities – current portion | 34 | **390** | 390 |
| Taxation | | **23,477** | 8,885 |
| | | **236,387** | 262,127 |
| **Total liabilities** | | **240,590** | 279,250 |
| **Total equity and liabilities** | | **1,047,655** | 990,721 |
| **Net current assets** | | **241,777** | 161,192 |
| **Total assets less current liabilities** | | **811,268** | 728,594 |

**Nicholas T. J. Colfer**
*Chairman*

**James H. Kaplan**
*Executive Director*

# Company Balance Sheet

As at 31 December

| | Note | 2006<br>HK$'000 | 2005<br>HK$'000 |
|---|---|---|---|
| **Assets** | | | |
| **Non-current assets** | | | |
| Interests in subsidiaries | 19 | **306,093** | 308,878 |
| **Current assets** | | | |
| Other receivables | | **—** | 518 |
| Amount due from an indirectly held associate | 20 | **343** | 343 |
| Cash and cash equivalents | 29 | **255** | 232 |
| | | **598** | 1,093 |
| **Total assets** | | **306,691** | 309,971 |
| **Equity** | | | |
| **Capital and reserves attributable to equity holders of the Company** | | | |
| Share capital | 30 | **21,219** | 21,193 |
| Reserves | 31 | **277,852** | 287,656 |
| Proposed final dividend | 13, 31 | **6,366** | — |
| **Total Equity** | | **305,437** | 308,849 |
| **Liabilities** | | | |
| **Current liabilities** | | | |
| Other payables | | **1,254** | 1,122 |
| **Total liabilities** | | **1,254** | 1,122 |
| **Total equity and liabilities** | | **306,691** | 309,971 |
| **Net current liabilities** | | **(656)** | (29) |
| **Total assets less current liabilities** | | **305,437** | 308,849 |

**Nicholas T. J. Colfer**
*Chairman*

**James H. Kaplan**
*Executive Director*

# Consolidated Statement of Changes in Equity

## For the year ended 31 December 2006

| | | Attributable to equity holders of the Company | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Note | Share capital HK$'000 | Share premium HK$'000 | Capital reserves HK$'000 | Other properties revaluation reserves HK$'000 | General reserves HK$'000 | Exchange reserves HK$'000 | Retained earnings HK$'000 | Proposed final dividend HK$'000 | Capital and reserves HK$'000 | Minority interests HK$'000 | Total equity HK$'000 |
| Balance at 1 January 2006 | | 21,193 | 189,417 | 88,725 | 4,821 | 16,000 | 2,908 | 360,543 | — | 683,607 | 27,864 | 711,471 |
| Currency translation differences | | — | — | — | — | — | 57,861 | — | — | 57,861 | 1,229 | 59,090 |
| Capital reserve released on disposal of an investment property | | — | — | (17,077) | — | — | — | 17,077 | — | — | — | — |
| Reversal of deferred tax on other properties | | — | — | — | (660) | — | — | — | — | (660) | — | (660) |
| Appropriation to the reserves | | — | — | 153 | — | — | — | (153) | — | — | — | — |
| Net income recognised directly in equity | | — | — | (16,924) | (660) | — | 57,861 | 16,924 | — | 57,201 | 1,229 | 58,430 |
| Profit for the year | | — | — | — | — | — | — | 32,694 | — | 32,694 | 4,326 | 37,020 |
| Net income recognised for the year | | — | — | (16,924) | (660) | — | 57,861 | 49,618 | — | 89,895 | 5,555 | 95,450 |
| Repayment of amounts to minority interests | | — | — | — | — | — | — | — | — | — | (29) | (29) |
| Dividend paid to minority interests | | — | — | — | — | — | — | — | — | — | (186) | (186) |
| Employee share options scheme: value of employee services | | — | — | 51 | — | — | — | — | — | 51 | — | 51 |
| Proceeds from shares issued | 30, 31 | 26 | 282 | — | — | — | — | — | — | 308 | — | 308 |
| Proposed final dividend | | — | — | — | — | — | — | (6,366) | 6,366 | — | — | — |
| | | 26 | 282 | 51 | — | — | — | (6,366) | 6,366 | 359 | (215) | 144 |
| Balance at 31 December 2006 | | 21,219 | 189,699 | 71,852 | 4,161 | 16,000 | 60,769 | 403,795 | 6,366 | 773,861 | 33,204 | 807,065 |

Note: The capital reserves included statutory reserve funds set up by subsidiaries and jointly controlled entities in the Mainland China. According to the relevant laws and financial regulations, upon approval by the Board, the statutory reserve funds may be used to make up prior years' losses, if any, and to increase the capital of such subsidiaries and jointly controlled entities.

Consolidated Statement of Changes in Equity (Continued)

## For the year ended 31 December 2005

| | Note | Share capital HK$'000 | Share premium HK$'000 | Capital reserves HK$'000 | Other properties revaluation reserves HK$'000 | Available for-sale revaluation reserves HK$'000 | General reserves HK$'000 | Exchange reserves HK$'000 | Retained earnings HK$'000 | Capital and reserves HK$'000 | Minority interests HK$'000 | Total equity HK$'000 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Attributable to equity holders of the Company | | | | | | | | | | |
| Balance at 1 January 2005 | | 21,170 | 189,162 | 88,861 | 5,128 | 6,505 | 16,000 | 15,118 | 332,983 | 674,927 | 20,794 | 695,721 |
| Currency translation differences | | — | — | (398) | (307) | — | — | (12,210) | — | (12,915) | 262 | (12,653) |
| Changes in fair value of available-for-sale financial assets | | — | — | — | — | 6,420 | — | — | — | 6,420 | — | 6,420 |
| Release of reserve upon liquidation of an available-for-sale financial asset | | — | — | — | — | (12,925) | — | — | — | (12,925) | — | (12,925) |
| Appropriation to the reserves | | — | — | 86 | — | — | — | — | (86) | — | — | — |
| Net income recognised directly in equity | | — | — | (312) | (307) | (6,505) | — | (12,210) | (86) | (19,420) | 262 | (19,158) |
| Profit for the year | | — | — | — | — | — | — | — | 27,646 | 27,646 | 6,808 | 34,454 |
| Net income recognised for the year | | — | — | (312) | (307) | (6,505) | — | (12,210) | 27,560 | 8,226 | 7,070 | 15,296 |
| Employee share options scheme: value of employee services | | — | — | 176 | — | — | — | — | — | 176 | — | 176 |
| Proceeds from shares issued | 30, 31 | 23 | 255 | — | — | — | — | — | — | 278 | — | 278 |
| | | 23 | 255 | 176 | — | — | — | — | — | 454 | — | 454 |
| Balance at 31 December 2005 | | 21,193 | 189,417 | 88,725 | 4,821 | — | 16,000 | 2,908 | 360,543 | 683,607 | 27,864 | 711,471 |

# Consolidated Cash Flow Statement

For the year ended 31 December

| | Note | 2006<br>HK$'000 | 2005<br>HK$'000 |
|---|---|---|---|
| Operating activities | | | |
| Cash generated from/(used in) operations | a | **75,820** | (1,164) |
| Tax paid | | **(14,874)** | (10,103) |
| Net cash generated from/(used in) operating activities | | **60,946** | (11,267) |
| Investing activities | | | |
| Purchases of property, plant and equipment | | **(15,168)** | (22,404) |
| Increase in construction in progress | | **(17,493)** | (41,414) |
| Proceeds on disposal of property, plant and equipment | | **2,165** | 630 |
| Proceeds on disposal of investment properties | | **43,714** | 28,185 |
| Proceeds on disposal of subsidiaries, less cash disposed | b | **14,389** | — |
| Proceeds on disposal of available-for-sale financial assets | | **137** | — |
| Proceeds on disposal of financial assets held for trading | | **—** | 3,147 |
| Proceeds on disposal of a jointly controlled entity | | **—** | 7,692 |
| Repayment of finance lease receivables | | **657** | 1,346 |
| Repayment by/(advance to) an associate | | **1,212** | (781) |
| Repayment by/(advance to) jointly controlled entities | | **5,363** | (11,479) |
| Purchase of financial assets at fair value through profit or loss | | **(22,727)** | — |
| Interest received | | **1,643** | 1,165 |
| Dividend received from an associate | | **—** | 891 |
| Dividend received from jointly controlled entities | | **6,719** | 17,925 |
| Dividend received from an available-for-sale financial asset | | **—** | 17 |
| Net cash generated from/(used in) investing activities | | **20,611** | (15,080) |
| Financing activities | | | |
| New shares issued | | **308** | 278 |
| New bank loans | | **—** | 40,690 |
| Repayment of bank loans | | **(107,503)** | — |
| Repayment of other long-term liabilities | | **(390)** | (390) |
| Interest paid | | **(3,912)** | (3,578) |
| Dividend paid to minority interests | | **(186)** | — |
| Repayment of amounts due to minority interests | | **(29)** | — |
| Net cash (used in)/generated from financing activities | | **(111,712)** | 37,000 |
| Net (decrease)/increase in cash and cash equivalents | | **(30,155)** | 10,653 |
| Cash and cash equivalents at the beginning of the year | | **87,079** | 76,965 |
| Effect of foreign exchange rate changes | | **2,052** | (539) |
| Cash and cash equivalents at the end of the year | | **58,976** | 87,079 |
| Analysis of the balances of cash and cash equivalents | | | |
| Cash at bank and on hand | 29 | **55,013** | 83,738 |
| Short-term bank deposits | 29 | **3,963** | 3,341 |
| | | **58,976** | 87,079 |

**a. Reconciliation of profit after income tax expenses to cash generated from/(used in) operations**

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Profit after income tax expenses | **37,020** | 34,454 |
| Income tax expenses recognised in consolidated profit and loss account | **18,533** | 10,845 |
| Depreciation of property, plant and equipment | **45,826** | 39,932 |
| Amortisation of leasehold land and land use rights | **532** | 408 |
| Net (gain)/loss on disposal of property, plant and equipment | **(137)** | 92 |
| Net (gain)/loss on disposal of investment properties | **(1,294)** | 470 |
| Share of (profits)/losses of | | |
| an associate | **(220)** | 69 |
| jointly controlled entities | **(27,959)** | (24,343) |
| Reversal of impairment of jointly controlled entities | **(2,900)** | — |
| Surplus on revaluation of investment properties | **(6,486)** | (15,648) |
| Loss on disposal of subsidiaries | **5,498** | — |
| Impairment of inventories | **1,236** | 6,423 |
| Impairment of property, plant and equipment | **312** | — |
| Impairment of construction in progress | **—** | 4,470 |
| Impairment of/(reversal of impairment of) | | |
| trade and other receivables | **2,874** | (139) |
| Profit on disposal of financial assets held for trading | **—** | (17) |
| Loss on disposal of an available-for-sale financial asset | **56** | — |
| Increase in derivative financial instruments | **(649)** | — |
| Gain on disposal of a jointly controlled entity | **—** | (7,692) |
| Write-off of an available-for-sale financial asset | **—** | 114 |
| Gain on liquidation of an available-for-sale financial asset | **—** | (21,084) |
| Employee share options expenses | **51** | 176 |
| Dividend income from an available-for-sale financial asset | **—** | (17) |
| Interest expenses | **3,912** | 3,578 |
| Interest income | **(1,643)** | (1,165) |
| Operating profit before working capital changes | **74,562** | 30,926 |
| Increase in inventories | **(28,783)** | (30,978) |
| Increase in trade and other receivables | **(22,614)** | (45,710) |
| Increase in trade and other payables | **53,679** | 45,453 |
| Increase in net investment in finance leases | **(1,024)** | (855) |
| Cash generated from/(used in) operations | **75,820** | (1,164) |

**b. Disposal of subsidiaries**

The assets and liabilities of the subsidiaries disposed consisted of the following:

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Property, plant and equipment | **5,148** | — |
| Inventories | **6,693** | — |
| Trade and other receivables | **12,891** | — |
| Cash and cash equivalents | **4,811** | — |
| Net investment in finance leases | **1,312** | — |
| Deferred tax assets | **819** | — |
| Trade and other payables | **(6,976)** | — |
| | **24,698** | — |
| Less: Loss on disposal of subsidiaries | **(5,498)** | — |
| Total cash consideration | **19,200** | — |
| | | |
| Net cash inflow arising on disposal : | | |
| Proceeds on disposal of subsidiaries | **19,200** | — |
| Less: Cash of subsidiaries disposed | **(4,811)** | — |
| | **14,389** | — |

## 1. General Information

Tai Ping Carpets International Limited (the "Company") and its subsidiaries (collectively known as the "Group") are principally engaged in the manufacture, import, export and sale of carpets, manufacture and sale of yarns, manufacture and sale of mattresses, and property holding. During the year, the Group ceased its operation in interior furnishings in Hong Kong.

