



DREAM INTERNATIONAL LIMITED

德 林 國 際 有 限 公 司

(incorporated in Hong Kong with limited liability)
(於香港註冊成立之有限公司)

Stock Code 股份代號 : 1126

ANNUAL REPORT

2007年報

2007





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International
Limited



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Corporate Information

Board of Directors

Executive Directors

Mr. Kyoo Yoon CHOI (*Chairman and Executive Director*)

Mr. Young M. LEE (*Executive Managing Director and
Chief Financial Officer*)

Mr. James WANG

Mr. Jung Kuk LEE (*appointed on 31 May 2007*)

Mr. Hyun Ho KIM (*appointed on 31 May 2007*)

Mrs. Shin Hee CHA (*President*) (*resigned on 31 May 2007*)

Mr. Tae Sub CHOI (*Vice-president and Chief Operation Officer*)
(*resigned on 31 May 2007*)

Independent Non-executive Directors

Mr. Valiant, Kin Piu CHEUNG

Professor Cheung Heon YI

Dr. Chan YOO

Audit Committee

Professor Cheung Heon YI (*Chairman*)

Mr. Valiant, Kin Piu CHEUNG

Dr. Chan YOO

Remuneration Committee

Dr. Chan YOO (*Chairman*)

Mr. Valiant, Kin Piu CHEUNG

Professor Cheung Heon YI

Mr. Young M. LEE

Registered Office and Principal Place of Business

8th Floor

Tower 5, China HK City

33 Canton Road

Tsimshatsui Kowloon

Hong Kong

Company Secretary

Mr. Chi Chung SHUM, CPA

Auditor

PricewaterhouseCoopers

Certified Public Accountants

33/F, Cheung Kong Center

2 Queen's Road Central

Hong Kong

Authorised Representatives

Mr. Young M. LEE

Mr. Chi Chung SHUM

Principal Bankers

The Hongkong and

Shanghai Banking Corporation Limited

Citibank, N.A.

Shinhan Finance Limited

Share Registrar

Tricor Abacus Limited

26/F., Tesbury Centre

28 Queens Road East

Hong Kong

Financial Relations Consultant

Strategic Financial Relations Limited

Unit A, 29/F., Admiralty Centre I

18 Harcourt Road, Hong Kong

Website Address

www.dream-i.com.hk

Stock Code

Stock Exchange, Hong Kong 1126

Access to Reuters 1126.HK

Access to Bloomberg 1126:HK

Chairman's Statement

Mr. Kyoo Yoon Choi
Chairman



Dear Shareholders,

In 2007, the continuing escalation in labour and material costs, appreciation of the Renminbi, and lowered refund on export value-added tax in China represented key obstacles that toy manufacturers in the country were confronted with. To operate under such challenging conditions, Dream International Limited (the “Company”) and its subsidiaries (collectively the “Group”) implemented various strategies of business restructuring and revenue enhancement which achieved a fair level of success during the year under review.

In terms of business restructuring, we chose to close our plant near Shanghai in the fourth quarter of the financial year and concentrate our mainland production activities at our four plants in inland China. The benefit of such a move includes taking advantage of more agreeable labour rates, boosting efficiency and taking greater control of costs. Meanwhile, operation of our plant in Vietnam progressed smoothly, driving our overall gross profit margin up to 15.6% from 14.8% last year. Also part of our restructuring efforts, the management team and workforce at Dream INKO Co. Ltd (“Dream INKO”) have been streamlined with a resultant saving of HK\$11.2 million in administrative expenses, thus significantly narrowing our operating loss. For enhancing profitability, we carefully reviewed our product mix and continued to migrate towards higher margin, larger volume orders.

To broaden our revenue streams, we have redoubled efforts at attracting new customers. For our steel and plastic toys business, we successfully secured a character license with The Walt Disney Company (“Disney”) to manufacture scooters and ride-on products to meet its China market objectives. Moreover, we were able to include a marketing company and a large US retail chain store into our expanding customer portfolio. As for our plush stuffed toys operation, we took the initiative of enriching our product mix, which included bolstering our offering of electronic educational plush toys as they have enjoyed strong demand in the US market. We also reached an agreement with a well-known entertainment company and served as their new original equipment manufacturer. In securing contracts with numerous distinguished customers, we have thus proven that our products and services are of the highest quality, and our Company is worthy of trust and respect.



While we will continue to make every effort to improve efficiency and profitability, we are fully aware that the business environment in China will remain difficult in the foreseeable future. Pressures associated with the country's rising labour cost, currency appreciation, and aftershocks of new labour laws are expected to persist. Customers have realised the operational complexion in China has changed as well and have been willing to bear part of the burden of increased costs. Compounding matters are the economic uncertainties which now loom over the US, a significant toy market. Unsurprisingly, such harsh conditions have already accelerated the consolidation of the toy industry, weeding out less competitive players and leaving the fittest ones, like Dream International Limited, in the industry.

Catering for the challenging operational environment in China, our Vietnam operations are progressing on schedule with two more plants expected to open in 2008. Likewise, our efforts in restructuring the Shanghai and Shenzhen plants are underway and expected to conclude this year. The reorganisation of our production bases will allow us to generate greater profits through enhanced efficiency, thus taking full advantage of new business opportunities.

Appreciation

On behalf of the Board, I would like to take this opportunity to express my appreciation to the management team and staff for their commitment and contributions to the Group. I would also like to extend my gratitude to our shareholders, business partners and customers for their loyal support over the past year.

Kyoo Yoon Choi
Chairman

Hong Kong,
18 April 2008

Management Discussion and Analysis

Financial Review

Toy manufacturers in China continued to face challenges in 2007. To cope with the difficult times, the Group implemented a series of measures to restructure its business. For the year ended 31 December 2007, the Group strategically eliminated small quantity orders and focused on serving larger scale and higher margin customers, hence its turnover decreased by 12.7% to HK\$946.3 million (2006: HK\$1,084.4 million). Its operations in inland China and Vietnam were on smooth track, with gross profit down only by 7.5% to HK\$148.0 million (2006: HK\$160.0 million), in spite of heavier cost burden from rising labour costs in China and high material costs, as well as appreciation of the Renminbi. As for the Group's gross profit margin, it improved from 14.8% to 15.6%.

The restructuring of Dream INKO allowed it to cut its own administrative expenses by 25.3% to HK\$33.0 million and narrowed the Group's operating loss to HK\$15.2 million, a significant recovery when compared to last year's loss of HK\$117.8 million. With operating performance improved and the write-back of over-provision for Hong Kong profits tax booked in the first half of this year, loss attributable to equity holders for the entire year shrank by almost 96.3% to HK\$4.8 million (2006: loss of HK\$129.7 million). Excluding one-off goodwill impairment losses incurred in 2006, the Group's loss still had a 83.6% slash.

The Group maintained a healthy financial position with cash and bank deposits (excluding long-term structured deposits) of HK\$107.2 million (31 December 2006: HK\$82.8 million) as at 31 December 2007.

Business Review

During the year under review, the Group continued to strengthen its foundation by restructuring its business. In terms of cost control, the Group shifted a larger portion of its production to inland China where labour costs are relatively lower. The Group also expanded its production capacity in Vietnam to alleviate pressure from the appreciating Renminbi. With a streamlined workforce and corporate structure, the Group was able to save on administrative expenses and improve operational efficiency. To expand its revenue source, the Group secured quality customers for existing products and enriched its product mix. It focused on higher margin customers and products to enhance profitability.

Product Analysis

Plush stuffed toys recorded revenue of HK\$801.3 million, representing 84.7% of the Group's total turnover. Original Equipment Manufacturing ("OEM") business continued to be the Group's core business and accounted for 83.1% of the revenue of the plush stuffed toy segment. The Group maintained close cooperation with renowned character owners and licensors as well as a famous international fast food chain that became the Group's customer in the second half of 2006. In the first quarter of 2008, the Group secured a renowned entertainment company as a new customer and has begun manufacturing plush toys for the customer's North American markets.

Management Discussion and Analysis

Revenue from Original Design Manufacturing (“ODM”) business amounted to HK\$135.6 million during the year, accounting for 16.9% of the turnover of the plush stuffed toy segment. Since interactive educational electronic plush toys were launched in 2006, they have been well received in the market and attracting regular orders from a retail chain store. Sales contributions from these featured products are expected to increase in 2008.

Steel and plastic toys accounted for the remaining 15.3% of the Group’s total turnover. During the year, the Group secured new customers, a US retail chain store giant and a marketing company that distributes toys to major US retailers, and accordingly diversified the channels for it to penetrate the US market. Encouraged by the success of a scooter product it jointly developed with the Group, the marketing firm has placed orders for tricycles and other ride-on products in 2008. In May 2007, the Group secured a character license from Disney to manufacture scooters and ride-on products for Disney’s China market and the first shipment was made in August 2007. At the same time, the Group also expanded the China market with scooters and inline skates under the “Great” and “Far Great” brands. Building on positive market responses to its products, the Group will continue to explore more business opportunities in the US and China markets.

Market Analysis

For the year ended 31 December 2007, North America remained as the Group’s largest market and accounted for 44.3% of the Group’s total turnover, attributable mainly to the securing of new customers by the steel and plastic toys segment. Japan was the second largest market of the Group and its turnover contribution grew to 29.9%. Contribution from this market increased because the Group retained relatively more Japanese customers who offer higher profit margins. Another major market Europe brought in 18.0% of the Group’s turnover which was similar to last year, while the proportion from the China market increased slightly to 6.9%.

Operational Analysis

The Group had 10 plants in operation during the year, of which nine were in China and one in Vietnam, running at an average utilisation rate of 85.4%. It closed a plush toy plant near Shanghai in the fourth quarter in 2007 to cope with rising labour costs in urban areas in China and focused its attention on operating the four plants in inland cities, namely Shuyang in Jiangsu Province, Beiliu in Guangxi Province, as well as Mingguang and Chaohu in Anhui Province.

To mitigate the increasing manufacturing costs in China, the Group expanded its production base in Vietnam and invested US\$450,000 in the construction of a fabric plant in the second half of 2007. The new plant will be equipped with facilities for fabric dyeing and a polyester line relocated from Shanghai and has capacity to produce 200,000 yards of fabric per month. It is scheduled to commence trial production in the first half of 2008 and mass production in the second half year. With the support of its own material and processing lines, the Group will be able to boost production efficiency in Vietnam notably.

Management Discussion and Analysis

Prospects

Looking ahead, with the Renminbi appreciating continuously and raw material and labour costs climbing, and the Chinese government cutting export value-added tax refund and introducing new labour laws, the operational environment in the country is expected to remain stern in the coming year. This, together with the downturn of the US economy affecting consumption sentiment worldwide, will create testing times for the toy industry. However, as more and more small manufacturers are ousted by the tough market environment, sizeable players like Dream International Limited will benefit. The fact that the Group has been able to transfer certain rising costs to customers is a clear sign of its growing bargaining power in the market. With the overall industry trend taken into consideration, the Group is prudently optimistic about its business in the future.

While China will continue to be the main production base, the Group will also be shifting part of its operations to Vietnam to take advantage of the lower labour costs there. In addition to the new fabric plant currently being built, the Group will set up one more plush toy plant with 1,000 sewing machines in Vietnam in 2008 to boost economies of scale and cost-effectiveness. For the operation in China, the Group is in the process of reducing production of a plush toy plant near Shanghai to concentrate production activities in inland China. The Group expects to see the utilisation rates of its production facilities and profit margins to increase after its production bases are restructured.

To sharpen its competitive edges, the Group will inject more resources into R&D of higher margin products and explore new alliances with potential customers who are looking for quality and reliable manufacturing partners. Boasting advantages in production capacity, quality control and design ability, the Group believes it will be a preferred partner to major multi-national customers and the resultant business will brace its position as the largest plush stuffed toy manufacturer in the world.

Directors and Senior Management

Executive Directors

Mr. Kyoo Yoon Choi, aged 59, is the Chairman and Executive Director of the Company and the founder of the Group. He studied at Seoul National University in Korea between 1968 and 1972 and graduated with a bachelor's degree in engineering. Prior to setting up the Group in Korea in 1984, Mr. Choi had over eight years of experience in the plush toy business at Daewoo Corporation, which was one of the leading conglomerates in Korea at the time. Mr. Choi is responsible for the strategic planning and overall business development of the Group.

Mr. Young M. Lee, aged 52, is the Executive Managing Director and the Chief Financial Officer of the Company. Mr. Lee has 20 years of working experience in US in the areas of accounting and finance such as public accounting, consulting to financial institutions, mergers and acquisitions, corporate controllership and investment banking. Prior to joining the Group in May 2001, Mr. Lee was the Managing Director of Kohap (Hong Kong) Ltd., which is the trading and financing arm of a Korean conglomerate, Kohap Ltd.. He is responsible for the overall financial management, strategic and business planning of the Group.

Mr. James Wang, aged 46, is the Managing Director of Dream International USA. He joined Dream International USA on 1 July 1991 and has been in charge of the Group's marketing function in the US. Mr. Wang graduated from the University of California, Los Angeles, with a bachelor degree in business administration in 1986. Prior to joining the Group, Mr. Wang had extensive experience in the fields of logistics and trading from his previous employments with Trans-union Line, KAL Trading Co. and Daewoo America Corp. He was appointed as an Executive Director on 1 April 2005.