The Company is a limited liability company incorporated in Bermuda. The address of its registered office is Canon's Court, 22 Victoria Street, P.O. Box HM 1179, Hamilton HM EX, Bermuda. The principal office in Hong Kong is located at 26/F, Tower A, Regent Centre, 63 Wo Yi Hop Road, Kwai Chung, Hong Kong.

The Company's shares are listed on the Main Board of the The Stock Exchange of Hong Kong Limited.

The consolidated accounts are presented in thousands of Hong Kong dollars (HK$'000), unless otherwise stated, and have been approved and authorised for issue by the Board of Directors on 20 April 2007.

## 2. Summary of Significant Accounting Policies

The principal accounting policies applied in the preparation of these consolidated accounts are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

### 2.1 Basis of preparation

The consolidated accounts have been prepared in accordance with Hong Kong Financial Reporting Standards and Interpretations ("collectively known as HKFRS") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"). In addition, the consolidated accounts include the appropriate disclosures required by the Rules Govering the Listing of Securities on The Stock Exchange of Hong Kong Limited and the Hong Kong Companies Ordinance. The consolidated accounts have been prepared under the historical cost convention except for (i) certain buildings which are stated at revalued amounts less subsequent accumulated depreciation and accumulated impairment losses; and (ii) available-for-sale financial assets, financial assets held at fair value through profit or loss, and investment properties, which are carried at fair value.

In the current year, the Group also applied, for the first time, the following new standards, amendments and interpretations issued by the HKICPA (hereinafter collectively referred to as the "new HKFRSs") that are effective for the accounting periods beginning on or after 1 December 2005 or 1 January 2006.

**HKAS 19 Amendment**
Actuarial gains and losses, Group plans and disclosures

**HKAS 21 Amendment**
Net investment in a foreign operation

**HKAS 39 Amendment**
Cash flow hedge accounting of forecast intragroup transactions

**HKAS 39 Amendment**
The fair value option

**HKAS 39 & HKFRS 4 Amendments**
Financial guarantee contracts

**HKFRS 6**
Exploration for and evaluation of mineral resources

**HK(IFRIC) — Interpretation 4**
Determining whether an arrangement contains a lease

**HK(IFRIC) — Interpretation 5**
Rights to interests arising from decommissioning, restoration and environmental rehabilitation funds

**HK(IFRIC) — Interpretation 6**
Liabilities arising from participating in a specific market — waste electrical and electronic equipment

The adoption of the above new HKFRSs has had no material effect on how the results for the current or prior accounting periods have been prepared and presented. Accordingly, no prior period adjustment is required.

The Group has not applied for the early adoption of the following new standards, amendments and interpretations that have been issued but are not yet effective. The Group is in the process of making an assessment of the impact of these new standards, amendments and interpretations to the Group's results of operations and financial position in the period of initial application.

| | Effective for accounting periods beginning on or after |
|---|---|
| **HKAS 1 (Amendment)**<br>Capital disclosures | 1 January 2007 |
| **HKFRS 7**<br>Financial instruments: disclosure | 1 January 2007 |
| **HKFRS 8**<br>Operating segments | 1 January 2009 |
| **HK(IFRIC) — Interpretation 7**<br>Applying the restatement approach under HKAS 29 financial reporting in hyperinflationary economies | 1 March 2006 |
| **HK(IFRIC) — Interpretation 8**<br>Scope of HKFRS 2 | 1 May 2006 |
| **HK(IFRIC) — Interpretation 9**<br>Reassessment of embedded derivatives | 1 June 2006 |
| **HK(IFRIC) — Interpretation 10**<br>Interim financial reporting and impairment | 1 November 2006 |
| **HK(IFRIC) — Interpretation 11**<br>Group and treasury share transactions | 1 March 2007 |
| **HK(IFRIC) — Interpretation 12**<br>Service concession arrangements | 1 January 2008 |

The preparation of the accounts in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgments in the process of applying the Group' s accounting policies. The areas involving a higher degree of judgment or complexity or areas where assumptions and estimates are significant to the consolidated accounts, are disclosed in Note 4.

### 2.2 Consolidation

The consolidated accounts include the accounts of the Company and all its subsidiaries made up to 31 December.

#### (a) Subsidiaries

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the consolidated profit and loss account.

In the Company's balance sheet the investments in subsidiaries are stated at cost less provision for impairment losses. The results of subsidiaries are accounted by the Company on the basis of dividend received and receivable.

**(b) Transactions with minority interests**

The Group applies a policy of treating transactions with minority interests as transactions with parties external to the Group. Disposals to minority interests result in gains and losses for the Group that are recorded in the consolidated profit and loss account. Purchases from minority interests result in goodwill, being the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary.

**(c) An associate and jointly controlled entities**

An associate is an entity over which the Group has significant influence but does not have control or joint control.

A jointly controlled entity involves the establishment of a corporation, partnership or other entity in which each venturer has an interest. The entity operates in the same way as other entities, except that a contractual arrangement between the venturers establishes joint control over the economic activity of the entity.

Investments in an associate and jointly controlled entities are accounted for using the equity method of accounting and are initially recognised at cost. The Group's investments in an associate and jointly controlled entities includes goodwill (net of any accumulated impairment loss) identified on acquisition.

The Group's share of the post-acquisition profits or losses of an associate and jointly controlled entities is recognised in the consolidated profit and loss account, and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investments. When the Group' s share of losses in the associate or jointly controlled entities equals or exceeds its interest in such associate or jointly controlled entities, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate or jointly controlled entities.

Unrealised gains on transactions between the Group and its associate and jointly controlled entities are eliminated to the extent of the Group's interest in the associate and jointly controlled entities. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of the associate and jointly controlled entities are changed where necessary to ensure consistency with the policies adopted by the Group.

On the Company's balance sheet, the investments in an associate and jointly controlled entities are stated at cost less provision for impairment losses. The results of the associate and jointly controlled entities are accounted for by the Company on the basis of dividends received and receivable.

**2.3 Segment reporting**

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that is subject to risks and returns that are different from those of segments operating in other economic environments.

In accordance with the Group's internal financial reporting the Group has determined that business segments be presented as the primary reporting format and geographical as the secondary reporting format.

Unallocated costs represent corporate expenses. Segment assets consist primarily of intangible assets, property, plant and equipment, leasehold land and land use rights, investment properties, construction in progress, inventories, receivables and operating cash, and mainly exclude investment in an associate and investment in jointly controlled entities. Segment liabilities comprise operating liabilities and exclude items such as tax liabilities, deferred taxation, and bank borrowings. Capital expenditure comprises additions to property, plant and equipment, leasehold land and land use rights, investment properties, construction in progress, and additions resulting from acquisition through purchases of subsidiaries including goodwill.

In respect of geographical segment reporting, sales are based on the country in which the customer is located, and total assets and capital expenditure are where the assets are located.

**2.4 Foreign currency translation**

**(a) Functional and presentation currency**

Items included in the accounts of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated accounts are presented in Hong Kong dollar, which is the Company's functional and presentation currency.

**(b) Transactions and balances**

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated profit and loss account.

**(c) Group companies**

The results and financial position of all the group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

(i) assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;

(ii) income and expenses for each profit and loss account are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and

(iii) all resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign operation, and of borrowings, are taken to shareholders' equity. When a foreign operation is sold, exchange differences that were recorded in equity are recognised in the consolidated profit and loss account as part of the gain or loss on sale.

Goodwill and fair value adjustments on the identifiable assets acquired arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

**2.5 Property, plant and equipment**

Buildings comprise mainly factories, retail outlets and offices. They are stated at cost or valuation less accumulated depreciation and impairment losses. Certain buildings were at valuation which was carried out prior to 30 September 1995. Under transitional provision in paragraph 80A of HKAS 16, the Group is not required to make regular revaluations in accordance with paragraphs 31 and 36 of HKAS 16. All other property, plant and equipment are stated at historical cost less accumulated depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repair and maintenance costs are expensed in the consolidated profit and loss account during the financial period in which they are incurred.

Depreciation of property, plant and equipment is calculated using the straight-line method to allocate cost or revalued amounts to their residual values over their estimated useful lives, at the following annual rates:

| | |
|---|---|
| Buildings | 2% – 4.5% |
| Plant and machinery | 8% – 20% |
| Furniture, fixtures and equipment | 6% – 25% |
| Motor vehicles | 18% – 20% |

Construction-in-progress, representing building on which construction work has not been completed, is stated at cost, which includes construction expenditures incurred and other direct costs capitalised during the construction period, less accumulated impairment losses. No depreciation is provided in respect of construction-in-progress until the construction work is completed. On completion, the construction in progress is transferred to appropriate categories of property, plant and equipment.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

The asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2.7).

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the consolidated profit and loss account. When revalued assets are sold, the amounts included in other reserves are transferred to retained earnings.

**2.6 Investment properties**

Property that is held for long-term rental yields or for capital appreciation or both, and that is not occupied by Group companies, is classified as investment property.

Investment properties comprise land held under operating leases and buildings held under finance leases.

Land held under operating leases is classified and accounted for as an investment property when the rest of the definition of investment property is met. The operating lease is accounted for as if it were a finance lease.

Investment property is measured initially at its cost, including related transaction costs.

After initial recognition, investment property is carried at fair value. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset. If this information is not available, the Group uses alternative valuation methods such as recent prices on less active markets or discounted cash flow projections. These valuations are performed in accordance with the guidance issued by the International Valuation Standards Committee. These valuations are reviewed annually by external valuers. Investment property that is being redeveloped for continuing use as investment property, or for which the market has become less active, continues to be measured at fair value.

The fair value of investment property reflects, among other things, rental income from current leases and assumptions about rental income from future leases in the light of current market conditions.

The fair value also reflects, on a similar basis, any cash outflows that could be expected in respect of the property. Some of those outflows are recognised as a liability, including finance lease liabilities in respect of land classified as investment property; others, including contingent rent payments, are not recognised in the financial statements.

Subsequent expenditure is charged to the asset's carrying amount only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repair and maintenance costs are expensed in the consolidated profit and loss account during the financial period in which they are incurred.

Changes in fair value are recognised in the consolidated profit and loss account.

If an investment property becomes owner-occupied, it is reclassified as property, plant and equipment, and its fair value at the date of reclassification becomes its cost for accounting purposes. Property that is being constructed or developed for future use as investment property is classified as property, plant and equipment and stated at cost until construction or development is complete, at which time it is reclassified and subsequently accounted for as investment property.

If an item of property, plant and equipment becomes an investment property because its use has changed, any difference resulting between the carrying amount and the fair value of this item at the date of transfer is recognised in equity as a revaluation of property, plant and equipment under HKAS 16. However, if a fair value gain reverses a previous impairment loss, the gain is recognised in the consolidated profit and loss account.

Investment property held for sale without redevelopment is classified within non-current assets held for sale, under HKFRS 5.

**2.7 Impairment of assets**

Assets that have an indefinite useful life are not subject to amortisation, but are at least tested annually for impairment and are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

**2.8 Financial assets and liabilities**

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables, and available-for-sale financial assets. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition and re-evaluates this designation at every reporting date.

**(a) Financial assets at fair value through profit or loss**

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives are also categorised as held for trading unless they are designated as hedges. Assets in this category are classified as current assets if they are either held for trading or are expected to be realised within 12 months of the balance sheet date.

**(b) Loans and receivables**

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. Loans and receivables are included as trade and other receivables in the balance sheet. Please refer to Note 2.10.

**(c) Available-for-sale financial assets**

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date.

Purchases and sales of investments are recognised on trade date — the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Investments are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables are carried at amortised cost using the effective interest method.

Unrealised and realised gains and losses arising from changes in the fair value of the financial assets at fair value through profit or loss category including interest and dividend income, are included in the consolidated profit and loss account within other operating income/expenses in the period in which they arise.