Mr. Jung Kuk Lee, aged 46, has been acting as the managing director of Dream Vina Co., Ltd. ("Dream Vina"), a wholly owned subsidiary of the Company, since 1 July 2004. He pioneered to set up the Dream Vina successfully in Ho Chi Minh City of Vietnam in 2004. He first joined C & H Co., Ltd., the immediate holding company of the Company, in June 1989 and was specified in sales and marketing function. In 1995, he was relocated to Shenzhen factory to be in-charge of the sales and quality control functions of the Company before relocated to Vietnam. Prior to joining C & H Co., Ltd., Mr. Lee acquired a year of working experience in Mun-Kyung Savings & Loan Association in South Korea. Mr. Lee graduated from the Kyung-Buk University in South Korea, with a bachelor degree of German literature in 1988.

Mr. Hyun Ho Kim, aged 42, is currently the head of accounting department of the Company. He joined the accounting department of C & H Co., Ltd. in October 1994. After nine years of service, Mr. Kim was gradually promoted to the position of general manager before he was relocated to Hong Kong to take charge of the accounting department of the Company in October 2003. Prior to joining C & H Co., Ltd., Mr. Kim acquired eight years comprehensive accounting experience in Poong Han Co., Ltd., a manufacturer of fabric and yarn, in South Korea. Mr. Kim graduated from the Seok-Yeong University in South Korea, with a bachelor degree of Economics in 1995.

Directors and Senior Management

Independent Non-executive Directors

Mr. Valiant, Kin Piu Cheung, aged 62, was a partner at KPMG, a leading international accounting firm in Hong Kong. Mr. Cheung has extensive experience in assurance and corporate finance work, particularly on trading and manufacturing corporations in Hong Kong and the People's Republic of China (the "PRC"), and has assisted a number of companies in obtaining a listing on stock exchanges in Hong Kong, the PRC, Singapore and the US. In addition, he has provided financial advisory and due diligence services to foreign investors on investments in the PRC. Mr. Cheung is a fellow member of the Institute of Chartered Accountants in England and Wales and the Hong Kong Institute of Certified Public Accountants. He was appointed as the Company's Independent Non-executive Director on 22 October 2001.

Professor Cheong Heon Yi, aged 43, received his bachelor's degree and a master's degree in business administration from Seoul National University in Korea. Professor Yi was also awarded a philosophy of doctorate degree in accounting in 1997 from the University of California, Los Angeles. Professor Yi has taught at the University of California, Los Angeles for a year before joining the Hong Kong Polytechnic University in 1997. Professor Yi's research interests include financial reporting and corporate governance. His teaching focuses on financial accounting at the undergraduate level and financial reporting and corporate governance at the postgraduate level. He was appointed as the Company's Independent Non-Executive Director on 22 November, 2003.

Dr. Chan Yoo, aged 43, graduated from Massachusetts Institute of Technology ("MIT"), Cambridge, MA, U.S. with a bachelor degree in Electrical Engineering and Computer Science in 1989. He obtained his master degree in Nuclear Engineering from MIT in 1991. He was conferred his PhD in Nuclear Engineering from MIT in 1995. Dr. Yoo gained over four years consulting experience from an international consultancy firm McKinsey & Company, Inc., Chicago office in U.S. and Seoul office in Korea. In the year 2000, Dr. Yoo set up McQs, incorporated in Seoul, Korea to provide business consulting services for Korean manufacturing companies to achieve world-class operational excellence and has been the Chief Executive Officer of the company since then. He was appointed as an independent non-executive director with effect from 30 September 2004.

Senior Management

Mr. Yong Kook Kim, aged 59, is the Vice-president of J.Y. Toys Co., Limited ("J Y Toys"). He joined the Group on 1 June 1987 and is in charge of the day-to-day operation and management of J Y Toys and J. Y. Plasteel (Suzhou) Co. Ltd..

Mr. Man Jin Cho, aged 66, is the Executive Managing Director of C & H Suzhou. He has extensive experience in the field of acrylic knitted fabric manufacturing. He joined the Group on 1 May 1997 and helped the Group in establishing C & H Plush in the same year to expand into acrylic knitted fabric business. Mr. Cho is now responsible for the production operation of acrylic knitted fabric and developing materials for plush toys.

Mr. Dong Wook Cha, aged 47, is the Head of accounting and administration department of the Company. Mr. Cha has over seven years of experience in the field of accounting from his employments with Dongkook Trading Co. and Hyundai Heavy Industrial Co., Ltd. He joined C & H Korea on 1 February 1986 and has been working in the accounting and administration department of the Group since 1996.

Report of the Directors

The directors submit their report together with the audited financial statements for the year ended 31 December 2007.

Principal activities and geographical analysis of operations

The principal activities of the Company are the design, development, manufacturing and sale of plush stuffed and steel and plastic toys and investment holding. The principal activities of the subsidiaries are set out in Note 9 to the financial statements.

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

Results and appropriations

The results of the Group for the year are set out in the consolidation income statement on page 36.

The directors do not recommend the payment of a dividend.

Reserves

Movements in the reserves of the Group and of the Company during the year are set out in Note 17 to the financial statements.

Property, plant and equipment

Details of the movements in property, plant and equipment of the Group and of the Company are set out in Note 7 to the financial statements.

Distributable reserves

Distributable reserves of the Company at 31 December 2007, calculated under section 79B of the Hong Kong Companies Ordinance, amounted to HK\$132,781,000 (2006: HK\$107,319,000).

Report of the Directors

Purchase, sale of redemption of securities

During the year ended 31 December 2007, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's shares.

Five year financial summary

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on pages 103 to 104.

Share option scheme

The Company has a share option scheme which was adopted on 22 January 2002 whereby the directors of the Company are authorised, at their discretion, to invite employees of the Group, including directors of any company in the Group, to take up options to subscribe for shares of the Company. The exercise price of the options is the highest of (i) the nominal value of the shares, (ii) the closing price of the shares on The Stock Exchange of Hong Kong Limited (the "SEHK") on the date of grant and (iii) the average closing price of the shares on the SEHK for the five business days immediately preceding the date of grant. The options may be exercised progressively after one to three years from the date of grant and are exercisable for a period to be notified by the directors to each option holder upon the grant of the option. Such period will not exceed ten years from the date on which the option is granted.

The maximum number of shares which may be issued upon the exercise of all outstanding options and yet to be exercised under the share option scheme shall not exceed 30% of the issued share capital of the Company from time to time. Subject always to the above overall limit, the directors may grant options under the share option scheme, generally and without further authority, in respect of such number of shares which may be issued upon exercise of all options to be granted under the share option scheme not exceeding 10% of the issued share capital of the Company as at 7 February 2002, being the date on which the Company's shares were listed on the SEHK. For the purpose of calculating the above, options lapsed in accordance with the share option scheme shall not be counted.

The total number of securities available for issue under the share option scheme as at 31 December 2007 was 46,471,000 shares (including options for 14,346,000 shares that have been granted but not yet lapsed or exercised) which represented 6.95% of the issued share capital of the Company at 31 December 2007. In respect of the maximum entitlement of each participant under the scheme, the number of securities issued and to be issued upon exercise of the options granted to each participant in any 12-month period is limited to 1% of the Company's ordinary shares in issue.

Report of the Directors

As at 31 December 2007, the directors individually and other employees in aggregate of the Company had the following interests in options to subscribe for shares of the Company granted at nominal consideration under the share option scheme of the Company. The options are unlisted. Each option gives the holder the right to subscribe for one ordinary share of the Company of par value US\$0.01 each.

| | Date granted | Period during which options exercisable (Note 1) | Exercise price per share | Number of options | | |
|--|-----------------|---|--------------------------|---------------------------|------------------------------------|-----------------------------|
| | | | | Balance at 1 January 2007 | Lapsed during the year (Note 2) | Balance at 31 December 2007 |
| Directors: | | | | | | |
| Shin Hee Cha (resigned on 31 May 2007) | 2 January 2004 | 2 January 2005 to 2 January 2014 | HK\$1.87 | 3,500,000 | – | 3,500,000 |
| Young M. Lee | 7 February 2002 | 7 February 2003 to 7 February 2012 | HK\$1.18 | 1,360,000 | – | 1,360,000 |
| Tae Sub Choi (resigned on 31 May 2007) | 15 April 2003 | 15 April 2004 to 15 April 2013 | HK\$1.43 | 1,365,000 | 1,365,000 (Note 3) | – |
| James Wang | 7 February 2002 | 7 February 2003 to 7 February 2012 | HK\$1.18 | 520,000 | – | 520,000 |
| Jung Kuk Lee (appointed on 31 May 2007) | 7 February 2002 | 7 February 2003 to 7 February 2012 | HK\$1.18 | 520,000 | – | 520,000 |
| Employees in aggregate: | 7 February 2002 | 7 February 2003 to 7 February 2012 | HK\$1.18 | 4,161,000 | 520,000 (Note 4) | 3,641,000 |
| | 15 April 2003 | 15 April 2004 to 15 April 2013 | HK\$1.43 | 455,000 | | 455,000 |
| | 2 January 2004 | 2 January 2005 to 2 January 2014 | HK\$1.87 | 5,350,000 | 1,000,000 (Note 4) | 4,350,000 |
| | | | | <u>17,231,000</u> | <u>2,885,000</u> | <u>14,346,000</u> |

Report of the Directors

Notes:

- (1) The maximum percentage of the share options that may be exercised is determined in stages as follows:

| | Percentage of share options granted |
|---|--|
| On or after 1st year anniversary of the date of grant | 30% |
| On or after 2nd year anniversary of the date of grant | another 30% |
| On or after 3rd year anniversary of the date of grant | another 40% |

- (2) Pursuant to the condition of the share option scheme, any unexercised number of options granted to any employee will lapse three months after the employee ceases employment relationship with the Company.
- (3) This 1,365,000 share options related to Mr. Tae Sub Choi who resigned as director of and ceased employment relationship with the Company on 31 May 2007. These outstanding share options were lapsed by 1 September 2007.
- (4) This 1,520,000 share options related to various employees who left the Group on or before 30 September 2007. These outstanding share options were lapsed by 31 December 2007.
- (5) The options granted to the directors are registered under the names of the directors who are also the beneficial owners.

The life of the above granted share options is ten years commencing on the date on which an option is granted in accordance with the scheme.

Directors' interests in contracts

Apart from the related party transactions as disclosed in Note 33 to the financial statements, no other contracts of significance in relation to the Group's business to which the Company, any of its fellow subsidiaries or its holding company 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.

Biographical details of directors and senior management

Brief biographical details of directors and senior management are set out on page 9 to 10.

Report of the Directors

Directors

The directors during the year were:

Chairman and executive director

Kyoo Yoon Choi

Executive directors

Shin Hee Cha (resigned on 31 May 2007)

Tae Sub Choi (resigned on 31 May 2007)

Young M. Lee

James Wang

Jung Kuk Lee (appointed on 31 May 2007)

Hyun Ho Kim (appointed on 31 May 2007)

Independent non-executive directors

Valiant, Kin Piu Cheung

Cheong Heon Yi

Chan Yoo

In accordance with articles 101 and 92 of the Articles of Association, Mr. Young M. Lee, Mr. James Wang, Mr. Valiant Kin Piu Cheung, Mr. Jung Kuk Lee and Mr. Hyun Ho Kim shall retire from office by rotation at the Annual General Meeting and Mr. Young M. Lee, Mr. James Wang, Mr. Jung Kuk Lee and Mr. Hyun Ho Kim being eligible, offer themselves for re-election at the Annual General Meeting. Mr. Valiant Kin Piu Cheung does not offer himself for re-election and accordingly will cease to be Director on conclusion of the Annual General Meeting.

Directors' service contracts

The service contract of Valiant, Kin Piu Cheung, the independent non-executive director, was renewed by the Board of Directors on 22 October 2007 for a term of period commencing on 22 October 2007 to the forthcoming Annual General Meeting.

The service contract of Cheong Heon Yi, the independent non-executive director, was renewed by the Board of Directors on 21 November 2007 for a term of 2 years commencing on 22 November 2007.

The service contract of Chan Yoo, the independent non-executive director, was renewed by the Board of Directors on 30 September 2006 for a term of 2 years commencing on 30 September 2006.

Their remuneration is determined by the Board of Directors on the renewal of their service contracts.

No director proposed for re-election at the forthcoming Annual General Meeting has an unexpired service contract which is not determinable by the Company or any of its subsidiaries within one year without payment of compensation, other than normal statutory obligations.

Report of the Directors

Directors' and chief executives' interests and short positions in shares, underlying shares and debentures of the Company or any associated corporation

At 31 December 2007, the interests and short positions of each director and chief executive in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of the Securities and Futures Ordinance (the "SFO")) as recorded in the register required to be kept by the Company under Section 352 of Part XV of the SFO or otherwise notified to the Company and the SEHK pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") were as follows:

(i) Long positions in ordinary shares of US\$0.01 each

| | Number of shares held | | | Total | Percentage of issued share capital of the Company |
|--|--------------------------------|---------------------|-------------------------|-------------|---|
| | Personal interests (Note 1) | Family interests | Corporate interests | | |
| The Company | | | | | |
| - Kyoo Yoon Choi | - | - | 455,000,000 (Note 2) | 455,000,000 | 68.06% |
| - Young M. Lee | 1,740,000 | - | - | 1,740,000 | 0.26% |
| - Jung Kuk Lee (appointed on 31 May 2007) | 170,000 | - | - | 170,000 | 0.03% |
| - Tae Sub Choi (resigned on 31 May 2007) | 585,000 | - | - | 585,000 | 0.09% |
| C & H Co., Ltd | | | | | |
| - Kyoo Yoon Choi | 189,917 | 124,073 (Note 3) | - | 313,990 | 61.03% |
| - Shin Hee Cha (resigned on 31 May 2007) | 21,319 | - | - | 21,319 | 4.14% |
| - Tae Sub Choi (resigned on 31 May 2007) | 5,685 | - | - | 5,685 | 1.10% |

Notes:

- (1) The shares are registered under the names of the directors and chief executives of the Company who are the beneficial owners.
- (2) Kyoo Yoon Choi in his own name holds approximately 36.91 % of the issued share capital of C & H Co., Ltd, and together with his wife, Woul Hee Cha, hold approximately 61.03% of the issued share capital of C & H Co., Ltd, which owned 382,850,000 shares in the Company. In addition, Kyoo Yoon Choi beneficially owns 100% of interest of Uni-Link Technology Limited which owned 72,150,000 shares of the Company.
- (3) The wife of Kyoo Yoon Choi, Woul Hee Cha, holds approximately 24.12% of the issued share capital of C & H Co., Ltd.

Report of the Directors

(ii) Long positions in underlying shares of the Company

The directors and chief executives of the Company have been granted options under the Company's share option scheme, details of which are set out in the section "Share option scheme" above.

Save as disclosed above, at no time during the period was the Company, its holding company, its associates or fellow subsidiaries a party to any arrangement to enable the director and chief executive of the Company (including their spouses and children under 18 years of age) to hold any interests or short positions in the shares in or underlying shares in, or debentures of, the Company and its associated corporation required to be disclosed pursuant to the SFO or otherwise notified to the Company and the SEHK pursuant to the Model Code.

Substantial shareholders' interests and short positions in the shares and underlying shares of the Company

The register of substantial shareholders required to be kept under Section 336 of Part XV of the SFO shows that as at 31 December 2007, the Company had been notified of the following substantial shareholders' interest and short positions, being 5% or more of the Company's issued share capital. These interests are in addition to those disclosed above in respect of directors and chief executives:

| Name | <u>Capacity in which shares held</u> | <u>Number of shares held</u> | <u>Percentage of the issued share capital of the Company</u> |
|------------------------------------|--|----------------------------------|--|
| C & H Co., Ltd. (Note) | Beneficial owner | 382,850,000 | 57.27% |
| Uni-Link Technology Limited (Note) | Beneficial owner | 72,150,000 | 10.79% |

Note:

Kyoo Yoon Choi, being a director of C & H Co., Ltd., together with his wife, Woul Hee Cha, hold approximately 61.03% of the issued share capital of C & H Co., Ltd. and Kyoo Yoon Choi beneficially owns 100% of the issued share capital of Uni-Link Technology Limited. Kyoo Yoon Choi is considered to have deemed interests in the 455,000,000 ordinary shares as to approximately 68.06% of the issued shares of the Company. James Wang, being a director of the Company, is also a director of Uni-Link Technology Limited.

Save as disclosed above, as at 31 December 2007, the Company is not aware of any other registered substantial shareholder who holds 5% or more of the issued share capital of the Company.

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.

Report of the Directors

Major customers and suppliers

The percentage of sales and purchases for the year attributable to the Group's major customers and suppliers are as follows:

Sales

| | |
|---------------------------------------|-------|
| – The largest customer | 18.7% |
| – Five largest customers in aggregate | 54.9% |

Purchases

| | |
|---------------------------------------|-------|
| – The largest supplier | 5.3% |
| – Five largest suppliers in aggregate | 19.3% |

None of the directors, their associates or any shareholder (which to the knowledge of the directors owns more than 5% of the Company's share capital) had an interest in the major customers or suppliers noted above.

Connected transactions

During the year, the Group has entered into connected transactions and continuing connected transaction with connected persons and has complied with the disclosure requirements in accordance with Chapter 14A of the Rules Governing the Listing of Securities on the Main Board of the SEHK ("the Listing Rules"). The directors, including the independent non-executive directors, of the Company confirmed that the aforesaid connected transactions were entered into:

- (i) in the ordinary and usual course of business;
- (ii) either on normal commercial terms or, on terms no less favourable to the Group than available to or from independent third parties; and
- (iii) In accordance with the relevant agreements governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

The board has received from its auditor a letter confirming that the continuing connected transaction (the "Transaction"):

- (i) have been approved by the Board of the Company;
- (ii) have been entered into in accordance with the relevant agreement governing the Transaction; and
- (iii) have not exceeded the relevant caps.

During the year, the details of the continuing connected transaction, which was exempted from the approval of independent shareholders but was subject to the announcement and reporting requirements under Listing Rules, with C & H Co., Ltd. and its subsidiaries excluding the Group ("C & H Korea Group") was as follows:

- (1) On 24 August 2007, the Group renewed its property lease agreement with C & H Co., Ltd. for Dream INKO Co., Ltd ("Dream INKO")'s principal place of business in Seoul, Korea. The property lease agreement is renewable upon its expiry in July 2008. The terms of the property lease agreement were agreed after arm's length negotiation by reference to enquiries made with other landlords, tenants and real estate agents in the proximity area.

Report of the Directors

During the year ended 31 December 2007, the rental paid amounted to HK\$3,146,000 (2006: HK\$5,079,000).

Besides, details of completed connected transactions which were subject to the announcement and reporting requirements but exempted from the approval of independent shareholders for the year are set out below:

- (1) On 1 June 2007, Dream INKO entered into a Loan Agreement to lend to KTI Co., Ltd. (“KTI”), Korean Won 1,000 million for a fixed period of one year without any securities required.

KTI is wholly owned by C & H Co., Ltd., which owns 51.27% of the issued share capital of the Company. As such, KTI is a fellow subsidiary of the Company and therefore a connected person of the Company.

Details of the terms of the Loan Agreement are disclosed in the announcement dated 11 June 2007.

- (2) On 9 October 2007, Dream Vina Co., Ltd. (“Dream Vina”) a wholly owned subsidiary of the Company, entered into the Agreement of Transfer of Assets with C & H Vina Co., Ltd. (“C & H Vina”), to dispose of the Assets to C & H Vina for an aggregate consideration of US\$1,170,000.

C & H Vina is wholly owned by C & H Co., Ltd., which owns 51.27% of the issued share capital of the Company. As such, C & H Vina is a fellow subsidiary of the Company and therefore a connected person of the Company.

Details of the terms of the Agreement of Transfer of Assets are disclosed in the announcement dated 9 October 2007.

Compliance with the code on corporate governance practices

During the year ended 31 December 2007, the Company has fully complied with the Code on Corporate Governance Practice as set out in Appendix 14 of the Listing Rules.

Sufficiency of public float

Based on the information that is publicly available to the Company and within the knowledge of the directors, it is confirmed that there is sufficient public float of more than 25% of the Company’s issued shares at 18 April 2008.

Report of the Directors

Directors' interests in competing business

During the year ended 31 December 2007, C & H Korea Group, as set out below, is principally engaged in the business of properties investment in Seoul, leather the goods and accessories agency, fabric, textile manufacturing and investment holding in PRC, Vietnam and Sri Lanka through its wholly owned subsidiaries C & H Hitex Co., Ltd., Jung Yoon Textiles (Private) Limited, Vina Tarpaulin Inc. and C & H Lanka I (PVT) Ltd. Mr. Kyoo Yoon Choi, Mrs. Shin Hee Cha and Mr. Tae Sub Choi are deemed to be interested in these businesses some of which may compete with the Group's businesses as they are shareholders of C & H Co., Ltd. and Mr. Kyoo Yoon Choi is also a director of C & H Co., Ltd.

| Name of company | Nature of competing business | Remarks |
|---|---|---|
| C & H Lanka (PVT) Ltd. ("C & H Lanka") | C & H Lanka is a wholly owned subsidiary of C & H Korea. The directors of C & H Lanka are Mr. Kyoo Yoon Choi, Ms. Shin Hee Cha, and Mr. Young Dae Noh. C & H Lanka was engaged in the manufacturing of plush stuffed toys in Sri Lanka. C & H Lanka is undergoing winding-up procedure and the local court has appointed liquidators Mr. J. David & M.S. Iyayawickrama of MS SMIS Associates as directors of the company. | Pursuant to the Deed of Undertaking ¹ , C & H Lanka agreed not to engage or otherwise be involved in any business which competes or is likely to compete with the Group's business in any of the regions that the Group engages business in. Its business was limited to production of quota related plush stuffed toys and orders that could not be handled by the Group. |
| Jung Yoon Textiles (Private) Ltd. ("JY Textile") | JY Textile is a wholly owned subsidiary of C & H Korea. The directors of JY Textile are Mr. Kyoo Yoon Choi and Mr. Kyung Soon Song. JY Textile is engaged in the manufacturing and dyeing of fabrics. | JY Textile is engaged in manufacturing of fabrics and dyeing of fabrics for local customers in Sri Lanka |

The transactions with the above companies are set out in the paragraph headed "Connected transactions"

¹ In relation to the listing of the company's shares on the Main Board of the SEHK, C & H Co., Ltd. has entered into the Deed of Undertaking in favour of the company to effect that for so long as C & H Co., Ltd. and its associates are beneficially interested, directly or indirectly, whether individually or taken together, in 30% or more of the issued capital of the company, C & H Co., Ltd. will not, and C & H Co., Ltd. will procure that none of its subsidiaries, other than the Group, will engage or otherwise be involved in any business which competes or is likely to compete, either directly or indirectly, with any of the restricted business in any of the regions in which the group engages in and undertakes the restricted business (such regions include the PRC, Taiwan, Europe, the US and Japan). Such an undertaking shall extend to all subsidiaries of C & H Korea Group.

Report of the Directors

Compliance with the model code for securities

The Company has adopted a code of conduct regarding securities transactions by directors as set out in Appendix 10 of the Listing Rules. The Company has made specific enquiries of all directors and all directors have confirmed that they complied with the required standard of dealings set out therein during the year.

Audit committee

The audit committee has reviewed with the management and the Company's auditor, PricewaterhouseCoopers, the accounting principles and practices adopted by the Group and discussed internal control and financial reporting matters of the final results for year ended 31 December 2007.

Auditor

The consolidated financial statements have been audited by PricewaterhouseCoopers, who will retire and, being eligible, offer themselves for re-appointment at the forthcoming Annual General Meeting of the Company.

On behalf of the Board

Young M. Lee
Director

Hong Kong, 18 April 2008

Corporate Governance Practices

The Board of Directors of the Company (the “Board”) believes that corporate governance is essential to the sustainable success of the Company and trust that all stakeholders of the Company can benefit from better transparency and accountability of a high standard of corporate governance.

In the opinion of the Board, the Company has applied the principles and complied with the code provisions contained in the Code on Corporate Governance Practices (the “CG Code”) as set out in Appendix 14 of the Listing Rules of The Stock Exchange of Hong Kong Limited (the “SEHK”) during the year ended 31 December 2007.

Directors’ Securities Transactions

The Company has adopted the code of conduct regarding directors’ securities transactions as set out in the Model Code for Securities Transactions by Directors of Listed Issuers (the “Model Code”) of the Listing Rules. All the directors have confirmed that they have complied with the required standards as set out in the Model Code throughout the year.

Board of Directors

As at 31 December 2007, the Board consisted of five executive directors, namely Mr. Kyoo Yoon Choi (Chairman), Mr. Young M. Lee (Executive Managing Director and CFO), Mr. James Wang, Mr. Jung Kuk Lee and Mr. Hyun Ho Kim, and three independent non-executive directors (“INEDs”) (collectively the “Directors”), namely Mr. Valiant Kin Piu Cheung, Professor Cheong Heon Yi and Dr. Chan Yoo. There is no financial, business, family or other material/relevant relationship. The principal functions of the Board are to supervise the management of the business and affairs; to approve the strategic plans, investment and funding decision; to review the Group’s financial performance and operative initiatives. The role of INEDs is to bring an independent and objective view to the Board’s deliberations and decisions. Mr. Valiant Cheung was a retired audit partner of KPMG and Professor Yi is currently teaching financial accounting and corporate governance in the Accountancy Faculty of the Hong Kong Polytechnic University. The Board considers both of them have profound professional qualifications and expertise in accounting and financial management so that they are of sufficient caliber and number for their independent views to carry weight. The Company has received from each of the INEDs, an annual confirmation of his independence pursuant to Rule 3.13 of the Listing Rules. The Company considers all of the INEDs are independent.

The Company has arranged for appropriate liability insurance since 2002 to indemnify its Directors for their liabilities arising out of corporate activities. The insurance coverage is reviewed on an annual basis.

Corporate Governance Practices

The Board will conduct meeting on a regular basis and on an ad hoc basis so far as the business required. The Board held a total of six board meetings during the year. The INEDs may take independent professional advice at the Company's expense in carrying out their functions. The Board is supplied with relevant information by the senior management pertaining to matters to be brought before the Board for decision as well as reports relating to operational and financial performance of the Group before each regular board meeting. At least 14 days notice of a regular board meeting is given to all directors to give them the opportunity to attend. Board papers are dispatched to the directors at least 3 days before the meeting to ensure that they have sufficient time to review the papers and be adequately prepared for the meeting.