Unrealised gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised in equity. When available-for-sale financial assets are sold or impaired, the accumulated fair value adjustments are included in the consolidated profit and loss account.

The fair value of quoted investments is based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, and option pricing models, making maximum use of market inputs and relying as little as possible on entity-specific inputs.

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity securities classified as available-for-sale, a significant or prolonged decline in the fair value of the securities below their cost is considered an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss — measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in the consolidated profit and loss account is removed from equity and recognised in the consolidated profit and loss account. Impairment losses recognised in the consolidated profit and loss account on equity instruments are not reversed through the consolidated profit and loss account.

**(d) Trade and other payables**

Trade payables and other short-term monetary liabilities are recognised at amortised cost.

### 2.9 Inventories

Inventories are stated at the lower of cost and net realisable value. The cost of finished goods and work-in-progress, which is determined principally on the weighted average basis, comprises design costs, raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity). It excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

### 2.10 Trade and other receivables

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The amount of the impairment is recognised in the consolidated profit and loss account.

### 2.11 Cash and cash equivalents

Cash and cash equivalents include cash on hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less.

### 2.12 Bank borrowings

Bank borrowings are recognised initially at fair value, net of transaction costs incurred. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability, including fees and commissions paid to agents, advisers, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the consolidated profit and loss account over the period of the borrowings using the effective interest method.

Bank borrowings are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expires.

Bank borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

### 2.13 Income tax

Income taxes for the year comprise current tax and deferred tax.

Current tax is based on the profit or loss from ordinary activities adjusted for items that are non-assessable or disallowable for income tax purposes and is calculated using tax rates that have been enacted or substantively enacted at the balance sheet date.

Income taxes are recognised in the profit and loss account except when they relate to items directly recognised to equity in which case the taxes are also directly recognised in equity.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated accounts. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, an associate and jointly controlled entities, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary differences will not reverse in the foreseeable future.

**2.14 Employee benefits**

**(a) Employee leave entitlements**

Salaries, bonus, paid annual leave and the cost of other benefits to the Group are accrued in the year in which the associated services are rendered by employees of the Group.

**(b) Profit sharing and bonus plans**

The expected cost of profit sharing and bonus payments is recognised as a liability when the Group has a present legal or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made.

Liabilities for profit sharing and bonus plans are expected to be settled within 12 months and are measured as the amounts expected to be paid when they are settled.

**(c) Pensions obligations**

The Group operates a number of defined contribution plans (the "Plans") throughout the world, the assets of which are held in separate trustee-administered funds. The Plans are generally funded by payments from employees and by the relevant Group companies. The Group's contributions to the Plans are expensed as incurred and are reduced by contributions forfeited by those employees who leave the Plans prior to contributions vesting fully.

In Hong Kong, the Group operates a Mandatory Provident Fund Scheme (the "Scheme") for all Hong Kong employees. Under the Scheme, employees are required to contribute 5% of their monthly basic salaries whereas the Group's monthly contribution will depend on the employees' years of service, subject to a minimum of 5% of relevant income up to HK$20,000.

**(d) Share-based compensation**

The Group operates an equity-settled, share-based compensation plan. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example, profitability and sales growth targets). Non-market vesting conditions are included in assumptions about the number of options that are expected to become exercisable. At each balance sheet date, the entity revises its estimates of the number of options that are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment to equity over the remaining vesting period.

The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised.

**2.15 Leases**

**(a) Finance lease**

(The Group as lessor)

Leases of assets where the Group has substantially all the risks and rewards of ownership are classified as finance leases. When assets are leased out under a finance lease, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognised over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

**(b) Operating lease**

(The Group as both lessor and lessee)

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged in the consolidated profit and loss account on a straight-line basis over the period of the lease.

Assets leased out under operating leases are included in property, plant and equipment in the balance sheet. They are depreciated over their expected useful lives on a basis consistent with similar owned property, plant and equipment. Rental income (net of any incentives given to lessees) is recognised on a straight-line basis over the lease terms.

**2.16 Revenue recognition**

Revenue comprises the fair value for the sale of goods and services in the ordinary course of the Group's activities. Revenue is shown, net of value-added tax, and discounts and after eliminating sales within the Group. Revenue is recognised as follows:

(a) Revenue from sales of carpets, yarns, underlays and interior furnishings is recognised on the transfer of risks and rewards of ownership, which generally coincides with the time when the goods are delivered to customers and title has passed.

(b) Revenue from installation of carpets is recognised in the accounting period in which the installation services are rendered, by reference to completion of the specific transaction assessed on the basis of the actual service provided.

(c) Rental income from investment properties and interior furnishings is recognised on a straight line basis over the lease term.

(d) Interest income is recognised on a time-proportion basis using the effective interest method. When a receivable is impaired, the Group reduces the carrying amount to its recoverable amount, being the estimated future cash flow discounted at original effective interest rate of the instrument, and continues unwinding the discount as interest income. Interest income on impaired loans is recognised using the original effective interest rate.

(e) Dividend income is recognised when the right to receive payment is established.

**2.17 Dividend distribution**

Dividend distribution to the Company's shareholders is recognised as a liability in the accounts in the period in which the dividend is approved by the Company's shareholders.

Final dividend proposed by the Directors is classified as a separate allocation of retained earnings within capital and reserves on the balance sheet. Final dividend is recognised as a liability when it is approved by the shareholders.

## 3. Financial Risk Management

The Group is subject to the following market risks:

**(a) Foreign exchange risk**

The Group operates internationally and is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the Hong Kong dollar. Foreign exchange risk arises from future commercial transactions, recognised assets and liabilities and net investments in foreign operations. Management monitors exchange rate movements closely to ascertain if any material exposure may arise.

**(b) Credit risk**

The Group has no significant concentrations of credit risk as the Group has a large number of customers, internationally dispersed. Sales to retail customers are made in cash or via major credit cards. For project sales, the Group will request the customers for initial deposits and will accept orders only from those customers with an appropriate credit history. The Group also performs periodic assessment of the trade receivables and believes that adequate provision for uncollectible receivables has been made.

**(c) Liquidity risk**

Prudent liquidity risk management implies maintaining sufficient cash and marketable securities, the availability of funding through an adequate amount of committed credit facilities and the ability to close out market positions. Due to the dynamic nature of the underlying businesses, Management aims to maintain flexibility in funding by keeping committed credit lines available.

**(d) Interest rate risk**

The Group is exposed to changes in interest rates due to its bank borrowings. The Group enters into debt obligations to support general corporate purposes including capital expenditure and working capital needs. The Group does not use any derivative instruments to reduce its economic exposure to changes in interest rates.

**(e) Raw material price risk**

The major operation of the Group includes manufacture of carpets and the raw materials used in the production include wool, silk and dyestuff. The production process includes the use of petro products, including fuel and dyestuff. Therefore the Group's gross margin is exposed to the fluctuation in the prices of raw materials and petro products. The Group does not use any derivative instruments to reduce its exposures to such risks.

**(f) Fair values estimation**

The Group has investment properties in Hong Kong and the Mainland China. In accordance with HKAS 40 "Investment properties", all investment properties are carried at fair value. The fair value is based on active market prices which in turn depend on the property market conditions and the economic environment in the area at which such properties are located. As the movements in the fair value of investment properties are recognised in the consolidated profit and loss, the Group's results are exposed to the risk of fluctuation of such fair values.

The nominal value less estimated credit adjustment of receivables and payables approximates their fair value.

## 4. Critical Accounting Estimates and Judgments

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

### (a) Useful lives and impairment of property, plant and equipment

The Group's management determines the estimated useful lives of its property, plant and equipment.

This estimate is based on the historical experience of the actual useful lives of property, plant and equipment of similar nature and functions. Management will increase the depreciation charge where useful lives are less than previously estimated lives, and will write-off or write-down technically obsolete or non-strategic assets that have been abandoned or sold.

The impairment loss for property, plant and equipment is recognised as the amount by which the carrying amount exceeds its recoverable amount in accordance with the accounting policy stated in Note 2.7. The recoverable amounts have been determined based on fair value less costs to sell, which are based on the best information available to reflect the amount obtainable at each balance sheet date, from the disposal of the asset in an arm's length transaction between knowledgeable, willing parties, after deducting the costs to disposal.

### (b) Income tax

The Group is subject to income taxes in numerous jurisdictions. Significant judgment is required in determining the worldwide provision for income taxes. There are certain transactions and calculations for which the ultimate tax determination may be uncertain. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

### (c) Net realisable value of inventories

Net realisable value of inventories is the estimated selling price in the ordinary course of business, less estimated costs of completion and selling expenses. These estimates are based on current market conditions and the historical experience of manufacturing and selling products of similar nature. Management reassesses the estimation on each of the balance sheet date.

### (d) Impairment of receivables

The Group's management determines the provision for impairment of receivables. This estimate is based on the credit history of its customers and current market conditions. Management reassesses the estimation on each of balance sheet date.

### (e) Impairment of investments in an associate and jointly controlled entities

The Group's management determines the impairment on its interests in an associate and jointly controlled entities based on an assessment of the recoverable amounts of the investments.

## 5. Revenues and Segmental Information

During the year, revenues are recognised as follows:

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Continuing operations | | |
| Sales of carpets | **816,867** | 627,340 |
| Yarn manufacturing and trading | **48,548** | 57,635 |
| Sales of interior furnishings | **29,937** | 18,845 |
| Gross rental income from investment properties | **4,674** | 5,612 |
| | **900,026** | 709,432 |
| Discontinued operation | | |
| Sales of interior furnishings | **23,738** | 46,197 |
| Total revenues | **923,764** | 755,629 |

**Primary reporting format - business segments**

The Group was organised on a worldwide basis into four main business segments in 2006:

| | | |
|---|---|---|
| Continuing operations | | |
| Carpet | - | Manufacture, import, export and sale of carpets |
| Yarn | - | Manufacture and sale of yarns |
| Interior furnishings | - | Manufacture and sale of mattresses |
| Property holding | - | Mainly rental income from property holding |
| Discontinued operation | - | Sale and leasing of interior furnishings |

**Secondary reporting format - geographical segments**

Although the Group's four business segments were managed on a worldwide basis during 2006, they operated in seven main geographical areas:

| | | |
|---|---|---|
| Hong Kong & Macau | - | Carpet, interior furnishings and property holding |
| Mainland China | - | Carpet, interior furnishings and property holding |
| South East Asia | - | Carpet and property holding |
| Middle East | - | Carpet |
| Other Asian countries | - | Carpet |
| Europe | - | Carpet |
| North America | - | Carpet and yarn |
| Others | - | Carpet |

The principal activities of 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.

## 5.1 Business segments

The following tables present turnover, profit and certain assets, liabilities and expenditure information of the Group's business segments for the years ended 31 December 2006 and 2005.

For the year ended 31 December 2006

| | Carpet HK$'000 | Yarn HK$'000 | Interior furnishings HK$'000 | Property holding HK$'000 | Elimination HK$'000 | Unallocated HK$'000 | Continuing operations Total HK$'000 | Discontinued operation (Interior furnishing) HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|---|---|---|
| Revenue | | | | | | | | | |
| - External revenue | 816,867 | 48,548 | 29,937 | 4,674 | — | — | 900,026 | 23,738 | 923,764 |
| - Inter-segment revenue* | 255 | — | — | 2,069 | (2,324) | — | — | — | — |
| | 817,122 | 48,548 | 29,937 | 6,743 | (2,324) | — | 900,026 | 23,738 | 923,764 |
| **Segment results** | **15,166** | **5,951** | **2,164** | **14,617** | **—** | **(5,890)** | **32,008** | **(3,622)** | **28,386** |
| Finance costs | | | | | | | (3,912) | — | (3,912) |
| Share of profits of | | | | | | | | | |
| an associate | 220 | — | — | — | — | — | 220 | — | 220 |
| jointly controlled entities# | 30,859 | — | — | — | — | — | 30,859 | — | 30,859 |
| Profit before income tax expenses | | | | | | | 59,175 | (3,622) | 55,553 |
| Income tax expenses | | | | | | | (18,191) | (342) | (18,533) |
| Profit for the year | | | | | | | 40,984 | (3,964) | 37,020 |
| Segment assets | 746,359 | 48,220 | 15,694 | 46,335 | — | 11,660 | | | 868,268 |
| Interest in an associate | 21,682 | — | — | — | — | — | | | 21,682 |
| Interests in jointly controlled entities | 157,705 | — | — | — | — | — | | | 157,705 |
| **Total assets** | | | | | | | | | **1,047,655** |
| **Segment liabilities** | **194,506** | **1,727** | **2,836** | **417** | **—** | **41,104** | | | **240,590** |
| Capital expenditure | 29,494 | 158 | 3,009 | — | — | — | | | 32,661 |
| Depreciation | 38,977 | 4,130 | 468 | — | — | — | 43,575 | 2,251 | 45,826 |
| Amortisation of leasehold land and land use rights | 532 | — | — | — | — | — | 532 | — | 532 |

# Included a reversal of impairment of HK$2,900,000

* Inter-segment transactions were entered into under normal commercial terms and conditions that would also be available to unrelated third parties.