Directors' attendance at the Board meetings held during the year:

| Name of director | <u>Number of attendance</u> |
|---|-----------------------------|
| Kyoo Yoon Choi (<i>Chairman</i>) | 3/6 |
| Shin Hee Cha (resigned on 31 May 2007) | 1/6 |
| Tae Sub Choi (resigned on 31 May 2007) | 1/6 |
| Young M. Lee | 6/6 |
| James Wang | 6/6 |
| Jung Kuk Lee (appointed on 31 May 2007) | 4/6 |
| Hyun Ho Kim (appointed on 31 May 2007) | 4/6 |
| Valiant, Kin Piu Cheung | 6/6 |
| Cheong Heon Yi | 6/6 |
| Chan Yoo | 5/6 |

Delegation by the Board

The Board is responsible for determining the overall strategy and approving the annual business plan of the Group, and ensuring the business operations are properly planned, authorised, undertaken and monitored. All policy matters of the Group, material transactions where there is conflict of interests, considered as being notifiable or connected transactions with meaning ascribed to by the Listing Rules from time to time should be reserved to the decision of the Board.

The Board has delegated functions that are necessary and incidence to carry out the decision of the Board or to facilitate the day-to-day operation of the Group in ordinary course of business to the executive management and divisional heads of different business units under the instruction / supervision of Chief Executive Officer, Chief Financial Officer and Chief Operation Officer. The Board and the management will also seek advice from the Audit Committee and Remuneration Committee. These committees are mainly composed of and chaired by INEDs. In case of urgency, executive management is empowered to make any decisions in prompt response to any opportunities and threats that might arise from time to time. However, those emergency decisions or any other exceptional decisions made by management should be reported back to the Board for ratification as soon as practical.

Corporate Governance Practices

The three independent non-executive directors are persons of high calibre, with academic and professional qualifications in the fields of finance, accounting, consulting and business management. With their experience gained from senior positions held in other companies, they provide valuable support towards the effective discharge of the duties and responsibilities of the Board. Each independent non-executive director gives an annual confirmation of his independence to the Company, and the Company considers these directors to be independent under Rule 3.13 of the Listing Rules. These three INEDs comprise the Audit and Remuneration Committees formed by the Board.

Chairman and Chief Executive Officer

The post of Chairman and Chief Executive Officer (“CEO”) are separate and are not held by the same individual to ensure their independence, accountability and responsibility. The Chairman of the Board, Mr. Kyoo Yoon Choi, is responsible formulating the strategic planning, business development, overall leadership and effective running of the Board, by ensuring that all key and appropriate issues are discussed by the Board in a timely and constructive manner.

The post of CEO, supported by other chief executives, is delegated with the authority and responsible for running the Group’s business, and implementation of the Group’s strategy in achieving the overall commercial objectives. Upon the resignation of Mr. Min on 31 December 2005, the current duties of the CEO is temporarily shared by other executive directors and key executives except the Chairman until a suitable successor is found by the Company.

Nomination, Appointment and Re-election of Directors

The Company does not have a Nomination Committee. The Board as a whole is responsible for the procedure of agreeing to the appointment of its members and for nominating appropriate person for election by shareholders at the general meeting, either to fill a casual vacancy or as an addition to the existing directors.

Those directors appointed by the Board during the year shall hold office only until the next following general meeting of the Company and shall then be eligible for re-election. The circular dispatched to the shareholders before the general meeting contains, inter alia, detailed information on election of directors including detailed biography of all directors standing for election or re-election to ensure shareholders to make an informed decision on their election.

The Company has specified the term of two years appointment for independent non-executive directors (“INEDs”) who are the only non-executive directors of the Company. None of the INEDs has entered into any service contracts with the Company which is not determinable by the Company within one year without payment of compensation, other than statutory compensation. Moreover, they are also subject to retirement by rotation and re-election at the Annual General Meeting of the Company in accordance with the Articles of Association.

Corporate Governance Practices

According to the Articles of Association of the Company, (i) any director appointed to fill a casual vacancy shall be subject to re-election by Shareholders at the Company's next following general meeting after the appointment rather than the Company's next following Annual General Meeting after the appointment, (ii) every director shall be subject to retirement by rotation at least once every three years and directors holding office as the Chairman of the Board or the Managing Director shall also be subject to retirement by rotation and (iii) the Company may remove any Director by an ordinary resolution instead of special resolution.

Remuneration Committee

The Remuneration Committee of the Company comprises one executive director and three INEDs. The Remuneration Committee was formed in January 2005 and meetings shall be held at least once a year. Two meetings were held in 2007. The attendance of each member is set out as follows:

Directors' attendance at the Remuneration Committee meetings held during the year:

| Name of director | <u>Number of attendance</u> |
|------------------------------|-----------------------------|
| Chan Yoo (<i>Chairman</i>) | 2/2 |
| Valiant, Kin Piu Cheung | 2/2 |
| Cheong Heon Yi | 2/2 |
| Young M. Lee | 2/2 |

At the meetings held during the year, the retirement compensation and incentive bonus for directors were reviewed and discussed. The Company has adopted a share option scheme on 22 January 2002, which serves as an incentive to attract, retain and motivate talented eligible staff, including the directors. Details of the share option scheme are set out in Note 16 to the financial statements. The emolument payable to directors will depend on their respective contractual terms and nature under employment contracts, if any, and as recommended by the Remuneration Committee. Details of the directors' remuneration are set out in Note 25 to the financial statements. The major roles and functions of the Group's Remuneration Committee are as follows:

1. To review annually and recommend to the Board the overall remuneration policy for the directors and key senior management officers;
2. To review annually the performance of the executive directors and key senior management officers and recommend to the Board specific adjustments in remuneration and/or reward payments;

Corporate Governance Practices

3. To ensure that the level of remuneration for Non-executive Directors and INEDs are linked to their level of responsibilities undertaken and contribution to the effective functioning of the Board of the respective companies in the Group; and
4. To ensure that no director is involved in deciding his own remuneration.

The terms of reference of the Remuneration Committee are posted on the Company's website.

Directors' and Auditor's Responsibilities for the Financial Statements

The Management provides such explanation and information to the Board so as to enable the Board to make an informed assessment of the financial and other information put before the approval by the Board.

The Directors acknowledge their responsibility to prepare financial statements for each financial year, which give a true and fair view of the state of affairs of the Group and in presenting the interim and annual financial statements, and announcements to shareholders in a timely manner. In preparing the financial statements for the year ended 31 December 2007, the directors have selected suitable accounting policies and have applied them consistently, adopted appropriate Hong Kong Financial Reporting Standards ("HKFRSs") and Hong Kong Accounting Standards ("HKASs") which are pertinent to its operations and relevant to the financial statements, made judgements and estimates that are prudent and reasonable. The Board is not aware of any material uncertainties relating to events or conditions that may cast significant doubt upon the Group's ability to continue as a going concern, the Board therefore continues to adopt the going concern approach in preparing the accounts.

The Board acknowledges its responsibility to present a balanced, clear and understandable assessment in the Company's annual and interim reports, other price-sensitive announcement and other financial disclosures required under the Listing Rules, and reports to the regulators.

The auditor's responsibilities are set out in the Independent Auditor's Report.

Corporate Governance Practices

Audit Committee

The Audit Committee of the Company comprises three INEDs. The Audit Committee shall meet at least twice a year. Two meetings were held during the year. Brief report of the major findings raised in Audit Committee meeting are presented by the Chairman of the Audit Committee to the Board immediately in the subsequent Board meeting. The minutes of the Audit Committee meetings were circulated to the Board for information and for action by the Board where appropriate. Both the INEDs and external auditor clearly expressed that no meeting without the presence of the management was required. The executive director Mr. Young M. Lee was invited to attend the meetings as the chief financial officer. The attendance of each member is set out as follows:

Directors' attendance at the Audit Committee meetings held during the year:

| Name of director | <u>Number of attendance</u> |
|------------------------------------|-----------------------------|
| Cheong Heon Yi (<i>Chairman</i>) | 2/2 |
| Valiant, Kin Piu Cheung | 2/2 |
| Chan Yoo | 2/2 |
| Young M. Lee | 2/2 |

During the year ended 31 December 2007, the Audit Committee had performed the following work:

- (i) reviewed the interim financial report for the six months ended 30 June 2007 and annual financial report for the year ended 31 December 2007;
- (ii) reviewed the major impact of the changes in accounting policies and practices and Listing Rules on the accounting treatment and financial reporting of the Company;
- (iii) reviewed the effectiveness of internal control system;
- (iv) discussed the nature and scope of the external audit and reporting obligations and reviewed the external auditor's statutory audit plan;
- (v) reviewed the findings and recommendations of the management letter from the external auditor in relation to the interim review and audit of the Group;
- (vi) reviewed and recommended for approval by the Board the 2007 audit scope, fee and supply of any non-audit services; and
- (vii) reviewed the connected transactions entered into by the Group during the year.

Corporate Governance Practices

The major roles and functions of the Audit Committee are as follows:

1. To consider the appointment of the external auditors, the audit fees, and any questions of resignation or dismissal of the external auditor of the Group.
2. To discuss with the internal and external auditors the nature and scope of the audit.
3. To review the interim and annual financial statements before submission to the Board.
4. To discuss problems and reservations arising from the interim review and final audit, and any matters the auditors may wish to discuss.
5. To review the external auditor's management letters and management's response.
6. To supervise the performance of the internal auditor's review on the Group companies' financial control, internal control and risk management systems.
7. To consider the major findings of internal investigations and management's response.

The terms of reference of the Audit Committee are posted on the Company's website.

Auditor's Remuneration

During the year under review, the remuneration paid to the Company's auditor, Messrs PricewaterhouseCoopers, is set out as follows:

| Service rendered | Fees paid/payable <i>HK\$'000</i> |
|--------------------|--------------------------------------|
| Audit services | 3,300 |
| Non-audit services | 788 |
| | 4,088 |

Corporate Governance Practices

Internal Controls

The Company set up an internal audit department in May 2006. The head of internal audit department was appointed by the Board to head the review of the effectiveness of the internal control system of the Group which cover all material controls, including financial, operational and compliance controls as well as risk management functions. The internal auditor has performed review of the internal control system of the Group for the year ended 31 December 2007 and the relevant review report has been submitted to the Audit Committee in April 2008 for consideration. The Board, through the reviews made by the Internal auditor and the Audit Committee, considers that the Group's internal control system has implemented effectively.

Communications with Shareholders

The Board recognises the importance of good communications with all shareholders. The Company's Annual General Meeting is a valuable forum for the Board to communicate directly with the shareholders. The Chairman of the Board as well as Chairmen of the Audit and Remuneration Committees together with the external auditor are present to answer shareholders' questions. An Annual General Meeting circular is distributed to all shareholders at least 21 days before the Annual General Meeting. It sets out the procedures for demanding and conducting a poll and other relevant information of the proposed resolutions. Separate resolutions are proposed at general meetings on each substantially separate issue, including the election of individual Directors. The Chairman explains the procedures for demanding and conducting a poll again at the beginning of the Annual General Meeting and (except where a poll is demanded) reveals how many proxies for and against have been filed in respect of each resolution. The results of the poll, if any, will be published in the newspapers and on the Company's website.

A key element of effective communication with shareholders and investors is the prompt and timely dissemination of information in relation to the Group. The Company has announced all its price-sensitive information, announcements, interim and annual results in a timely manner in compliance with the Listing Rules.

Corporate Governance Practices

Voting by Poll

The Company informs the shareholders (in its circulars convening a general meeting) the procedures for voting by poll and the rights of shareholders to demand a poll to ensure compliance with the requirements on the poll voting procedures. In accordance with provision 73 of Article of Association of the Company, at any general meeting a resolution put to the vote of the meeting shall be decided on a show of hands, unless a poll is (before or on the declaration of the result of the show of hands) demanded by:

- i) the chairman; or
- ii) at least three shareholders present in person or by a duly authorised corporate representative or by proxy for the time being entitled to vote at the meeting; or
- iii) any shareholder or shareholders present in person or by a duly authorised corporate representative or by proxy and representing not less than one-tenth of the total voting rights of all shareholders having the rights to vote at the meeting; or
- iv) a shareholder or shareholders present in person or by a duly authorised corporate representative or by proxy and holding shares in the Company conferring a right to vote at the meeting being shares on which an aggregate sum has been paid up equal to not less than one-tenth of the total sum paid up on all the shares conferring that right.

The Company should count all proxy votes, and except where a poll is required, the chairman of a meeting should indicate to the meeting the level of proxies lodged on each resolution, and the balance for and against the resolution, after it has been dealt with on a show of hands. The issuer should ensure that votes cast are properly counted and recorded.

The chairman of a meeting should at the commencement of the meeting ensure that an explanation is provided of:

- i) the procedure for demanding a poll by shareholders before putting a resolution to the vote on a show of hands; and
- ii) the detailed procedures for conducting a poll and then answer any questions from shareholders whenever voting by way of a poll is required.

Independent Auditor's Report



羅兵咸永道會計師事務所

PricewaterhouseCoopers
33/F, Cheung Kong Center
2 Queen's Road Central
Hong Kong
Telephone (852) 2289 8888
Facsimile (852) 2810 9888

INDEPENDENT AUDITOR'S REPORT
TO THE SHAREHOLDERS OF DREAM INTERNATIONAL LIMITED
(incorporated in Hong Kong with limited liability)

We have audited the consolidated financial statements of Dream International Limited (the "Company") and its subsidiaries (together, the "Group") set out on pages 33 to 102, which comprise the consolidated and company balance sheets as at 31 December 2007, and the consolidated income statement, the consolidated statement of changes in equity and the 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 of the Company are responsible for the preparation and the true and fair presentation of these consolidated financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants, and the 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 consolidated financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with section 141 of the Hong Kong Companies Ordinance and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

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 judgement, 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.

Independent Auditor's Report

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2007 and of the Group's loss 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 Hong Kong Companies Ordinance.

PricewaterhouseCoopers

Certified Public Accountants

Hong Kong, 18 April 2008

Consolidated Balance Sheet

As at 31 December 2007

| | Notes | 2007 HK\$'000 | 2006 HK\$'000 |
|--|-------|------------------|------------------|
| ASSETS | | | |
| Non-current assets | | | |
| Leasehold land and land use rights | 6 | 15,153 | 16,168 |
| Property, plant and equipment | 7 | 182,022 | 199,878 |
| Intangible assets | 8 | 16,623 | 17,268 |
| Investments in associates | 10 | 1,373 | 1,298 |
| Deferred income tax assets | 20 | 3,826 | 3,180 |
| Other financial assets | 12 | 76,284 | 71,054 |
| | | <u>295,281</u> | <u>308,846</u> |
| Current assets | | | |
| Inventories | 13 | 156,637 | 166,123 |
| Trade and other receivables | 14 | 168,393 | 204,572 |
| Tax recoverable | | 591 | – |
| Cash and cash equivalents | 15 | 107,222 | 82,798 |
| | | <u>432,843</u> | <u>453,493</u> |
| Total assets | | <u>728,124</u> | <u>762,339</u> |
| EQUITY | | | |
| Capital and reserves attributable to the Company's equity holders | | | |
| Share capital | 16 | 52,019 | 52,019 |
| Reserves | 17 | 379,972 | 369,618 |
| | | 431,991 | 421,637 |
| Minority interests | | <u>18,220</u> | <u>20,474</u> |
| Total equity | | <u>450,211</u> | <u>442,111</u> |

Consolidated Balance Sheet (Continued)

As at 31 December 2007

| | Notes | 2007 HK\$'000 | 2006 HK\$'000 |
|--|-------|------------------|------------------|
| LIABILITIES | | | |
| Non-current liabilities | | | |
| Borrowings | 19 | 780 | 8,684 |
| Deferred income tax liabilities | 20 | 248 | 322 |
| Retirement benefit obligations | 21 | 10,689 | 10,703 |
| | | <u>11,717</u> | <u>19,709</u> |
| Current liabilities | | | |
| Trade and other payables | 18 | 149,845 | 157,515 |
| Current income tax liabilities | | 2,467 | 12,214 |
| Borrowings | 19 | 113,884 | 130,790 |
| | | <u>266,196</u> | <u>300,519</u> |
| Total liabilities | | <u>277,913</u> | <u>320,228</u> |
| Total equity and liabilities | | <u>728,124</u> | <u>762,339</u> |
| Net current assets | | <u>166,647</u> | <u>152,974</u> |
| Total assets less current liabilities | | <u>461,928</u> | <u>461,820</u> |

Young M. LEE
Director

Hyun Ho KIM
Director

Balance Sheet

As at 31 December 2007

| | Notes | 2007 HK\$'000 | 2006 HK\$'000 |
|--|-------|------------------|------------------|
| ASSETS | | | |
| Non-current assets | | | |
| Property, plant and equipment | 7 | 12,974 | 18,211 |
| Intangible assets | 8 | 315 | 308 |
| Investments in subsidiaries | 9 | 226,734 | 236,775 |
| Investments in associates | 10 | 1,248 | 1,248 |
| Other financial assets | 12 | 75,373 | 69,231 |
| | | <u>316,644</u> | <u>325,773</u> |
| Current assets | | | |
| Inventories | 13 | 39,648 | 51,129 |
| Trade and other receivables | 14 | 143,202 | 145,559 |
| Tax recoverable | | 524 | – |
| Cash and cash equivalents | 15 | 34,061 | 11,769 |
| | | <u>217,435</u> | <u>208,457</u> |
| Total assets | | <u>534,079</u> | <u>534,230</u> |
| EQUITY | | | |
| Capital and reserves attributable to the Company's equity holders | | | |
| Share capital | 16 | 52,019 | 52,019 |
| Reserves | 17 | 316,503 | 291,041 |
| Total equity | | <u>368,522</u> | <u>343,060</u> |
| LIABILITIES | | | |
| Non-current liabilities | | | |
| Borrowings | 19 | – | 4,800 |
| Deferred income tax liabilities | 20 | 248 | 322 |
| Retirement benefit obligations | 21 | 9,073 | 6,537 |
| | | <u>9,321</u> | <u>11,659</u> |
| Current liabilities | | | |
| Trade and other payables | 18 | 96,832 | 127,309 |
| Current income tax liabilities | | – | 7,877 |
| Borrowings | 19 | 59,404 | 44,325 |
| | | <u>156,236</u> | <u>179,511</u> |
| Total liabilities | | <u>165,557</u> | <u>191,170</u> |
| Total equity and liabilities | | <u>534,079</u> | <u>534,230</u> |
| Net current assets | | <u>61,199</u> | <u>28,946</u> |
| Total assets less current liabilities | | <u>377,843</u> | <u>354,719</u> |

Young M. LEE

Director

Hyun Ho KIM

Director

The notes on pages 39 to 102 are an integral part of this financial statement.

Consolidated Income Statement

For the year ended 31 December 2007

| | Note | 2007 HK\$'000 | 2006 HK\$'000 |
|---|------|------------------|------------------|
| Turnover | 5 | 946,328 | 1,084,357 |
| Cost of sales | 24 | (798,360) | (924,319) |
| Gross profit | | 147,968 | 160,038 |
| Other income | 23 | 6,357 | 4,025 |
| Selling and distribution expenses | 24 | (37,444) | (38,310) |
| Administrative expenses | 24 | (134,459) | (137,218) |
| Goodwill impairment losses | 8 | – | (100,194) |
| Other gains/(losses) – net | 22 | 2,395 | (6,073) |
| Operating loss | | (15,183) | (117,732) |
| Finance costs – net | 26 | (5,016) | (4,842) |
| Share of loss of associates | | (16) | (237) |
| Loss before income tax | | (20,215) | (122,811) |
| Income tax credit/(expense) | 27 | 11,986 | (8,673) |
| Loss for the year | | (8,229) | (131,484) |
| Attributable to: | | | |
| Equity holders of the Company | | (4,831) | (129,671) |
| Minority interests | | (3,398) | (1,813) |
| | | (8,229) | (131,484) |
| Loss per share (expressed in HK\$ per share) | | | |
| – basic and diluted | 29 | (0.007) | (0.194) |
| Dividend | 30 | – | – |

Consolidated Statement Of Changes In Equity

For the year ended 31 December 2007

| | Attributable to equity holders of the Company | | | | Total equity HK\$'000 |
|--|--|----------------------|-------------------|-----------------------------------|-----------------------------|
| | Share capital HK\$'000 | Reserves HK\$'000 | Total HK\$'000 | Minority interests HK\$'000 | |
| | | | | | |
| Balance at 1 January 2006 | 52,019 | 490,930 | 542,949 | 14,998 | 557,947 |
| Currency translation differences | – | 7,499 | 7,499 | 269 | 7,768 |
| Loss for the year | – | (129,671) | (129,671) | (1,813) | (131,484) |
| Equity settled share-based transactions | – | 860 | 860 | – | 860 |
| Capital contributions received from minority shareholders | – | – | – | 7,020 | 7,020 |
| Balance at 31 December 2006 | 52,019 | 369,618 | 421,637 | 20,474 | 442,111 |
| Balance at 1 January 2007 | 52,019 | 369,618 | 421,637 | 20,474 | 442,111 |
| Currency translation differences | – | 15,185 | 15,185 | 1,144 | 16,329 |
| Loss for the year | – | (4,831) | (4,831) | (3,398) | (8,229) |
| Balance at 31 December 2007 | 52,019 | 379,972 | 431,991 | 18,220 | 450,211 |

Consolidated Cash Flow Statement

For the year ended 31 December 2007

| | Notes | 2007 HK\$'000 | 2006 HK\$'000 |
|--|-------|------------------|------------------|
| Cash flows from operating activities | | | |
| Cash generated from operations | 31 | 42,254 | 39,210 |
| Net income tax refunded/(paid) | | 1,127 | (583) |
| Interest received from other financial assets | | 1,659 | 2,561 |
| Net cash generated from operating activities | | 45,040 | 41,188 |
| Cash flows from investing activities | | | |
| Purchase of property, plant and equipment | 7 | (14,528) | (75,366) |
| Proceeds from sale of property, plant and equipment | 31 | 12,654 | 3,315 |
| Proceeds from sale of club membership | | 1,260 | – |
| Purchase of club memberships and patent | 8 | (753) | (5,384) |
| Loan granted to a fellow subsidiary | | (8,300) | – |
| Prepaid operating lease payments for leasehold land and land use right | 6 | – | (4,841) |
| Bank interest received | | 3,116 | 2,842 |
| Net cash used in investing activities | | (6,551) | (79,434) |
| Cash flows from financing activities | | | |
| Interest paid | | (8,132) | (7,684) |
| Proceeds from borrowings | | 100,162 | 91,594 |
| Repayments of borrowings | | (101,043) | (76,312) |
| Capital contributions from minority shareholders | | – | 7,020 |
| Net cash (used in)/generated from financing activities | | (9,013) | 14,618 |
| Net increase/(decrease) in cash, cash equivalents and bank overdrafts | | | |
| Cash, cash equivalents and bank overdrafts at beginning of year | | 74,836 | 95,973 |
| Effect of foreign exchange rate change | | 2,910 | 2,491 |
| Cash, cash equivalents and bank overdrafts at end of year | 15 | 107,222 | 74,836 |

The notes on pages 39 to 102 are an integral part of these consolidated financial statements.

Notes to the Financial Statements

For the year ended 31 December 2007

1 General information

The principal activities of Dream International Limited (the “Company”) and its subsidiaries (together, the “Group”) are the design, development, manufacturing and sale of plush stuffed and steel and plastic toys.

The Company is a limited liability company incorporated in Hong Kong. The address of its registered office is 8/F, Tower 5, China Hong Kong City, 33 Canton Road, Tsimshatsui, Kowloon, Hong Kong.

The Company has its primary listing on the Main Board of The Stock Exchange of Hong Kong Limited (the “SEHK”).

These consolidated financial statements are presented in thousands of units of Hong Kong dollar (HK\$’000), unless otherwise stated. These consolidated financial statements have been approved for issue by the Board of Directors on 18 April 2008.

2 Summary of significant accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements 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 financial statements of Dream International Limited have been prepared in accordance with Hong Kong Financial Reporting Standards (“HKFRS”). The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale financial assets, financial assets and financial liabilities (including derivative financial instruments) at fair value through income statement, which are carried at fair value.

The preparation of financial statements in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group’s accounting policies.

Notes to the Financial Statements

For the year ended 31 December 2007

2 Summary of significant accounting policies (Continued)

2.1 Basis of preparation (Continued)

(a) New standards, amendments to standards and interpretations effective in 2007

The following new standards, amendments to standards and interpretations are effective for the year ended 31 December 2007:

| | |
|--------------------|---|
| HKAS 1 (Amendment) | Presentation of Financial Statements – Capital Disclosures |
| HKFRS 7 | Financial Instruments: Disclosures |
| HK(IFRIC)-Int 7 | Applying the Restatement Approach under HKAS 29 Financial Reporting in Hyperinflationary Economies |
| HK(IFRIC)-Int 8 | Scope of HKFRS 2 |
| HK(IFRIC)-Int 9 | Reassessment of Embedded Derivatives |
| HK(IFRIC)-Int 10 | Interim Financial Reporting and Impairment |

The adoption of the above standards, amendments to standards and interpretations did not have significant impact to the Group's accounting policy except that there were additional disclosures required by HKAS 1 (Amendment) and HKFRS 7.

(b) New/revised standards and interpretations that are not yet effective and have not been early adopted by the Group.

The following new/revised standards and interpretations are not yet effective and have not been early adopted by the Group:

| | |
|---------------------|---|
| HKAS 1 (Revised) | Presentation of Financial Statements |
| HKAS 23 (Revised) | Borrowing Costs |
| HKAS 27 (Revised) | Consolidated and Separate Financial Statements |
| HKFRS 2 (Amendment) | Share-based Payment |
| HKFRS 3 (Revised) | Business Combination |
| HKFRS 8 | Operating Segments |
| HK(IFRIC)-Int 11 | HKFRS 2 – Group and Treasury Share Transactions |
| HK(IFRIC)-Int 12 | Service Concession Arrangements |
| HK(IFRIC)-Int 13 | Customer Loyalty Programmes |
| HK(IFRIC)-Int 14 | HKAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction |

Notes to the Financial Statements

For the year ended 31 December 2007

2 Summary of significant accounting policies (Continued)

2.2 Consolidation

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

(a) Subsidiaries

Subsidiaries are all entities (including special purpose 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 income statement.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Company's balance sheet the investments in subsidiaries are stated at cost less provision for impairment losses (Note 2.8). 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 income statement. 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.

Notes to the Financial Statements

For the year ended 31 December 2007

2 Summary of significant accounting policies (Continued)

2.2 Consolidation (Continued)

(c) Associates

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for using the equity method of accounting and are initially recognised at cost.

The Group's share of its associates' post-acquisition profits or losses is recognised in the income statement, 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 investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, 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.