For the year ended 31 December 2005

| | Carpet HK$'000 | Yarn HK$'000 | Interior furnishings HK$'000 | Property holding HK$'000 | Elimination HK$'000 | Unallocated HK$'000 | Continuing operations Total HK$'000 | Discontinued operation (Interior furnishings) HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|---|---|---|
| Revenue | | | | | | | | | |
| - External revenue | 627,340 | 57,635 | 18,845 | 5,612 | — | — | 709,432 | 46,197 | 755,629 |
| - Inter-segment revenue* | 2,244 | 10 | — | 1,239 | (3,493) | — | — | — | — |
| | 629,584 | 57,645 | 18,845 | 6,851 | (3,493) | — | 709,432 | 46,197 | 755,629 |
| **Segment results** | **(29,878)** | **8,685** | **1,152** | **22,298** | **—** | **26,533** | **28,790** | **(4,187)** | **24,603** |
| Finance costs | | | | | | | (3,578) | — | (3,578) |
| Share of (loss)/profits of | | | | | | | | | |
| an associate | (69) | — | — | — | — | — | (69) | — | (69) |
| jointly controlled entities | 24,343 | — | — | — | — | — | 24,343 | — | 24,343 |
| Profit before income tax expenses | | | | | | | 49,486 | (4,187) | 45,299 |
| Income tax expenses | | | | | | | (11,728) | 883 | (10,845) |
| Profit for the year | | | | | | | 37,758 | (3,304) | 34,454 |
| Segment assets | 658,535 | 54,166 | 41,554 | 77,750 | — | 4,232 | | | 836,237 |
| Interest in an associate | 21,166 | — | — | — | — | — | | | 21,166 |
| Interests in jointly controlled entities | 133,318 | — | — | — | — | — | | | 133,318 |
| **Total assets** | | | | | | | | | **990,721** |
| **Segment liabilities** | **139,251** | **2,392** | **8,436** | **1,019** | **—** | **128,152** | | | **279,250** |
| Capital expenditure | 58,650 | 360 | 4,808 | — | — | — | | | 63,818 |
| Depreciation | 33,255 | 2,269 | 385 | — | — | — | 35,909 | 4,023 | 39,932 |
| Amortisation of leasehold land and land use rights | 408 | — | — | — | — | — | 408 | — | 408 |

* Inter-segment transactions were entered into under normal commercial terms and conditions that would also be available to unrelated third parties.

## 5.2 Geographical segments

The following tables present turnover, profit, assets and capital expenditure information of the Group's geographical segments for the years ended 31 December 2006 and 2005:

For the year ended 31 December 2006

| | Turnover | | | Segment results | | | | |
|---|---|---|---|---|---|---|---|---|
| | Continuing operations HK$'000 | Discontinued operation HK$'000 | Total HK$'000 | Continuing operations HK$'000 | Discontinued operation HK$'000 | Total HK$'000 | Total assets HK$'000 | Capital expenditure HK$'000 |
| Hong Kong and Macau | 76,555 | 23,489 | 100,044 | 12,828 | (3,719) | 9,109 | 96,577 | 4,390 |
| Mainland China | 35,889 | — | 35,889 | (423) | — | (423) | 140,326 | 7,871 |
| South East Asia | 235,449 | 96 | 235,545 | 10,087 | 57 | 10,144 | 377,733 | 13,436 |
| Middle East | 25,612 | — | 25,612 | (2,895) | — | (2,895) | — | — |
| Other Asian countries | 30,281 | — | 30,281 | 3,399 | — | 3,399 | — | — |
| Europe | 74,004 | — | 74,004 | (10,513) | — | (10,513) | 37,795 | 1,449 |
| North America | 408,654 | 153 | 408,807 | 23,107 | 40 | 23,147 | 204,177 | 5,515 |
| Others | 13,582 | — | 13,582 | 2,308 | — | 2,308 | — | — |
| | 900,026 | 23,738 | 923,764 | 37,898 | (3,622) | 34,276 | 856,608 | 32,661 |
| Unallocated items | | | | (5,890) | | | | |
| Operating profit | | | | 32,008 | | | | |
| Interest in an associate* | | | | | | | 21,682 | |
| Interests in jointly controlled entities# | | | | | | | 157,705 | |
| Unallocated assets | | | | | | | 11,660 | |
| **Total assets** | | | | | | | **1,047,655** | |

For the year ended 31 December 2005

| | Turnover | | | Segment results | | | | |
|---|---|---|---|---|---|---|---|---|
| | Continuing operations HK$'000 | Discontinued operation HK$'000 | Total HK$'000 | Continuing operations HK$'000 | Discontinued operation HK$'000 | Total HK$'000 | Total assets HK$'000 | Capital expenditure HK$'000 |
| Hong Kong and Macau | 51,155 | 42,305 | 93,460 | 15,367 | (4,128) | 11,239 | 112,357 | 5,192 |
| Mainland China | 32,949 | 2,515 | 35,464 | 499 | 153 | 652 | 136,320 | 2,325 |
| South East Asia | 221,675 | — | 221,675 | 11,462 | — | 11,462 | 361,545 | 30,497 |
| Middle East | 26,920 | — | 26,920 | (811) | — | (811) | — | — |
| Other Asian countries | 21,434 | — | 21,434 | 1,045 | — | 1,045 | — | — |
| Europe | 66,569 | — | 66,569 | (8,236) | — | (8,236) | 33,088 | 1,671 |
| North America | 277,912 | 342 | 278,254 | (18,414) | 63 | (18,351) | 188,695 | 24,133 |
| Others | 10,818 | 1,035 | 11,853 | 1,345 | (275) | 1,070 | — | — |
| | 709,432 | 46,197 | 755,629 | 2,257 | (4,187) | (1,930) | 832,005 | 63,818 |
| Unallocated items | | | | 26,533 | | | | |
| Operating profit | | | | 28,790 | | | | |
| Interest in an associate* | | | | | | | 21,166 | |
| Interests in jointly controlled entities# | | | | | | | 133,318 | |
| Unallocated assets | | | | | | | 4,232 | |
| **Total assets** | | | | | | | **990,721** | |

* Located in South East Asia

\# Located in the Mainland China

## 6. Interest Income

| | 2006<br>HK$'000 | 2005<br>HK$'000 |
|---|---|---|
| Bank interest income | **1,643** | 1,101 |

## 7. Operating Profit

| | 2006<br>HK$'000 | 2005<br>HK$'000 |
|---|---|---|
| Operating profit is stated after crediting and charging the following: | | |
| **Crediting:** | | |
| Gain on disposal of property, plant and equipment | **137** | — |
| Reversal of impairment of trade and other receivables | — | 139 |
| Net exchange gains | — | 1,073 |
| **Charging:** | | |
| Depreciation of property, plant and equipment (Note 16) | **45,826** | 39,932 |
| Amortisation of leasehold land and land use rights (Note 15) | **532** | 408 |
| Loss on disposal of property, plant and equipment | — | 92 |
| Impairment of inventories | **1,277** | 1,269 |
| Impairment of trade and other receivables | **2,874** | — |
| Impairment of construction in progress | — | 4,470 |
| Employee benefit expenses (Note 9) | **276,486** | 226,188 |
| Operating lease charges | | |
| - Land and buildings | **19,193** | 17,287 |
| - Plant and machinery | **789** | 661 |
| Auditors' remuneration | **2,451** | 2,326 |
| Direct operating expenses arising from investment properties that generated rental income | **507** | 604 |
| Direct operating expenses arising from investment properties that did not generate rental income | — | 17 |
| Research and development costs | **2,297** | 2,270 |
| Net exchange losses | **2,896** | — |

## 8. Finance Costs

| | 2006<br>HK$'000 | 2005<br>HK$'000 |
|---|---|---|
| Interest on bank loans and overdrafts wholly repayable within five years | **3,912** | 3,578 |

## 9. Employee Benefit Expenses

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Wages and salaries (including Directors' emoluments) | **270,571** | 221,496 |
| Share options granted to a Director | **51** | 176 |
| Retirement benefit costs – defined contribution schemes (including Directors' emoluments) | **5,864** | 4,516 |
| Total | **276,486** | 226,188 |

**(a) Retirement benefit costs — defined contribution schemes**

Unvested benefits totalling HK$159,000 (2005: HK$178,000) were used during the year to reduce future contributions. As at 31 December 2006, unvested benefits totalling HK$105,000 (2005: HK$116,000) were available for use by the Group to reduce future contributions.

**(b) Directors' emoluments**

The emoluments of each Director for the year ended 31 December 2006 are set out below:

| Name of Directors | Fees HK$'000 | Salaries HK$'000 | Bonuses HK$'000 | Other benefits HK$'000 | Retirement benefit costs HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|
| Mr. Nicholas T. J. Colfer | 30 | — | — | — | — | 30 |
| Mr. Ian D. Boyce | 30 | — | — | — | — | 30 |
| Mr. Lincoln K. K. Leong @ | — | — | — | — | — | — |
| Mr. Nelson K. F. Leong # | 30 | — | — | — | — | 30 |
| Mr. David C. L. Tong | 50 | — | — | — | — | 50 |
| Mr. John J. Ying | 50 | — | — | — | — | 50 |
| Mrs. Yvette Y. H. Fung* | 50 | — | — | — | — | 50 |
| Mr. Michael T. H. Lee* | 50 | — | — | — | — | 50 |
| Mr. Roderic N. A. Sage* | 80 | — | — | — | — | 80 |
| Mr. Lincoln C. K. Yung* | 30 | — | — | — | — | 30 |
| Mr. James H. Kaplan | — | 3,900 | 2,477 | 118 | 140 | 6,635 |
| | 400 | 3,900 | 2,477 | 118 | 140 | 7,035 |

The emoluments of each Director for the year ended 31 December 2005 are set out below:

| Name of Directors | Fees HK$'000 | Salaries HK$'000 | Bonuses HK$'000 | Inducement Fees HK$'000 | Other benefits HK$'000 | Retirement benefit costs HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|---|---|
| Mr. Nicholas T. J. Colfer | 26 | — | — | — | — | — | 26 |
| Mr. Ian D. Boyce | 20 | — | — | — | — | — | 20 |
| Mr. Lincoln K. K. Leong @ | — | — | — | — | — | — | — |
| Mr. Nelson K. F. Leong # | 40 | — | — | — | — | — | 40 |
| Mr. David C. L. Tong (i) | 13 | — | — | — | — | — | 13 |
| Mr. John J. Ying | 40 | — | — | — | — | — | 40 |
| Mrs. Yvette Y. H. Fung* | 37 | — | — | — | — | — | 37 |
| Mr. Michael T. H. Lee* | 40 | — | — | — | — | — | 40 |
| Mr. Roderic N. A. Sage (ii) | 5 | — | — | — | — | — | 5 |
| Mr. Lincoln C. K. Yung* | 20 | — | — | — | — | — | 20 |
| Mr. James H. Kaplan | 20 | 3,120 | 1,385 | 390 | 47 | 69 | 5,031 |
| Ms. Alison S. Bailey (iii) | 17 | 1,453 | 468 | — | — | 108 | 2,046 |
| Mr. James S. Dickson Leach (iv) | 11 | — | — | — | — | — | 11 |
| Mr. Anthony Y. C. Yeh (v) | 14 | — | — | — | — | — | 14 |
| Mr. Kent M. C. Yeh (v) | 14 | — | — | — | — | — | 14 |
| | 317 | 4,573 | 1,853 | 390 | 47 | 177 | 7,357 |

* Independent Non-executive Directors
# Alternate Director to Mr. Lincoln K. K. Leong
@ Mr. Lincoln K. K. Leong's director fee was paid to his alternate Mr. Nelson K. F. Leong
(i) Appointed on 13 May 2005
(ii) Appointed on 15 November 2005
(iii) Resigned on 1 November 2005
(iv) Resigned on 13 May 2005
(V) Resigned on 8 September 2005

Apart from the above, the Directors' emoluments included share options expenses in respective of the options granted to Mr. James H. Kaplan, which amounted to HK$51,000 (2005: HK$176,000).