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

In the Company's balance sheet the investments in associates are stated at cost less provision for impairment losses (Note 2.8). The results of associated companies are accounted for by the Company on the basis of dividend 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 are subject to risks and returns that are different from those of segments operating in other economic environments.

2.4 Foreign currency translation

(a) Functional and presentation currency

Items included in the financial statements 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 financial statements are presented in Hong Kong dollar, which is different from the Company's functional currency of United States dollar ("US dollar"). The Company has used Hong Kong dollar as its presentation currency in view of the fact that the Company's shares are listed on the SEHK.

Notes to the Financial Statements

For the year ended 31 December 2007

2 Summary of significant accounting policies (Continued)

2.4 Foreign currency translation (Continued)

(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 income statement.

Changes in the fair value of monetary securities denominated in foreign currency classified as available for sale are analysed between translation differences resulting from changes in the amortised cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in the amortised cost are recognised in income statement, and other changes in the carrying amount are recognised in equity.

Translation differences on non-monetary financial assets and liabilities are reported as part of the fair value gain or loss. Translation difference on non-monetary financial assets and liabilities such as equities held at fair value through profit or loss are recognised in income statement as part of the fair value gain or loss. Translation differences on non-monetary financial assets such as equities classified as available for sale are included in the available-for-sale reserve in equity.

(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:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- income and expenses for each income statement 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
- all resulting exchange differences are recognised as a separate component of equity.

Notes to the Financial Statements

For the year ended 31 December 2007

2 Summary of significant accounting policies (Continued)

2.6 Property, plant and equipment (Continued)

Construction in progress is stated at cost capitalised, which includes construction costs and other direct costs, less any identified impairment loss. No depreciation is provided until the construction is completed and the assets are ready for intended use. Cost of completed construction work is transferred to the appropriate category of property, plant and equipment.

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

An 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 2.8).

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within other gains/(losses) – net, in the income statement.

2.7 Intangible assets

(a) Patents

Acquired patents are shown at historical cost. Patents have a finite useful life and are carried at cost less accumulated amortisation. Amortisation is calculated using the straight-line method to allocate the cost of patents over their estimated useful lives (5 years).

(b) Club memberships

Club memberships with indefinite useful lives are stated in the balance sheet at cost less accumulated impairment losses, and are tested annually for impairment (Note 2.8).

2.8 Impairment of investments in subsidiaries, associates and non-financial assets

Assets that have an indefinite useful life or have not yet available for use are not subject to amortisation and are tested annually for impairment. 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.

Notes to the Financial Statements

For the year ended 31 December 2007

2 Summary of significant accounting policies (Continued)

2.9 Financial assets

The Group classifies its financial assets in the following categories: loans and receivable and available-for-sale. The classification depends on the purposes for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

(a) **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 which are classified as non-current assets. Loans and receivables are classified as “trade and other receivables” and “cash and cash equivalents” in the balance sheet (Note 2.12 and Note 2.13).

(b) **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.

All financial assets are initially recognised at fair value plus transaction costs. Financial assets 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 are subsequently carried at fair value. Loans and receivables are carried at amortised cost using the effective interest method.

When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognised in equity are included in the income statement as gains and losses from investment securities.

Interest on available-for-sale securities calculated using the effective interest method is recognised in the income statement as part of other income. Dividends on available-for-sale equity instruments are recognised in the income statement as part of other income when the Group’s right to receive payments is established.

The fair values of quoted investments are 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.

Notes to the Financial Statements

For the year ended 31 December 2007

2 Summary of significant accounting policies (Continued)

2.9 Financial assets (Continued)

(b) Available-for-sale financial assets (Continued)

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 security below its cost is considered as 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 profit or loss – is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement. Impairment testing of trade receivables is described in Note 2.12.

2.10 Derivatives financial instruments

The Group has no derivative financial instrument designated as a hedging instrument. Derivative financial instruments are initially recognised at fair value and are subsequently remeasured at their fair value. Changes in the fair value are recognised immediately in the income statement within other gains/(losses) – net.

2.11 Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the weighted average costing method. The cost of finished goods and work in progress 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.

2.12 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 the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the trade receivable is impaired. 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 original effective interest rate. The carrying amount of the assets is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement within selling and distribution expenses. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts previously written off are credited against selling and distribution expenses in the income statement.

Notes to the Financial Statements

For the year ended 31 December 2007

2 Summary of significant accounting policies (Continued)

2.13 Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the balance sheet.

2.14 Share capital

Ordinary shares are classified as equity.

2.15 Trade payables

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

2.16 Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

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.

2.17 Current and deferred income tax

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the Company and its subsidiaries and associates operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

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 financial statements. 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.

Notes to the Financial Statements

For the year ended 31 December 2007

2 Summary of significant accounting policies (Continued)

2.17 Current and deferred income tax (Continued)

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

2.18 Employee benefits

(a) Pension obligations

The Group participates in various pension schemes, including defined benefit and defined contribution plans.

A defined contribution plan is a pension plan under which a company pays fixed contributions into separately administered funds. A company has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all qualified employees the benefits relating to employee service in the current and prior periods. The contributions are recognised as employee benefit expense when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available.

A defined benefit plan is a pension plan that is not a defined contribution plan. Typically, defined benefit plans define an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation.

The liability recognised in the balance sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets, together with adjustments for unrecognised actuarial gains or losses and past service costs. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds or treasury bond that are denominated in the currency in which the benefits will be paid and that have terms to maturity approximating to the terms of the related pension liability.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions in excess of the greater of 10% of the value of plan assets or 10% of the defined benefit obligation are charged to or credited against the income statement over the employees' expected average remaining working lives.

Past-service costs are recognised immediately in the income statement, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past-service costs are amortised on a straight-line basis over the vesting period.

Notes to the Financial Statements

For the year ended 31 December 2007

2 Summary of significant accounting policies (Continued)

2.18 Employee benefits (Continued)

(b) Share-based compensation

The Group operates a number of equity-settled, share-based compensation plans. 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 vest. At each balance sheet date, the entity revises its estimates of the number of options that are expected to vest. At each balance sheet date, the entity revises its estimates of the number of options that are expected to vest. It recognises the impact of the revision of original estimates, if any, in the income statement, with a corresponding adjustment to equity.

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.

(c) Termination benefits

Termination benefits are payable when employment is terminated by the Group before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits when it is demonstrably committed to either: terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal; or providing termination benefits as a result of an offer made to encourage voluntary redundancy. Benefits falling due more than 12 months after balance sheet date are discounted to present value.

2.19 Provisions

Provisions are recognised when: the Group has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

Notes to the Financial Statements

For the year ended 31 December 2007

2 Summary of significant accounting policies (Continued)

2.20 Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services in the ordinary course of the Group's activities. Revenue is shown net of value-added tax, returns, rebates and discounts and after eliminating sales within the Group.

The Group recognises revenue when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity and specific criteria have been met for each of the Group's activities as described below. The amount of revenue is not considered to be reliably measurable until all contingencies relating to the sale have been resolved. The Group bases its estimates on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement.

(a) **Sale of goods**

Revenue from the sale of goods is recognised upon shipment when significant risks and rewards of ownership of the goods are transferred to the buyer and collectibility of related receivables is reasonably assured.

(b) **Commission income**

Commission income on sales referred to manufacturers is recognised when the goods are delivered by the manufacturers to the ultimate customers.

(c) **Interest income**

Interest income is recognised on a time-proportion basis using the effective interest method.

2.21 Leases (as the lessee for operating leases)

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 to the income statement on a straight-line basis over the period of the lease.

2.22 Borrowing costs

Borrowing costs incurred for the construction of any qualifying asset are capitalised during the period of time that is required to complete and prepare the asset for its intended use. Other borrowing costs are expensed.

2.23 Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved by the Company's shareholders or directors, where appropriate.

Notes to the Financial Statements

For the year ended 31 December 2007

3 Financial risk management

3.1 Financial risk factors

The Group's activities expose it to a variety of financial risks: market risk (including foreign exchange risk, cash flow and fair value interest risk), credit risk and liquidity risk. The Group's overall risk management focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

(a) **Market risk**

(i) *Foreign exchange risk*

The Group mainly operates in the Mainland China and Hong Kong with most of the transactions settled in US dollar and Renminbi ("RMB"). The Group's assets and liabilities, and transactions arising from its operations that are exposed to foreign exchange risks are primarily with respect to US dollar. The Group has not used any forward contracts to hedge its exposure.

At 31 December 2007, if US dollar had strengthened/weakened by 10% against Hong Kong dollar with all other variables held constant, post-tax loss for the year would have been HK\$5,250,000 (2006: HK\$7,230,000) lower/higher.

(ii) *Cash flow and fair value interest rate risk*

The Group is subject to interest rate risk in relation to derivatives financial instrument, loan to a fellow subsidiary, borrowings and bank balances. Derivatives financial instrument, borrowings and bank balances carried at floating rates expose the Group to cash flow interest rate risk whereas those carried at fixed rates expose the Group to fair value interest rate risk. The Group has not entered into any interest rate swaps to hedge its exposure to interest rate risks.

If the market interest rates had been 100 basis points higher/lower at 31 December 2007, post-tax loss would have been approximately HK\$701,000 (2006: HK\$991,000) lower/higher.

(b) **Credit risk**

Credit risk is managed on a group basis. Credit risk arises from cash and cash equivalents, and deposits with banks and financial institutions, as well as credit exposures to customers, including outstanding receivables. For banks and financial institutions, deposits are only placed with reputable banks. For credit exposures to customers, Group management assesses the credit quality of the customer, taking into account its financial position, past experience and other factors.

As at 31 December 2006 and 2007, no customers were rated independently.

Notes to the Financial Statements

For the year ended 31 December 2007

3 Financial risk management (Continued)

3.1 Financial risk factors (Continued)

(c) Liquidity risk

Prudent liquidity risk management includes maintaining sufficient cash and the availability of funding from an adequate amount of committed credit facilities and the ability to close out market positions.

The Group maintains its liquidity mainly through funding generated from its daily operations.

Liquidity risk is the risk that funds will not be available to meet liabilities as they fall due, and it results from amount and maturity mismatches of assets and liabilities. Prudent liquidity risk management includes maintaining sufficient cash, the availability of funding from an adequate amount of committed credit facilities and the ability to close out market positions.

Banking facilities have been put in place for contingency purposes. As at 31 December 2007, the Group's total available banking facilities amounted to HK\$393,323,000 (2006: HK\$224,188,000).

The table below analyses the Group's financial liabilities that will be settled on a net basis into relevant maturity groupings based on the remaining period at the balance sheet to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

| | Less than 1 year HK\$'000 | Between 1 and 2 years HK\$'000 |
|--------------------------|---------------------------------|--------------------------------------|
| Group | | |
| At 31 December 2007 | | |
| Borrowings | 113,884 | 780 |
| Trade and other payables | 148,945 | – |
| At 31 December 2006 | | |
| Borrowings | 130,790 | 8,684 |
| Trade and other payables | 157,515 | – |
| Company | | |
| At 31 December 2007 | | |
| Borrowings | 59,404 | – |
| Trade and other payables | 96,832 | – |
| At 31 December 2006 | | |
| Borrowings | 44,325 | 4,800 |
| Trade and other payables | 127,309 | – |

Notes to the Financial Statements

For the year ended 31 December 2007

3 Financial risk management (Continued)

3.2 Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for equity holders and to reduce the cost of capital.

The Group monitors capital on the basis of the gearing ratio. This ratio is calculated as total borrowings divided by total equity.

The gearing ratios at 31 December 2007 and 2006 were as follows:

| | 2007 HK\$'000 | 2006 HK\$'000 |
|----------------------------|------------------|------------------|
| Total borrowings (Note 19) | 114,664 | 139,474 |
| Total equity | 450,211 | 442,111 |
| Gearing ratio | 25% | 32% |

3.3 Fair value estimation

The carrying value less impairment provision of other financial assets, trade receivables and payables are a reasonable approximation of their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

Notes to the Financial Statements

For the year ended 31 December 2007

4 Critical accounting estimates and judgements

Estimates and judgements 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) *Income taxes*

The Group is subject to income taxes in various jurisdictions. Significant judgement is required in determining the worldwide provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. 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.

(b) *Impairment of trade and other receivables*

Provision for impairment of trade and other receivables is determined based on the evaluation of collectability of trade and other receivables. A considerable amount of judgment is required in assessing the ultimate realisation of these receivables, including the current market condition.

(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 the current market condition and the historical experience of manufacturing and selling products of similar nature.

(d) *Fair value of other financial assets*

The fair value of other financial assets that are not traded in an active market is determined by using valuation techniques. The Group uses its judgement to select a variety of methods and make assumptions that are mainly based on market conditions existing at each balance sheet date. The Group uses discounted cash flow analysis for various available-for-sale financial assets that were not traded in active markets.

(e) *Defined benefit obligations*

The costs, assets and liabilities of defined benefit obligations are determined using actuarial valuation prepared by an independent firm of actuaries. Details of the key assumptions are disclosed in Note 21. Due to the long term nature of this plan, such estimates are subject to significant uncertainty. The assumptions and the resulting estimates are reviewed annually and, when appropriate, changes are made which affect the actuarial valuation and, hence, the amount of retirement benefit expense recognised in the income statement.