**(c) Five highest paid individuals**

The five individuals whose emoluments were the highest in the Group for the year include one (2005: two) Director(s) whose emoluments are reflected in the analysis presented above. The emoluments paid to the remaining four (2005: three) individuals during the year are as follows:

| | 2006<br>HK$'000 | 2005<br>HK$'000 |
|---|---|---|
| Basic salaries, housing and other allowances | **6,189** | 5,238 |
| Bonuses | **1,173** | 1,315 |
| Contributions to retirement schemes | **166** | 111 |
| | **7,528** | 6,664 |

The emoluments fell within the following bands:

| | No. of Individuals | |
|---|---|---|
| | **2006** | 2005 |
| Emolument bands | | |
| HK$1,500,001 – HK$2,000,000 | **3** | 1 |
| HK$2,000,001 – HK$2,500,000 | **—** | 1 |
| HK$2,500,001 – HK$3,000,000 | **1** | 1 |

## 10. Income Tax Expenses

Hong Kong profits tax has been provided at the rate of 17.5% (2005: 17.5%) on the estimated assessable profits for the year. Income tax expenses on the People's Republic of China (the "PRC") and overseas profits has been calculated on the estimated assessable profits for the year at the rates of taxation prevailing in the respective countries.

The amount of income tax expenses charged/(credited) to the consolidated profit and loss account represents:

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Current income tax expenses | | |
| - Hong Kong | **3,538** | — |
| - PRC and Overseas | **26,269** | 13,984 |
| (Over)/under provision in prior years | **(2,194)** | 335 |
| Deferred income tax credit | **(9,422)** | (2,591) |
| Income tax expenses | **18,191** | 11,728 |

Share of income tax expenses of an associate and jointly controlled entities of HK$324,000 (2005: HK$568,000) and HK$10,228,000 (2005: HK$8,352,000) respectively are included in the share of profits/(losses) of an associate and jointly controlled entities.

The taxation on the Group's profit before income tax expenses differs from the theoretical amount that would arise using the taxation rate of Hong Kong as follows:

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Profit before income tax expenses | **59,175** | 49,486 |
| Less: Share of profits of an associate and jointly controlled entities | **(28,179)** | (24,274) |
| Reversal of impairment of jointly controlled entities - not subject to taxation | **(2,900)** | — |
| Profit before income tax expenses of the Company and subsidiaries | **28,096** | 25,212 |
| Calculated at a taxation rate of 17.5% (2005: 17.5%) | **4,917** | 4,412 |
| Effect of different taxation rates in other tax jurisdictions | **6,184** | 5,109 |
| Income not subject to taxation | **(295)** | (10,714) |
| Expenses not deductible for taxation purposes | **1,243** | 1,979 |
| Tax losses not recognised | **8,336** | 12,744 |
| Recognition of previously unrecognised deductible temporary differences | **—** | (2,137) |
| (Over)/under provision in previous years | **(2,194)** | 335 |
| Income tax expenses | **18,191** | 11,728 |

## 11. Discontinued Operation

On 7 July 2006, the Company's entire interests in both Indigo Living Limited ("Indigo") and Banyan Tree Limited ("Banyan Tree") were sold at a consideration of HK$19,200,000. Both Indigo and Banyan Tree were wholly-owned subsidiaries before the disposal and collectively represented a separate line of business under the category "Interior Furnishings" for the purpose of HKFRS 5 "Non-current Assets Held for Sale and Discontinued Operations".

The aggregate results of Indigo and Banyan Tree for the period are as follows:

| | **2006*** **HK$'000** | 2005 HK$'000 |
|---|---|---|
| Turnover | **23,738** | 46,197 |
| Cost of sales | **(9,056)** | (18,507) |
| Gross profit | **14,682** | 27,690 |
| Interest income from banks and finance leases | **43** | 64 |
| Distribution costs | **(2,945)** | (2,720) |
| Administrative expenses | **(9,815)** | (23,815) |
| Other operating expenses, net | **(89)** | (5,406) |
| Profit before income tax expenses | **1,876** | (4,187) |
| Income tax(expenses)/credit | **(342)** | 883 |
| | **1,534** | (3,304) |
| Loss on disposal of discontinued operation | **(5,498)** | — |
| Loss after income tax expenses from discontinued operation | **(3,964)** | (3,304) |

* Up to 7 July 2006, the date of disposal.

During the period up to 7 July 2006, Indigo and Banyan Tree used an aggregate of HK$3,910,000 of cash in respect of the Group's net operating cash flows (2005: generated HK$4,617,000 cash from operating activities) and paid HK$2,091,000 (2005: HK$3,052,000) in respect of investing activities.

The assets and liabilities of Indigo and Banyan Tree at the date of disposal were disclosed in Note b of the Consolidated Cash Flow Statement.

## 12. Profit Attributable to Equity Holders of the Company

The profit attributable to equity holders of the Company is dealt with in the accounts of the Company to the extent of loss of HK$3,771,000 (2005: loss of HK$621,000).

## 13. Dividend

| | **2006** **HK$'000** | 2005 HK$'000 |
|---|---|---|
| Final dividend, proposed, of HK 3 cents per share (2005: Nil) | **6,366** | — |

At the Board meeting held on 20 April 2007, the Directors declared a final dividend of HK 3 cents per share. This proposed dividend is not reflected as a dividend payable in the accounts, but will be reflected as an appropriation of retained earnings for the year ended 31 December 2007.

## 14. Earnings Per Share

### (a) Continuing and discontinued operations

**Basic**

Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of shares in issue during the year.

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Profit attributable to equity holders of the Company | **32,694** | 27,646 |
| | **No. of ordinary shares** | |
| Weighted average number of ordinary shares in issue (thousands) | **212,187** | 211,933 |
| Basic earnings per share (HK cents) | **15.41** | 13.04 |

**Diluted**

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The Company has one category of dilutive potential ordinary shares, namely share options. For these share options a calculation is performed to determine the number of shares that could have been acquired at fair value (determined as average annual market share price of the Company's shares) based on the monetary value of the subscription rights attached to the outstanding share options. The number of shares calculated below is compared with the number of shares that would have been issued assuming the exercise of the share options.

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Profit attributable to equity holders of the Company | **32,694** | 27,646 |
| | **No. of ordinary shares** | |
| Weighted average number of ordinary shares in issue (thousands) | **212,187** | 211,933 |
| Adjustments for share options (thousands) (note) | — | 7 |
| Weighted average number of ordinary shares in issue for diluted earnings per share (thousands) | **212,187** | 211,940 |
| Diluted earnings per share (HK cents) | **15.41** | 13.04 |

Note: The share options did not have any dilutive effect for the year ended 31 December 2006 as the average market price of the Company's ordinary shares during the year was lower than the exercise price of the share options.

(b) **Continuing operations**

**Basic**

The calculation of the basic earnings per share from continuing operations attributable to the equity holders of the Company is based on the following information:

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Profit attributable to equity holders of the Company | **32,694** | 27,646 |
| Add: Loss attributable to equity holders from discontinued operation | **3,964** | 3,304 |
| Profit attributable to equity holders of the Company from continuing operations | **36,658** | 30,950 |
| | **No. of ordinary shares** | |
| Weighted average number of ordinary shares in issue (thousands) | **212,187** | **211,933** |
| **Basic earnings per share (HK cents)** | **17.28** | **14.60** |

**Diluted**

The calculation of the diluted earnings per share from continuing operations attributable to the equity holders of the Company is based on the profit attributable to equity holders from continuing operations of HK$36,658,000 (2005: HK$30,950,000). The denominators used are the same as those detailed above for diluted earnings per share from continuing and discontinued operations.

(c) **Discontinued operation**

**Basic**

The calculation of the basic loss per share from discontinued operation attributable to the equity holders of the Company is based on the following information:

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Loss attributable to equity holders from discontinued operations | **(3,964)** | (3,304) |
| | **No. of ordinary shares** | |
| Weighted average number of ordinary shares in issue (thousands) | **212,187** | 211,933 |
| Basic loss per share (HK cents) | **(1.87)** | (1.56) |

**Diluted**

The calculation of the diluted loss per share from discontinued operation attributable to the equity holders of the Company is based on the loss attributable to equity holders from discontinued operation of HK$3,964,000 (2005: HK$3,304,000). The denominators used are the same as those detailed above for diluted earnings per share from continuing and discontinued operations.

## 15. Leasehold Land and Land Use Rights

**Group**

The Group's interests in leasehold land and land use rights represent prepaid operating lease payments and their net book values are analysed as follows:

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| In Hong Kong held on | | |
| Leases of between 10 – 50 years | **11,740** | 12,031 |
| | | |
| Outside Hong Kong held on | | |
| Leases of between 10 – 50 years | **9,848** | 9,708 |
| | **21,588** | 21,739 |

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| At 1 January | 21,739 | 9,763 |
| Leasehold land received in the form of dividend in specie upon liquidation of an available-for-sale financial asset | — | 12,200 |
| Exchange differences | **381** | 184 |
| Amortisation of prepaid operating lease payment | **(532)** | (408) |
| At 31 December | **21,588** | 21,739 |

## 16. Property, Plant and Equipment

### Group

| | Buildings HK$'000 | Other assets HK$'000 | Total HK$'000 |
|---|---|---|---|
| **As at 1 January 2005** | | | |
| Cost or valuation | 146,446 | 445,227 | 591,673 |
| Accumulated depreciation | (47,127) | (273,541) | (320,668) |
| Net book amount | 99,319 | 171,686 | 271,005 |
| **Year ended 31 December 2005** | | | |
| Opening net book amount | 99,319 | 171,686 | 271,005 |
| Exchange differences | (3,344) | (5,329) | (8,673) |
| Additions | — | 22,404 | 22,404 |
| Property received in the form of dividend in specie upon liquidation of an available-for-sale financial asset | 16,900 | — | 16,900 |
| Transfer from construction in progress | 820 | 41,638 | 42,458 |
| Disposals | (175) | (547) | (722) |
| Depreciation | (5,536) | (34,396) | (39,932) |
| Closing net book amount | 107,984 | 195,456 | 303,440 |
| **As at 31 December 2005 and 1 January 2006** | | | |
| Cost or valuation | 158,608 | 488,505 | 647,113 |
| Accumulated depreciation | (50,624) | (293,049) | (343,673) |
| Net book amount | 107,984 | 195,456 | 303,440 |
| **Year ended 31 December 2006** | | | |
| Opening net book amount | **107,984** | **195,456** | **303,440** |
| Exchange differences | **10,118** | **18,494** | **28,612** |
| Additions | **58** | **15,110** | **15,168** |
| Transfer from construction in progress | **216** | **22,970** | **23,186** |
| Disposals | **—** | **(2,028)** | **(2,028)** |
| Disposal of a discontinued operation | **—** | **(5,148)** | **(5,148)** |
| Impairment | **—** | **(312)** | **(312)** |
| Depreciation | **(6,029)** | **(39,797)** | **(45,826)** |
| Closing net book amount | **112,347** | **204,745** | **317,092** |
| **As at 31 December 2006** | | | |
| Cost or valuation | **175,261** | **533,214** | **708,475** |
| Accumulated depreciation and impairment | **(62,914)** | **(328,469)** | **(391,383)** |
| Net book amount | **112,347** | **204,745** | **317,092** |

Other assets include plant and machinery, furniture, fixtures, equipment and motor vehicles.

Certain of the Group's buildings were revalued on an open market basis at 31 December 1989 by independent professional valuers, Jones Lang Wootton (now Jones Lang LaSalle) and W. Lamar Pinson, Inc. The revaluation was carried out prior to 30 September 1995. Under transitional provisions in paragraph 80A of HKAS 16, the Group is not required to make regular revaluations in accordance with paragraphs 31 and 36 of HKAS 16. The carrying amount of such revalued buildings would have been HK$5,752,000 (2005: HK$5,529,000) had it been stated at cost less accumulated depreciation.

The cost or valuation of property, plant and equipment is analysed as follows:

**Group**

| | **Buildings** | **Other assets** |
|---|---|---|
| | HK$'000 | HK$'000 |
| At cost | **163,841** | 533,214 |
| At valuation – 1989 | **11,420** | — |
| As at 31 December 2006 | **175,261** | 533,214 |
| | | |
| At cost | **147,781** | 488,505 |
| At valuation – 1989 | **10,827** | — |
| As at 31 December 2005 | **158,608** | 488,505 |

In 2005, the other assets category included furniture leased by Indigo to third party under operating leases with net book amount of HK$1,752,000. Indigo was disposed by the Group in July 2006.

## 17. Investment Properties

### Group

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Net book value as at 1 January | **73,130** | 77,212 |
| Property received in the form of dividend in specie upon liquidation of an available-for-sale financial asset | **—** | 10,950 |
| Surplus on revaluation of investment properties | **6,486** | 15,648 |
| Disposals | **(42,420)** | (28,655) |
| Reclassification to properties held for sale (Note 28) | **(4,436)** | — |
| Exchange differences | **4,040** | (2,025) |
| Net book value as at 31 December | **36,800** | 73,130 |

The investment properties were revalued by an independent, professionally qualified valuer, namely CB Richard Ellis. Valuations were based on current prices in an active market for all properties. Details of principal investment properties are set out on page 98.

The Group's interests in investment properties at their carrying values are analysed as follows:

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| In Hong Kong, held on | | |
| - Medium leases (10 – 50 years) | **21,300** | 20,050 |
| | | |
| Outside Hong Kong, held on | | |
| - Freehold | **—** | 38,380 |
| - Medium leases (10 – 50 years) | **15,500** | 14,700 |
| | **36,800** | 73,130 |

## 18. Construction in Progress

### Group

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| As at 1 January | **12,282** | 18,424 |
| Exchange differences | **1,404** | (628) |
| Additions | **17,493** | 41,414 |
| Transfer to property, plant and equipment | **(23,186)** | (42,458) |
| Impairment | **—** | (4,470) |
| As at 31 December | **7,993** | 12,282 |

## 19. Interests in Subsidiaries

**Company**

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Unlisted shares at directors' valuation in 1990 | **242,800** | 242,800 |
| Loans to a subsidiary | **66,270** | 61,226 |
| Amounts due from subsidiaries | **463,799** | 466,758 |
| | **772,869** | 770,784 |
| Loan from a subsidiary | **(13,213)** | (13,213) |
| Amounts due to subsidiaries | **(91,380)** | (89,673) |
| | **668,276** | 667,898 |
| Impairment | **(362,183)** | (359,020) |
| | **306,093** | 308,878 |

Details of principal subsidiaries are set out on pages 95 and 96. All balances due from/(to) subsidiaries are unsecured, interest-free and repayable on demand, except for an amount of HK$66,270,000 due from a subsidiary (2005: HK$61,226,000) which carries interest at prevailing market rates.

## 20. Amount Due from an Indirectly Held Associate

The amount due from an indirectly held associate is unsecured, interest-free and is repayable on demand.

## 21. Interest in an Associate

**Group**

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Share of net assets | **20,157** | 18,429 |
| Amounts due from an associate | **1,525** | 2,737 |
| | **21,682** | 21,166 |
| | | |
| Shares at cost – unlisted | **519** | 519 |

No dividend income was received from the associate during the year (2005: HK$1,870,000).

Share of the associate's taxation amounted to HK$324,000 (2005: HK$568,000). Details of the associate, which is unlisted, is set out on page 96.

An extract of the operating results and financial position of the associate, Philippine Carpet Manufacturing Corporation, which is based on its consolidated accounts as adjusted to conform with accounting principles generally accepted in Hong Kong ("HKGAAP") for the years ended and as at 31 December 2006 and 2005, is as follows:

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Operating results | | |
| Turnover | **71,271** | 73,716 |
| Profit/(loss) after income tax expenses | **670** | (210) |
| Group's share of profit/(loss) after income tax expenses | **220** | (69) |
| Financial position | | |
| Non-current assets | **46,883** | 38,945 |
| Current assets | **41,390** | 46,286 |
| Non-current liabilities | **(8,322)** | (7,806) |
| Current and other liabilities | **(18,515)** | (21,257) |
| Shareholders' funds | **61,436** | 56,168 |
| Group's share of net assets | **20,157** | 18,429 |

## 22. Interests in Jointly Controlled Entities

**Group**

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Share of net assets | **130,725** | 117,490 |
| Amounts due from jointly controlled entities | | |
| - Loan account | **458** | 458 |
| - Current account | **42,257** | 34,005 |
| | **42,715** | 34,463 |
| | **173,440** | 151,953 |
| Impairment | **(15,735)** | (18,635) |
| | **157,705** | 133,318 |
| Paid in capital at cost | **80,517** | 80,517 |

Dividend income from jointly controlled entities during the year amounted to HK$18,913,000 (2005: HK$17,925,000).

Share of jointly controlled entities taxation amounted to HK10,228,000 (2005: HK$8,352,000).

Details of the principal jointly controlled entities, which are unlisted, are set out on page 96.

An extract of the operating results and financial position of the Group's significant joint ventures, Weihai Shanhua Huabao Carpet Company Limited ("WHCL") and Weihai Shanhua Premier Carpet Company Limited ("WPCL"), which are based on their financial statements as adjusted to conform with HKGAAP for the years ended and as at 31 December 2006 and 2005, is as follows:

**WHCL**

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Operating results | | |
| Turnover | **461,870** | 330,513 |
| Profit after income tax expenses | **26,571** | 18,043 |
| Group's share of profit after income tax expenses | **13,020** | 8,841 |
| Financial position | | |
| Non-current assets | **295,988** | 214,856 |
| Current assets | **111,628** | 71,358 |
| Non-current liabilities | **(11,407)** | (5,383) |
| Current liabilities | **(258,224)** | (139,651) |
| Shareholder's funds | **137,985** | 141,180 |
| Group's share of net assets less impairment | **51,990** | 52,605 |

**WPCL**

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Operating results | | |
| Turnover | **266,039** | 192,419 |
| Profit after income tax expenses | **27,898** | 31,018 |
| Group's share of profit income tax expenses | **13,670** | 15,199 |
| Financial position | | |
| Non-current assets | **32,526** | 16,525 |
| Current assets | **161,517** | 147,173 |
| Non-current liabilities | **—** | — |
| Current liabilities | **(90,393)** | (69,615) |
| Shareholders' funds | **103,650** | 94,083 |
| Group's share of net assets less impairment | **48,768** | 45,531 |

## 23. Financial Assets at Fair Value Through Profit or Loss

**Group**

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| At 1 January | — | — |
| Addition | **22,727** | — |
| Exchange differences | **1,082** | — |
| As at 31 December | **23,809** | — |

Financial assets at fair value through profit or loss include the following:

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Unlisted treasury bonds — overseas | **23,809** | — |

The financial assets are traded on active liquid markets and their fair values are determined with reference to quoted market prices and denominated in Thai Baht in 2006.

## 24. Net Investment in Finance Leases

The total minimum lease payments receivable under finance leases and their present values are as follows:

**Group**

| | Present value of minimum lease payments receivable 2006 HK$'000 | Interest income relating to future periods 2006 HK$'000 | Total minimum lease payments receivable 2006 HK$'000 | Present value of minimum lease payments receivable 2005 HK$'000 | Interest income relating to future periods 2005 HK$'000 | Total minimum lease payments receivable 2005 HK$'000 |
|---|---|---|---|---|---|---|
| Amounts receivable: | | | | | | |
| Not later than one year | — | — | — | 735 | 45 | 780 |
| Later than one year and not later than five years | — | — | — | 210 | 15 | 225 |
| | | — | — | | 60 | 1,005 |
| Net investment in finance leases | — | | | 945 | | |

## 25. Inventories

**Group**

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Raw material | **88,202** | 74,687 |
| Work-in-progress | **23,140** | 22,333 |
| Finished goods | **97,729** | 73,788 |
| Consumable stores | **2,787** | 3,039 |
| | **211,858** | 173,847 |

The cost of inventories recognised as expenses and included in cost of goods sold amounted to HK$514,937,000 (2005: HK$432,587,000).

## 26. Trade and Other Receivables

**Group**

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Trade receivables | **176,182** | 151,745 |
| Less: Impairment loss of receivables | **(20,337)** | (15,493) |
| Trade receivables – net | **155,845** | 136,252 |
| Other receivables | **22,559** | 25,406 |
| | **178,404** | 161,658 |

The amounts approximated to the respective fair values as at 31 December 2006 and 2005. The credit terms of the Group range from 0 to 90 days, depending on the credit status and repayment history of customers. As at the balance sheet date, the ageing analysis of the trade receivables was as follows:

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| 10 – 30 days | **85,432** | 86,020 |
| 31 days – 60 days | **23,634** | 27,705 |
| 61 days – 90 days | **14,078** | 8,037 |
| Over 90 days | **53,038** | 29,983 |
| | **176,182** | 151,745 |

There is no concentration of credit risk with respect to trade receivables as the Group has a large number of customers, internationally dispersed.

The carrying amounts of the Group's trade receivables and other receivables were denominated in the following currencies:

| | Trade receivables | | Other receivables | |
|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| United States Dollar | **93,717** | 77,071 | **5,356** | 3,723 |
| Euro | **12,285** | 12,099 | **3,037** | 2,493 |
| Sterling Pound | **1,773** | 68 | **307** | 1,139 |
| Singapore Dollar | **—** | 158 | **58** | — |
| Renminbi | **4,721** | 3,938 | **6,729** | 8,170 |
| Thai Baht | **28,434** | 31,577 | **5,639** | 4,496 |
| Macau Patacas | **645** | — | **—** | — |
| Hong Kong Dollar | **14,270** | 11,341 | **1,433** | 5,385 |
| | **155,845** | 136,252 | **22,559** | 25,406 |

## 27. Derivative Financial Instruments

### Group

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Foreign currency forward contracts | **681** | — |

The carrying amounts of the Group's derivative financial instruments were denominated in Thai Baht in 2006.

## 28. Properties Held for Sale

### Group

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Properties located in Hong Kong under medium lease | **4,436** | — |

## 29. Cash and Cash Equivalents

| | Group | | Company | |
|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| Cash at bank and on hand | **55,013** | 83,738 | **255** | 232 |
| Short-term bank deposits | **3,963** | 3,341 | **—** | — |
| | **58,976** | 87,079 | **255** | 232 |

The amounts approximated to their respective fair values as at 31 December 2006 and 2005.

The effective interest rate on short-term bank deposits was 3.5% per annum (2005: 3.5% per annum); these deposits have maturity dates ranging between 17 to 43 days.

As at 31 December 2006, the Group's cash and bank balances included RMB13,203,000 (2005: RMB9,279,000) and US$78,000 (2005: US$1,365,000) placed with certain banks in PRC by certain PRC subsidiaries of the Group. These balances are subject to exchange controls.

The carrying amounts of the Group's cash and cash equivalents were denominated in the following currencies:

| | Group | | Company | |
|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| United States Dollar | **20,672** | 47,408 | **42** | 47 |
| Euro | **3,470** | 7,562 | **—** | — |
| Sterling Pound | **677** | 2,111 | **—** | — |
| Singapore Dollar | **1,832** | 870 | **—** | — |
| Renminbi | **13,203** | 8,958 | **—** | — |
| Thai Baht | **4,135** | 1,430 | **—** | — |
| Macau Patacas | **657** | 154 | **—** | — |
| Hong Kong Dollar | **14,330** | 18,586 | **213** | 185 |
| | **58,976** | 87,079 | **255** | 232 |

## 30. Share Capital

### Company

| | **No. of shares** | HK$'000 |
|---|---|---|
| Authorised – HK$0.10 per share: | | |
| At 1 January 2005 and 2006; 31 December 2005 and 2006 | **400,000,000** | 40,000 |
| Issued and fully paid: | | |
| At 1 January 2005 | **211,703,488** | 21,170 |
| Exercise of share options | **230,000** | 23 |
| As at 31 December 2005 and 1 January 2006 | **211,933,488** | 21,193 |
| Exercise of share options | **254,000** | 26 |
| At 31 December 2006 | **212,187,488** | 21,219 |

The movements of the share options for both years ended 31 December 2006 and 2005 were as follows:

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

| Name | Balance as at 1 January 2006 | Date of grant | Changes during the year: Granted | Lapsed | Exercised | Balance as at 31 December 2006 | Exercise price (HK$) (Note) | Exercisable period |
|---|---|---|---|---|---|---|---|---|
| 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 |

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. In 2006, the closing price of the shares immediately before the date on which the options were exercised was HK$1.20.