Notes to the Financial Statements

For the year ended 31 December 2007

5 Segment information

(a) Primary reporting format – business segments

The Group comprises two main business segments:

- plush stuffed toys
- steel and plastic toys

| | Plush stuffed toys | | Steel and plastic toys | | Unallocated | | Total | |
|-----------------------------|--------------------|----------------|------------------------|----------------|--------------|--------------|----------------|------------------|
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| Sales to external customers | 801,339 | 903,920 | 144,989 | 180,437 | – | – | 946,328 | 1,084,357 |
| Other income | 3,681 | 1,434 | 1,017 | 30 | 1,659 | 2,561 | 6,357 | 4,025 |
| Total | 805,020 | 905,354 | 146,006 | 180,467 | 1,659 | 2,561 | 952,685 | 1,088,382 |
| Segment result | (7,571) | (13,359) | (7,612) | (4,179) | – | – | (15,183) | (17,538) |
| Goodwill impairment losses | – | (99,532) | – | (662) | – | – | – | (100,194) |
| Operating loss | | | | | | | (15,183) | (117,732) |
| Finance costs – net | | | | | | | (5,016) | (4,842) |
| Share of loss of associates | | | | | | | (16) | (237) |
| Loss before income tax | | | | | | | (20,215) | (122,811) |
| Income tax credit/(expense) | | | | | | | 11,986 | (8,673) |
| Loss for the year | | | | | | | (8,229) | (131,484) |

Notes to the Financial Statements

For the year ended 31 December 2007

5 Segment information (Continued)

(a) Primary reporting format – business segments (Continued)

| | Plush stuffed toys | | Steel and plastic toys | | Total | |
|---|--------------------|------------------|------------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Segment assets | 497,640 | 548,417 | 148,410 | 138,390 | 646,050 | 686,807 |
| Investments in associates | 1,373 | 1,298 | – | – | 1,373 | 1,298 |
| Unallocated assets | | | | | 80,701 | 74,234 |
| Total assets | | | | | 728,124 | 762,339 |
| Segment liabilities | 105,222 | 126,440 | 55,312 | 41,778 | 160,534 | 168,218 |
| Unallocated liabilities | | | | | 117,379 | 152,010 |
| Total liabilities | | | | | 277,913 | 320,228 |
| Capital expenditure | 11,536 | 19,769 | 2,992 | 60,438 | 14,528 | 80,207 |
| Depreciation of property, plant and equipment | 23,398 | 21,943 | 6,707 | 4,127 | 30,105 | 26,070 |
| Amortisation of leasehold land and land use rights and patent | 337 | 217 | 779 | 756 | 1,116 | 973 |

Segment assets consist primarily of property, plant and equipment, intangible assets, inventories, trade and other receivables, and cash and cash equivalents. Unallocated assets comprise deferred income tax assets, other financial assets and tax recoverable.

Segment liabilities comprise operating liabilities. Unallocated liabilities comprises items such as borrowings, deferred income tax liabilities and current income tax liabilities.

Capital expenditure comprises additions to leasehold land and land use rights and property, plant and equipment.

Notes to the Financial Statements

For the year ended 31 December 2007

5 Segment information (Continued)

(b) Secondary reporting format – geographical segments

| | Turnover | | Segment assets | | Capital expenditure | |
|-------------------|------------------|------------------|------------------|------------------|---------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| North America | 419,357 | 534,694 | 1,743 | 2,016 | 65 | 137 |
| Japan | 283,074 | 271,226 | 4,182 | 4,297 | – | – |
| Europe | 170,576 | 187,552 | – | – | – | – |
| South Korea | 5,272 | 14,350 | 70,219 | 91,267 | 630 | 140 |
| PRC and Hong Kong | 65,363 | 67,200 | 507,258 | 538,328 | 11,996 | 70,738 |
| Vietnam | 185 | 539 | 62,648 | 50,899 | 1,837 | 9,192 |
| Others | 2,501 | 8,796 | – | – | – | – |
| | 946,328 | 1,084,357 | 646,050 | 686,807 | 14,528 | 80,207 |

The analysis of turnover by geographical segment is based on the destination of shipments of goods. No analysis of the contribution by geographical segment has been presented as the ratios of profit to turnover achieved for the above geographical segments are not substantially out of line with the Group's overall ratio of profit to turnover.

Notes to the Financial Statements

For the year ended 31 December 2007

6 Leasehold land and land use rights

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:

| | Group | |
|----------------------------------|----------|----------|
| | 2007 | 2006 |
| | HK\$'000 | HK\$'000 |
| Outside Hong Kong held on: | | |
| Leases of between 10 to 50 years | 15,153 | 16,168 |

Bank borrowings are secured on leasehold land and land use rights for the carrying amount of HK\$14,581,000 (2006: HK\$15,622,000) (Note 19).

| | Group | |
|--|----------|----------|
| | 2007 | 2006 |
| | HK\$'000 | HK\$'000 |
| Opening net book amount | 16,168 | 11,269 |
| Additions | – | 4,841 |
| Disposals | (1,278) | – |
| Amortisation of prepaid operating lease payments (Note 24) | (440) | (297) |
| Exchange differences | 703 | 355 |
| Closing net book amount | 15,153 | 16,168 |

Notes to the Financial Statements

For the year ended 31 December 2007

7 Property, plant and equipment

| | Group | | | | | | Total HK\$'000 |
|------------------------------------|---|---------------------------------------|------------------------------------|--|-------------------------------|--|-------------------|
| | Freehold land and buildings HK\$'000 | Leasehold improvements HK\$'000 | Plant and machinery HK\$'000 | Office equipment, furniture and fixtures HK\$'000 | Motor vehicles HK\$'000 | Construction in progress HK\$'000 | |
| At 1 January 2006 | | | | | | | |
| Cost | 66,012 | 22,411 | 124,030 | 25,464 | 12,906 | 8,501 | 259,324 |
| Accumulated depreciation | (9,819) | (17,506) | (59,729) | (16,896) | (8,284) | - | (112,234) |
| Net book amount | 56,193 | 4,905 | 64,301 | 8,568 | 4,622 | 8,501 | 147,090 |
| Year ended 31 December 2006 | | | | | | | |
| Opening net book amount | 56,193 | 4,905 | 64,301 | 8,568 | 4,622 | 8,501 | 147,090 |
| Exchange differences | 2,226 | 82 | 2,332 | 488 | (17) | 711 | 5,822 |
| Additions | 11,104 | 1,351 | 33,324 | 2,278 | 2,685 | 24,624 | 75,366 |
| Disposals | (1,983) | - | (18) | (51) | (278) | - | (2,330) |
| Depreciation | (2,947) | (1,913) | (16,557) | (3,074) | (1,579) | - | (26,070) |
| Transfer | 26,221 | - | 5,855 | 1,100 | - | (33,176) | - |
| Closing net book amount | 90,814 | 4,425 | 89,237 | 9,309 | 5,433 | 660 | 199,878 |
| At 31 December 2006 | | | | | | | |
| Cost | 103,985 | 23,960 | 166,756 | 28,954 | 12,576 | 660 | 336,891 |
| Accumulated depreciation | (13,171) | (19,535) | (77,519) | (19,645) | (7,143) | - | (137,013) |
| Net book amount | 90,814 | 4,425 | 89,237 | 9,309 | 5,433 | 660 | 199,878 |

Notes to the Financial Statements

For the year ended 31 December 2007

7 Property, plant and equipment (Continued)

| | Group | | | | | | Total |
|------------------------------------|-----------------------------------|---------------------------|------------------------|--|-------------------|--------------------------------|-----------|
| | Freehold land and buildings | Leasehold improvements | Plant and machinery | Office equipment, furniture and fixtures | Motor vehicles | Construction in progress | |
| | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| Year ended 31 December 2007 | | | | | | | |
| Opening net book amount | 90,814 | 4,425 | 89,237 | 9,309 | 5,433 | 660 | 199,878 |
| Exchange differences | 4,683 | 201 | 4,346 | 391 | 246 | 39 | 9,906 |
| Additions | 1,220 | 1,516 | 7,113 | 1,051 | 2,274 | 1,354 | 14,528 |
| Disposals | (5,365) | (131) | (4,749) | (225) | (1,715) | – | (12,185) |
| Depreciation | (4,914) | (2,130) | (17,728) | (3,285) | (2,048) | – | (30,105) |
| Transfer | – | 1,552 | – | – | – | (1,552) | – |
| Closing net book amount | 86,438 | 5,433 | 78,219 | 7,241 | 4,190 | 501 | 182,022 |
| At 31 December 2007 | | | | | | | |
| Cost | 105,327 | 16,926 | 164,899 | 28,111 | 9,420 | 501 | 325,184 |
| Accumulated depreciation | (18,889) | (11,493) | (86,680) | (20,870) | (5,230) | – | (143,162) |
| Net book amount | 86,438 | 5,433 | 78,219 | 7,241 | 4,190 | 501 | 182,022 |

Bank borrowings are secured on buildings and plant and machinery for the carrying amount of HK\$83,345,000 (2006: HK\$93,232,000) (Note 19).

Notes to the Financial Statements

For the year ended 31 December 2007

7 Property, plant and equipment (Continued)

| | Company | | | | | Total HK\$'000 |
|------------------------------------|---|---------------------------------------|------------------------------------|--|-------------------------------|-------------------|
| | Freehold land and buildings HK\$'000 | Leasehold improvements HK\$'000 | Plant and machinery HK\$'000 | Office equipment, furniture and fixtures HK\$'000 | Motor vehicles HK\$'000 | |
| At 1 January 2006 | | | | | | |
| Cost | 4,603 | 17,019 | 34,457 | 12,555 | 3,612 | 72,246 |
| Accumulated depreciation | (191) | (13,897) | (20,556) | (10,214) | (3,247) | (48,105) |
| Net book value | <u>4,412</u> | <u>3,122</u> | <u>13,901</u> | <u>2,341</u> | <u>365</u> | <u>24,141</u> |
| Year ended 31 December 2006 | | | | | | |
| Opening net book value | 4,412 | 3,122 | 13,901 | 2,341 | 365 | 24,141 |
| Additions | - | 74 | - | 98 | 240 | 412 |
| Disposals | - | - | (16) | - | - | (16) |
| Depreciation | (115) | (1,129) | (4,016) | (832) | (234) | (6,326) |
| Closing net book value | <u>4,297</u> | <u>2,067</u> | <u>9,869</u> | <u>1,607</u> | <u>371</u> | <u>18,211</u> |
| At 31 December 2006 | | | | | | |
| Cost | 4,603 | 17,093 | 34,407 | 12,615 | 1,540 | 70,258 |
| Accumulated depreciation | (306) | (15,026) | (24,538) | (11,008) | (1,169) | (52,047) |
| Net book value | <u>4,297</u> | <u>2,067</u> | <u>9,869</u> | <u>1,607</u> | <u>371</u> | <u>18,211</u> |

Notes to the Financial Statements

For the year ended 31 December 2007

7 Property, plant and equipment (Continued)

| | Company | | | | | Total | | | |
|------------------------------------|-----------------------------------|---------------------------|------------------------|--|-------------------|-----------------|----------|----------|----------|
| | Freehold land and buildings | Leasehold improvements | Plant and machinery | Office equipment, furniture and fixtures | Motor vehicles | | | | |
| | | | | HK\$'000 | | | HK\$'000 | HK\$'000 | HK\$'000 |
| | | | | HK\$'000 | | | HK\$'000 | HK\$'000 | HK\$'000 |
| Year ended 31 December 2007 | | | | | | | | | |
| Opening net book value | 4,297 | 2,067 | 9,869 | 1,607 | 371 | 18,211 | | | |
| Additions | – | 1,025 | 190 | 183 | – | 1,398 | | | |
| Disposals | – | (175) | (284) | – | – | (459) | | | |
| Depreciation | (115) | (1,139) | (3,976) | (744) | (202) | (6,176) | | | |
| Closing net book value | <u>4,182</u> | <u>1,778</u> | <u>5,799</u> | <u>1,046</u> | <u>169</u> | <u>12,974</u> | | | |
| At 31 December 2007 | | | | | | | | | |
| Cost | 4,603 | 8,088 | 29,787 | 11,341 | 1,407 | 55,226 | | | |
| Accumulated depreciation | <u>(421)</u> | <u>(6,310)</u> | <u>(23,988)</u> | <u>(10,295)</u> | <u>(1,238)</u> | <u>(42,252)</u> | | | |
| Net book value | <u>4,182</u> | <u>1,778</u> | <u>5,799</u> | <u>1,046</u> | <u>169</u> | <u>12,974</u> | | | |

The freehold land is located outside Hong Kong.