The Company uses the Black Scholes option pricing model (the "Model") to value share options at the date of grant. 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 below.

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 reserves.

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

| | |
|---|---|
| Date of grant | 10 January 2005 |
| Closing price at the date of grant | HK$1.18 |
| Risk free rate (Note i) | 0.58% - 1.63% |
| Expected life of options | 1 - 3 years |
| Expected volatility (Note ii) | 38.65% |
| Expected dividend per annum (Note iii) | HK$0.0218 |

Notes:

i. 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.

ii. 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.

iii. Expected dividend per annum: being the approximate average annual cash dividend for the past five financial years.

## 31. Reserves

The movements of reserves of the Group for both years ended 31 December 2006 and 2005 are set out in the Consolidated Statements of Changes in Equity on Pages 41 and 42.

The movements of reserves of the Company were as follows:

**Company**

| | Share premium HK$'000 | Capital reserve HK$'000 | Contributed surplus HK$'000 | Accumulated losses HK$'000 | Total HK$'000 | Proposed final dividend HK$'000 |
|---|---|---|---|---|---|---|
| At 1 January 2005 | 189,162 | — | 442,598 | (343,914) | 287,846 | — |
| Premium on issue of new shares | 255 | — | — | — | 255 | — |
| Employee share options scheme - value of employee ervices | — | 176 | — | — | 176 | — |
| Loss for the year | — | — | — | (621) | (621) | — |
| At 31 December 2005 | 189,417 | 176 | 442,598 | (344,535) | 287,656 | — |
| At 1 January 2006 | 189,417 | 176 | 442,598 | (344,535) | 287,656 | — |
| Premium on issue of new shares | 282 | — | — | — | 282 | — |
| Employee share options scheme - value of employee services | — | 51 | — | — | 51 | — |
| Loss for the year | — | — | — | (3,771) | (3,771) | — |
| | 189,699 | 227 | 442,598 | (348,306) | 284,218 | — |
| Proposed final dividend | | | | | (6,366) | 6,366 |
| At 31 December 2006 | | | | | 277,852 | 6,366 |

The contributed surplus of the Company represents the excess of the consolidated net assets of a subsidiary acquired over the nominal amount of the Company's shares issued for the acquisition, as a result of the Group reorganisation in 1990. Under the Companies Act 1981 of Bermuda (as amended), the contributed surplus of the Company is available for distribution to members of the Company.

## 32. Bank Borrowings – Unsecured

### Group

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Non-current | | |
| Repayable between 1 and 2 years | | |
| Thai Baht | — | 9,500 |
| | — | 9,500 |
| Current | | |
| Repayable within 1 year | | |
| Thai Baht | **11,000** | 55,859 |
| Hong Kong Dollar | — | 27,000 |
| United States Dollar | — | 16,977 |
| | **11,000** | 99,836 |
| Total bank borrowings | **11,000** | 109,336 |

The effective interest rates of the borrowings at the balance sheet dates were as follows:

| | 2006 | 2005 |
|---|---|---|
| Thai Baht | 4.5% | 4.7%-5.2% |
| Hong Kong Dollar | — | 5.2%-5.6% |
| United States Dollar | — | 5.7% |

The amounts approximated to their respective fair values as at 31 December 2006 and 2005.

## 33. Deferred Taxation

Deferred taxation is calculated in full on temporary differences under the liability method using a principal taxation rate of 17.5% (2005: 17.5%).

**Group**

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Deferred tax liabilities as at 1 January | (3,649) | (7,223) |
| Exchange differences | 41 | 100 |
| Deferred taxation charged/(credited) to consolidated profit and loss account | | |
| - Continuing operations | 9,422 | 2,591 |
| - Discontinued operation | (306) | 883 |
| Deferred taxation charged to other properties revaluation reserve: | | |
| - Continuing operations | (660) | — |
| Disposal of discontinued operation | (819) | — |
| Deferred tax assets/(liabilities) as at 31 December | 4,029 | (3,649) |

Deferred income tax assets are recognised for tax losses carried forward to the extent that realisation of the related tax benefit through the future taxable profits is probable. The Group has unrecognised tax losses of HK$225,865,000 (2005: HK$188,686,000) to carry forward against future taxable income.

The movements in deferred tax assets and liabilities (prior to offsetting of balances within the same taxation jurisdiction) during the year were as follows:

**Deferred tax liabilities**

**Group**

| | Accelerated tax depreciation allowance | | Revaluation of properties | | Others | | Total | |
|---|---|---|---|---|---|---|---|---|
| | 2006 HK$'000 | 2005 HK$'000 | 2006 HK$'000 | 2005 HK$'000 | 2006 HK$'000 | 2005 HK$'000 | 2006 HK$'000 | 2005 HK$'000 |
| At 1 January | 3,964 | 5,035 | 8,955 | 10,378 | — | — | 12,919 | 15,413 |
| (Credited)/charged to consolidated profit and loss account | (3,200) | (1,071) | (8,185) | (971) | 195 | — | (11,190) | (2,042) |
| Charged to other properties revaluation reserve | — | — | 660 | — | — | — | 660 | — |
| Disposal of discontinued operation | (53) | — | — | — | — | — | (53) | — |
| Exchange differences | — | — | 911 | (452) | 9 | — | 920 | (452) |
| At 31 December | 711 | 3,964 | 2,341 | 8,955 | 204 | — | 3,256 | 12,919 |

### Deferred tax assets
### Group

| | Impairment of assets | | Tax losses | | Others | | Total | |
|---|---|---|---|---|---|---|---|---|
| | **2006** | 2005 | **2006** | 2005 | **2006** | 2005 | **2006** | 2005 |
| | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 | **HK$'000** | HK$'000 |
| At 1 January | **8,203** | 7,180 | **953** | 841 | **114** | 169 | **9,270** | 8,190 |
| (Credited)/charged to consolidated profit and loss account | **(2,187)** | 1,372 | **112** | 112 | **1** | (52) | **(2,074)** | (1,432) |
| Disposal of discontinued operation | **—** | — | **(872)** | — | **—** | — | **(872)** | — |
| Exchange differences | **956** | (349) | **—** | — | **5** | (3) | **961** | (325) |
| At 31 December | **6972** | 8,203 | **193** | 953 | **120** | 114 | **7,285** | 9,270 |

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The following amounts, determined after appropriate offsetting, are shown on the consolidated balance sheet:

### Group

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Deferred tax assets | **6,631** | 1,983 |
| Deferred tax liabilities | **(2,602)** | (5,632) |
| | **4,029** | (3,649) |

## 34 . Other Long-term Liabilities
### Group

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Non-current portion | | |
| - Repayable between 1 and 2 years | **390** | 390 |
| - Repayable between 2 to 5 years | **1,601** | 1,991 |
| | **1,991** | 2,381 |
| Current portion | **(390)** | (390) |
| Total long-term liabilities | **1,601** | 1,991 |

Other long-term liabilities represent the consideration payable to the vendor in respect of the acquisition of White Oak Carpet Mills, Inc. in 2001. The amounts approximated to the respective fair values as at 31 December 2006 and 2005.

All carrying amounts of the Group's other long-term liabilities were denominated in United States Dollar in 2006 and 2005.

## 35. Trade and Other Payables

### Group

| | 2006<br>HK$'000 | 2005<br>HK$'000 |
|---|---|---|
| Trade payables | **42,391** | 46,482 |
| Other payables | **159,129** | 106,534 |
| | **201,520** | 153,016 |

At the balance sheet date, the ageing analysis of the trade payables was as follows:

| | 2006<br>HK$'000 | 2005<br>HK$'000 |
|---|---|---|
| Current — 30 days | **33,380** | 29,374 |
| 31 days — 60 days | **4,806** | 11,094 |
| 61 days — 90 days | **2,183** | 3,214 |
| Over 90 days | **2,022** | 2,800 |
| | **42,391** | 46,482 |

The carrying amounts of the Group's trade payables and other payables were denominated in the following currencies:

| | Trade payables | | Other payables | |
|---|---|---|---|---|
| | 2006<br>HK$'000 | 2005<br>HK$'000 | 2006<br>HK$'000 | 2005<br>HK$'000 |
| United States Dollar | **19,136** | 21,151 | **82,552** | 45,856 |
| Euro | **6,890** | 7,134 | **10,313** | 7,186 |
| Sterling Pound | **726** | 1,111 | **8,825** | 1,640 |
| Singapore Dollar | **6** | 1 | **434** | 147 |
| Renminbi | **1,102** | 1,127 | **12,209** | 8,745 |
| Thai Baht | **11,875** | 13,148 | **26,441** | 21,374 |
| Macau Patacas | **—** | — | **4,219** | 169 |
| Australian Dollar | **—** | 66 | **—** | — |
| Japanese Yen | **44** | 47 | **—** | — |
| Hong Kong Dollar | **2,612** | 2,730 | **14,136** | 21,404 |
| | **42,391** | 46,482 | **151,129** | 106,534 |

## 36. Future Operating Lease Income

As at 31 December 2006, the Group had future aggregate minimum lease payments receivable under non-cancellable operating leases as follows:

**Group**

| | 2006<br>Property<br>HK$'000 | 2006<br>Other assets<br>HK$'000 | 2005<br>Property<br>HK$'000 | 2005<br>Other assets<br>HK$'000 |
|---|---|---|---|---|
| Not later than one year | **1,439** | **—** | 1,638 | 4307 |
| Later than one year and not later than five years | **166** | **—** | 2,419 | 368 |
| | **1,605** | **—** | 4,057 | 4,675 |

## 37. Operating Lease Commitments

At 31 December 2006, the Group had future aggregate minimum lease payments under non-cancellable operating leases as follows:

**Group**

| | 2006<br>Property<br>HK$'000 | 2006<br>Other assets<br>HK$'000 | 2005<br>Property<br>HK$'000 | 2005<br>Other assets<br>HK$'000 |
|---|---|---|---|---|
| Not later than one year | **15,876** | **988** | 20,189 | 633 |
| Later than one year and not later than five years | **52,149** | **1,446** | 47,943 | 799 |
| Later than five years | **21,637** | **—** | 28,857 | — |
| | **89,662** | **2,434** | 96,989 | 1,432 |

## 38. Capital Commitments

### Group

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Contracted but not provided for in respect of property, plant and equipment | **4,191** | 1,208 |
| Authorised but not contracted for in respect of property, plant and equipment | **418** | 3,076 |
| | **4,609** | 4,284 |

The Group's share of capital commitments of the jointly controlled entities not included in the above was as follows:

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Contracted but not provided for in respect of property, plant and equipment | **23,946** | 24,996 |
| Authorised but not contracted for in respect of property, plant and equipment | **13,477** | 31,157 |
| | **37,423** | 56,153 |

## 39. Contingent Liabilities

| | Group | | Company | |
|---|---|---|---|---|
| | **2006 HK$'000** | 2005 HK$'000 | **2006 HK$'000** | 2005 HK$'000 |
| Guarantees for banking facilities granted to subsidiaries | — | — | **104,060** | 108,914 |
| Corporate guarantee in respect of performance bonds issued by the subsidiaries to customers | **3,793** | 4,892 | — | — |
| Counter-indemnity in respect of performance bonds issued by banks | **4,347** | 1,856 | — | — |
| Guarantees in lieu of utility deposit | **1,897** | 1,088 | — | — |
| Guarantees in lieu of accessory security for a sales order | **524** | 653 | — | — |
| Counter-indemnity in respect of advance performance bonds issued by banks | **2,348** | — | — | — |
| | **12,909** | 8,489 | **104,060** | 108,914 |

The Company has not recognised any deferred income in respect of the guarantees for banking facilities granted to subsidiaries as their fair value cannot be reliably measured and their transaction price was HK$Nil.

## 40. Related Party Transactions

The following transactions were carried out in the normal course of the Group's business:

### (1) Sales of goods and services

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Sales of carpets: | | |
| An associate (Note a) | **6,584** | 3,263 |
| The Hongkong and Shanghai Hotels, Limited ("HSH") (Note b) | **5,898** | 7,007 |
| Furniture sales and leasing | | |
| HSH (Note c) | **285** | 579 |
| | **12,767** | 10,849 |

(a) Sales to an associate were conducted in the normal course of business and at mutually agreed prices between the parties.

(b) By virtue of the fact that HSH is under common control with the Company, the Company's transactions with HSH and its subsidiaries are related party transactions. These transactions also fall under the definition of continuing connected transactions under the Listing Rules and are disclosed under the "Connected Transactions" section in the Directors' Report.

(c) Furniture sales and leasing to HSH and its subsidiaries were also continuing connected transactions under the Listing Rules, but as the gross amount of furniture sales and leasing in 2006 was less than the "de minimis" level in Rule 14A.33(3) of the Listing Rules, these transactions were exempt from disclosure by way of press announcement. These transactions were entered on normal commercial terms.

### (2) Purchase of goods and services

| | 2006 HK$'000 | 2005 HK$'000 |
|---|---|---|
| Purchase of goods from: | | |
| An associate (Note d) | **2,889** | 4,810 |
| Jointly controlled entities (Note d) | **23,735** | 4,382 |
| Feltech Manufacturing Company Limited ("FMCL") (Note e) | **1,408** | 813 |
| Purchase of services from: | | |
| Rental paid to HSH (Note f) | **235** | 448 |
| | **28,267** | 10,453 |

(d) Purchases from an associate and jointly controlled entities were conducted in the normal course of business and at mutually agreed prices between the parties.

(e) FMCL is 61.75% owned by Mr. Wan Tabtiang, a director of Carpets International Thailand Public Company Limited ("CIT", a 99% owned subsidiary of the Company) and has been selling carpet underlay to CIT on normal commercial terms. These transactions are also continuing connected transactions under the Listing Rules and are disclosed under the "Connected Transactions" section in the Directors' Report.

(f) Rental paid to HSH was based on fixed monthly amounts mutually agreed by parties involved.

### (3) Key management compensation

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Salaries and other short-term employee benefits | **32,141** | 23,307 |
| Share-based payments | **51** | 176 |
| | **32,192** | 23,483 |

### (4) Year-end balances arising from sales/purchases of goods/services

| | **2006** | 2005 |
|---|---|---|
| | **HK$'000** | HK$'000 |
| Trade receivables from related parties: | | |
| An associate | **1,525** | 1,403 |
| HSH | **53** | 286 |
| | **1,578** | 1,689 |
| Trade payables to related parties: | | |
| Jointly controlled entities | **5,378** | 901 |
| FMCL | **217** | 133 |
| | **5,595** | 1,034 |

## 41. Events After Balance Sheet Date

**(a) Formation of a new jointly controlled entities**

On 26 January 2007, Treasure Looms (China) Limited ("Treasure Looms"), a wholly-owned subsidiary of the Company, entered into a joint venture agreement with Weihai Shanhua Carpets Group Company Limited ("Shanhua", a company incorporated in the PRC) to establish a jointly controlled entity (the "JV Company") in the PRC. The JV Company will principally be engaged in carpet manufacturing.

Treasure Looms has already established three other jointly controlled entities in the PRC with Shanhua.

The registered capital and total investment of the JV Company are US$6,000,000 (approximately HK$46,800,000) and US$15,000,000 (approximately HK$117,000,000) respectively. 49% of the registered capital, or US$2,940,000 (approximately HK$22,932,000), would be contributed in cash by Treasure Looms within 6 months after the issuance of business license of the JV Company, and the contribution was expected to be financed through dividend payments to be made to the Treasure Looms from two other jointly controlled entities with Shanhua.

**(b) New Corporate Income Tax Law in the PRC**

On 16 March 2007, the 5th Plenary Session of the 10th National People's Congress passed the Corporate Income Tax Law of the People's Republic of China ("the New Corporate Income Tax Law") which will take effect on 1 January 2008. The Group is not able to make an estimate of the expected financial effect of the New Corporate Tax Law on its deferred tax assets and liabilities. The enactment of the New Corporate Tax Law is not expected to have any financial effect on the amounts accrued on the balance sheet in respect of current tax payable.

## 42. Comparatives

The Group previously classified the expenses of certain sales offices as distribution costs. In 2006, the Group reclassified the expenses of such sales offices in accordance with their nature, in order to align with all other group companies for similar items. Management believes that such reclassification will provide a clearer presentation of the Group's results.

The Group also included impairment of inventories and construction in progress in other operating expenses. In 2005, such items were disclosed separately on the face of the consolidated profit and loss account.

The Group has realigned the presentation of the 2005 comparative figures in the cash flow statement to conform with the current year's presentation. These included separate disclosure of the change in the impairment of trade and other receivables previously aggregated within working capital changes, and reclassifying changes in amounts due from an associate and jointly controlled entities previously presented under working capital changes to investing activities.

# Principal Subsidiaries, Associated Company and Jointly Controlled Entities

The table lists below the subsidiaries of the Group which, in the opinion of the Directors principally affected the results or assets of the Group. To give details of other subsidiaries would in the opinion of the Directors, result in particulars of excessive length.

| Name | Country of incorporation and operations | Principal activities | Issued and paid-up capital | Percentage of equity attributable to the Group |
|---|---|---|---|---|
| **Subsidiaries** | | | | |
| Costigan Limited | British Virgin Island | Investment holding | 100 shares of US$1 each | 100%# |
| Luard Enterprises Limited | British Virgin Island | Investment holding | 1 share of US$1 each | 100%# |
| Tai Ping Carpets Limited | Hong Kong | Carpet trading | 2,000,000 shares of HK$10 each | 100% |
| Foshan Nanhai Tai Ping Carpets Company Limited | The People's Republic of China | Carpet manufacturing | US$5,000,000 | 80% |
| Suzhou Shuilian Mattress Co. Ltd. | The People's Republic of China | Mattress manufacturing and trading | US$1,730,000 | 82% |
| Tai Ping Carpets International Trading (Shanghai) Company Limited | The People's Republic of China | Carpet trading | US$200,000 | 100% |
| Carpets International Thailand Public Company Limited | Thailand | Carpet manufacturing | 10,000,000 shares of Baht 10 each | 99% |
| Tai Ping Carpets (S) Pte. Limited | Singapore | Carpet trading | S$5,000,000 | 100% |
| Tai Ping Carpets Interieur GmbH | Germany | Carpet trading | Euro 511,292 | 100% |
| Tai Ping Carpets Europe SAS | France | Carpet trading | Euro 350,000 | 100% |

# Directly held by the Company

| Name | Country of incorporation and operations | Principal activities | Issued and paid-up capital | Percentage of equity attributable to the Group |
|---|---|---|---|---|
| **Subsidiaries** (Continued) | | | | |
| Edward Fields, Inc. | USA | Carpet manufacturing | US$100,000 | 100% |
| Premier Yarn Dyers, Inc. | USA | Yarn dyeing | 1,100 shares of US$100 each | 100% |
| Tai Ping Carpets Americas, Inc. | USA | Carpet trading | 220,000 shares of US$1 each | 100% |
| White Oak Carpet Mills, Inc. | USA | Carpet manufacturing | 918 shares of US$1 each | 100% |
| **Associate** | | | | |
| Philippine Carpet Manufacturing Corporation | The Philippines | Carpet manufacturing | 1,017,581 shares of PHP 100 each | 33% |
| **Jointly Controlled Entities** | | | | |
| Weihai Shanhua Huabao Carpet Company Limited | The People's Republic of China | Carpet manufacturing | US$15,090,000 | 49% |
| Weihai Shanhua Premier Carpet Company Limited | The People's Republic of China | Carpet manufacturing | US$5,400,000 | 49% |
| Weihai Shanhua Floorcovering Products Company Limited | The People's Republic of China | Manufacture of carpet underlay | US$145,000 | 42% |

* None of the subsidiaries had issued any debt securities at the end of the year.

# Major Investment Properties

| Location | Lot number | Type | Lease term |
| --- | --- | --- | --- |
| Units A-E , 10th floor<br>Mai Gar Industrial Building,<br>146 Wai Yip Street<br>Kwun Tong,<br>Kowloon | 58/1000 shares of and<br>in Kwun Tong Inland<br>Lot Nos. 297 and 298 | Industrial | 2047 |
| The whole of Level 3 and Car Park Spaces<br>Nos. 30,31 and 32 on basement,<br>May Fair Tower, Nos. 85 and 87 Fumin Road,<br>Jingan District, Shanghai,<br>China | N/A | Commercial | 2042 |
| Rooms 1305-1307* and 1317-1320,<br>Tower A, Regent Centre,<br>63 Wo Yi Hop Road,<br>Kwai Chung,<br>Hong Kong | 592/71750 shares of<br>and in remaining portion<br>of Lot No. 299 in<br>D.D. 444 | Commercial | 2047 |

* Rooms 1305 and 1306 were sold in January 2007.

# Senior Management

| Name | Position held | Age* | Joined Group | Business Experience |
|---|---|---|---|---|
| Mr. Richard Bascetta | Real Estate & Facilities Director, Global | 59 | 2005 | Facilities Management |
| Ms. Rita S. H. Chan | Chief Information Officer | 41 | 2006 | Information technology |
| Mr. Eric A. S. Cooper | Group Technical Director | 55 | 2005 | Carpet manufacturing |
| Mr. Leslie C. Fillmann | Senior Vice President Commercial, Design Studios | 51 | 1999 | Carpet design |
| Mr. Jack S. Gates | President Premier Yarn Dyers, Inc. | 67 | 1983 | Carpet & textiles manufacturing |
| Mr. John P. Goggin | Managing Director Commercial, USA | 53 | 2004 | Carpet sales & marketing |
| Mr. Adam J. S. Jones | Managing Director Commercial, Europe | 35 | 2005 | Carpet sales & marketing |
| Mr. Robert E. Keilitz | Managing Director RBC, Asia | 58 | 2006 | Carpet sales & marketing |
| Ms. Susan F. MacKenzie | Managing Director RBC, USA | 45 | 2005 | Carpet sales & marketing |
| Mr. Raymond W. M. Mak | Chief Financial Officer & Company Secretary | 43 | 2005 | Financial management |
| Mr. Richard N. Morris | Managing Director Commercial, Asia | 43 | 2004 | Carpet sales & marketing |
| Mr. William J. Palmer | Managing Director Commercial, Global | 46 | 1999 | Carpet sales & marketing |
| Mr. Chalermchai Puapipat | Managing Director Carpets Inter | 41 | 1998 | Carpet manufacturing sales & marketing |
| .Ms. Simone S. Rothman | Chief Marketing Officer | 47 | 2004 | Marketing, PR & business development |
| Ms. Catherine Vergez | Managing Director RBC, Europe | 44 | 1991 | Carpet sales & marketing |
| Mr. Rainer H. Zimmermann | Senior Vice President Global Operations | 50 | 2006 | Manufacturing & logistics |

* age as at 20 April 2007

# Corporate Information



**Auditors**
BDO McCabe Lo Limited

**Bankers**
The Hong Kong and Shanghai Banking Corporation Limited
Standard Chartered Bank
Shanghai Commercial Bank Limited
Chong Hing Bank Limited

**Company Secretary and Qualified Accountant**
Raymond W. M. Mak

**Registrars and Transfer Agent**
The Bank of Bermuda Limited
Bank of Bermuda Building,
6 Front Street,
Hamilton, Bermuda

**Branch Registrars and Registration Office**
Computershare Hong Kong Investor Services Limited
46th Floor, Hopewell Centre,
183 Queen's Road East, Wanchai
Hong Kong.

**Registered Office**
Canon's Court
22 Victoria Street
PO Box HM 1179
Hamilton HM EX
Bermuda.

**Principal Office in Hong Kong**
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**Stock Exchange Code: 146**