Notes to the Financial Statements

For the year ended 31 December 2007

8 Intangible assets

| | Group | | | Total HK\$'000 |
|---|----------------------|---------------------------------|--------------------|-------------------|
| | Goodwill HK\$'000 | Club memberships HK\$'000 | Patent HK\$'000 | |
| At 1 January 2006 | | | | |
| Cost | 109,469 | 12,505 | – | 121,974 |
| Accumulated amortisation and impairment | (9,315) | – | – | (9,315) |
| Net book amount | <u>100,154</u> | <u>12,505</u> | <u>–</u> | <u>112,659</u> |
| Year ended 31 December 2006 | | | | |
| Opening net book amount | 100,154 | 12,505 | – | 112,659 |
| Exchange differences | – | 486 | – | 486 |
| Additions | 40 | 2,002 | 3,382 | 5,424 |
| Disposals | – | (431) | – | (431) |
| Impairment charge | (100,194) | – | – | (100,194) |
| Amortisation charge | – | – | (676) | (676) |
| Closing net book amount | <u>–</u> | <u>14,562</u> | <u>2,706</u> | <u>17,268</u> |
| At 31 December 2006 | | | | |
| Cost | – | 14,562 | 3,382 | 17,944 |
| Accumulated amortisation and impairment | – | – | (676) | (676) |
| Net book amount | <u>–</u> | <u>14,562</u> | <u>2,706</u> | <u>17,268</u> |
| Year ended 31 December 2007 | | | | |
| Opening net book amount | – | 14,562 | 2,706 | 17,268 |
| Exchange differences | – | 580 | – | 580 |
| Additions | – | 753 | – | 753 |
| Disposals | – | (1,292) | – | (1,292) |
| Impairment charge | – | (10) | – | (10) |
| Amortisation charge | – | – | (676) | (676) |
| Closing net book amount | <u>–</u> | <u>14,593</u> | <u>2,030</u> | <u>16,623</u> |
| At 31 December 2007 | | | | |
| Cost | – | 16,189 | 3,382 | 19,571 |
| Accumulated amortisation and impairment | – | (1,596) | (1,352) | (2,948) |
| Net book amount | <u>–</u> | <u>14,593</u> | <u>2,030</u> | <u>16,623</u> |

Notes to the Financial Statements

For the year ended 31 December 2007

8 Intangible assets (Continued)

| | Company | |
|--------------------------|----------|----------|
| | 2007 | 2006 |
| | HK\$'000 | HK\$'000 |
| Club memberships | | |
| At 1 January | | |
| Cost | 308 | – |
| Accumulated amortisation | – | – |
| Net book amount | 308 | – |
| Year ended 31 December | | |
| Opening net book amount | 308 | – |
| Additions | – | 308 |
| Exchange differences | 7 | – |
| Closing net book amount | 315 | 308 |
| At 31 December | | |
| Cost | 315 | 308 |
| Accumulated amortisation | – | – |
| Net book amount | 315 | 308 |

Notes to the Financial Statements

For the year ended 31 December 2007

9 Investments in subsidiaries

| | Company | |
|-------------------------------------|----------|----------|
| | 2007 | 2006 |
| | HK\$'000 | HK\$'000 |
| Unlisted shares, at cost | 198,766 | 192,914 |
| Less: provision for impairment loss | (57,956) | (10,030) |
| | 140,810 | 182,884 |
| Loans to subsidiaries | 175,924 | 143,891 |
| Less: provision for impairment loss | (90,000) | (90,000) |
| | 85,924 | 53,891 |
| | 226,734 | 236,775 |

The maximum exposure to credit risk at the reporting date is the fair value of the loans to subsidiaries mentioned above.

Notes to the Financial Statements

For the year ended 31 December 2007

9 Investments in subsidiaries (Continued)

Loans to subsidiaries are unsecured, interest-free and have no fixed repayable terms except for a term loan to a subsidiary of HK\$24,186,000 (2006: nil) which is unsecured, interest-bearing at LIBOR plus 0.5% per annum and will be fully repaid on 25 September 2008.

The following is a list of the principal subsidiaries at 31 December 2007:

| Company name | Country/place of incorporation/ establishment and operation | Principal activities | Particulars of issued share capital/ registered capital | Percentage of equity shares held | |
|---|---|--|---|----------------------------------|--------------|
| | | | | by the Company | by the Group |
| *Dream International USA, Inc. | United States of America | Trading of plush stuffed toys | US\$1,000,000 | 100% | 100% |
| J.Y. Toys Co., Limited | Hong Kong | Trading and Manufacture of steel and plastic toys | US\$1,500,000 | 100% | 100% |
| J.Y. International Company Limited | Hong Kong | Trading of plush stuffed toys and investment holding | US\$500,000 | 100% | 100% |
| * #Jung Yoon Toys (Shanghai) Co., Limited | PRC | Manufacture of plush stuffed toys | US\$420,000 | 100% | 100% |
| * #C & H Toys (Suzhou) Co., Ltd. | PRC | Manufacture of plush fabrics and plush stuffed toys | US\$9,200,000 | 100% | 100% |
| Dream Inko Co., Ltd | South Korea | Design, development and trading of plush stuffed toys | KRW100,000,000 | – | 100% |
| *Dream Vina Co., Ltd | Vietnam | Manufacture of plush stuffed toys | US\$4,300,000 | 100% | 100% |
| *Dream Vina II Co., Ltd | Vietnam | Manufacture of plush stuffed toys | US\$277,835 | – | 100% |
| *Dream Vina Textile., Ltd | Vietnam | Manufacture of fabrics and dyeing | US\$450,000 | – | 100% |
| * #C & H Toys (Shuyang) Co., Ltd | PRC | Manufacture of plush stuffed toys | US\$1,200,000 | 100% | 100% |
| C & H HK Corp., Ltd | Hong Kong | Trading of steel and plastic toys and investment holding | US\$8,500,000 | 66.47% | 66.47% |
| * #J.Y. Plasteel (Suzhou) Co., Ltd | PRC | Manufacture of bicycles and steel and plastic toys | US\$7,500,000 | – | 66.47% |
| * #Guangxi Beiliu Zhengrun Toys Co., Ltd | PRC | Manufacture of plush stuffed toys | HK\$1,670,000 | 100% | 100% |
| * #C & H Toys (Mingguang) Co., Ltd | PRC | Manufacture of plush stuffed toys | US\$1,000,000 | 100% | 100% |
| * #C & H Toys (Chaohu) Co., Ltd | PRC | Manufacture of plush stuffed toys | US\$2,000,000 | – | 100% |

* The statutory financial statements of these subsidiaries were audited by other auditors in accordance with the relevant accounting principles and financial regulations applicable to these subsidiaries in respective regions.

These are wholly-owned foreign investment enterprises registered under the laws of the PRC.

Notes to the Financial Statements

For the year ended 31 December 2007

10 Investments in associates

| | Group | | Company | |
|--------------------------|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Unlisted shares, at cost | – | – | 1,248 | 1,248 |
| Share of net assets | 1,373 | 1,298 | – | – |
| | 1,373 | 1,298 | 1,248 | 1,248 |

The Group's interests in its principal associates, all of which are unlisted, were as follows:

| | Assets HK\$'000 | Liabilities HK\$'000 | Equity HK\$'000 | Revenues HK\$'000 | Profit/(loss) HK\$'000 |
|----------------------------|--------------------|-------------------------|--------------------|----------------------|---------------------------|
| 2007 | | | | | |
| 100 per cent | 31,625 | (24,759) | 6,866 | 49,077 | (79) |
| Group's effective interest | 6,325 | (4,952) | 1,373 | 9,815 | (16) |
| 2006 | | | | | |
| 100 per cent | 17,215 | (10,723) | 6,492 | 40,503 | (1,185) |
| Group's effective interest | 3,443 | (2,145) | 1,298 | 8,101 | (237) |

Details of the associates are as follows:

| Company name | Country/place of incorporation/ establishment | Principal activities | Particulars of issued and paid up capital/ registered capital | Percentage of interest in ownership held | |
|------------------------------------|---|--------------------------------------|--|---|-----------------|
| | | | | by the Company | by the Group |
| Kedington Enterprises Inc. | British Virgin Islands | Investment holding | US\$ 800,000 | 20% | 20% |
| Yuan Lin Toys (Suzhou) Co., Ltd | PRC | Manufacture of plush stuffed toys | US\$1,000,000 | – | 20% |

Notes to the Financial Statements

For the year ended 31 December 2007

11 Financial instruments by category

| | Group | | | Total |
|---|--------------------------|---|---|----------------|
| | Loans and receivables | Derivatives financial instruments | Available- for-sale financial assets | |
| | HK\$'000 | HK\$'000 | HK\$'000 | |
| Assets as per consolidated balance sheet | | | | |
| 31 December 2007 | | | | |
| Other financial assets (Note 12) | – | 75,373 | 911 | 76,284 |
| Trade and other receivables (Note 14) | 168,393 | – | – | 168,393 |
| Cash and cash equivalents (Note 15) | 107,222 | – | – | 107,222 |
| Total | 275,615 | 75,373 | 911 | 351,899 |
| 31 December 2006 | | | | |
| Other financial assets (Note 12) | – | 69,231 | 1,823 | 71,054 |
| Trade and other receivables (Note 14) | 204,572 | – | – | 204,572 |
| Cash and cash equivalents (Note 15) | 82,798 | – | – | 82,798 |
| Total | 287,370 | 69,231 | 1,823 | 358,424 |

Notes to the Financial Statements

For the year ended 31 December 2007

11 Financial instruments by category (Continued)

| | Financial liabilities | | |
|--|------------------------------|--|--------------|
| | HK\$'000 | | |
| Liabilities as per consolidated balance sheet | | | |
| 31 December 2007 | | | |
| Trade and other payables (Note 18) | | | 148,945 |
| Borrowings (Note 19) | | | 114,664 |
| Total | | | 263,609 |
| 31 December 2006 | | | |
| Trade and other payables (Note 18) | | | 157,515 |
| Borrowings (Note 19) | | | 139,474 |
| Total | | | 296,989 |
| | Company | | |
| | Loans and receivables | Derivatives financial instruments | Total |
| | HK\$'000 | HK\$'000 | HK\$'000 |
| Assets as per balance sheet | | | |
| 31 December 2007 | | | |
| Other financial assets (Note 12) | – | 75,373 | 75,373 |
| Trade and other receivables (Note 14) | 143,202 | – | 143,202 |
| Cash and cash equivalents (Note 15) | 34,061 | – | 34,061 |
| Total | 177,263 | 75,373 | 252,636 |
| 31 December 2006 | | | |
| Other financial assets (Note 12) | – | 69,231 | 69,231 |
| Trade and other receivables (Note 14) | 145,559 | – | 145,559 |
| Cash and cash equivalents (Note 15) | 11,769 | – | 11,769 |
| Total | 157,328 | 69,231 | 226,559 |

Notes to the Financial Statements

For the year ended 31 December 2007

11 Financial instruments by category (Continued)

| | Financial liabilities |
|---|------------------------------|
| | HK\$'000 |
| Liabilities as per balance sheet | |
| 31 December 2007 | |
| Trade and other payables (Note 18) | 96,832 |
| Borrowings (Note 19) | 59,404 |
| Total | 156,236 |
| 31 December 2006 | |
| Trade and other payables (Note 18) | 127,309 |
| Borrowings (Note 19) | 49,125 |
| Total | 176,434 |

12 Other financial assets

| | Group | | Company | |
|---|--------------|----------|----------------|----------|
| | 2007 | 2006 | 2007 | 2006 |
| | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| Long-term structured deposit (Note (i)) | 75,373 | 69,231 | 75,373 | 69,231 |
| Unlisted equity securities (Note (ii)) | 911 | 1,823 | – | – |
| | 76,284 | 71,054 | 75,373 | 69,231 |

Note (i) The Group entered into the contract with a bank in 2005. The contract will mature in 2017 and the principal amount is US\$12,000,000 (equivalent to HK\$93,300,000). Interest payable quarterly in the first year at 6.5% per annum and in subsequent years at rates based on the spread between the 30 year and 10 year United States dollar swap rates. The bank may elect to early terminate the contract on any interest payment date before the maturity date by repaying the full principal amount plus accrued interest up to the termination date.

Notes to the Financial Statements

For the year ended 31 December 2007

12 Other financial assets (Continued)

Note (i) (Continued)

The long-term structured deposit is a hybrid instrument that includes a non-derivatives host contract and an embedded derivative. Upon inception this financial instrument was designated as derivative financial instrument with changes in fair value recognised in the income statement.

As at 31 December 2007, the effective interest rate of the long-term structured deposit is 4.2% (2006: 1.3%).

Note (ii) These unlisted equity securities are categorised as available-for-sale financial assets. The fair value of the unlisted equity investments cannot be measured reliably because they are not traded in the open market and there were no transactions for the investments during the year. The unlisted investments are stated at cost less accumulated impairment losses. An impairment loss of HK\$912,000 was recognised during the year (2006: nil).

All other financial assets are denominated in US dollar.

The maximum exposure to credit risk of other financial assets at the reporting date is their carrying values.

13 Inventories

| | Group | | Company | |
|------------------|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Raw materials | 71,116 | 83,982 | 19,155 | 24,783 |
| Work in progress | 35,504 | 38,292 | 4,261 | 7,753 |
| Finished goods | 50,017 | 43,849 | 16,232 | 18,593 |
| | 156,637 | 166,123 | 39,648 | 51,129 |

During the year, the Group recognised a provision for raw materials of HK\$3,523,000 (2006: HK\$3,225,000) and reversed a provision for finished goods of HK\$2,392,000 (2006: provision made of HK\$234,000).

Notes to the Financial Statements

For the year ended 31 December 2007

14 Trade and other receivables

| | Group | | Company | |
|--|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Trade receivables | 111,422 | 147,121 | 66,445 | 91,152 |
| Less: provision for impairment of receivables | (2,955) | (7,353) | – | – |
| Trade receivables, net | 108,467 | 139,768 | 66,445 | 91,152 |
| Prepayments and other receivables | 42,402 | 46,616 | 8,413 | 8,630 |
| Amount due from ultimate holding company | 8,194 | 13,961 | 8 | – |
| Amount due from a related company | 328 | – | – | – |
| Amounts due from fellow subsidiaries | 419 | 4,014 | 227 | – |
| Amounts due from associates | 283 | 213 | – | – |
| Amounts due from subsidiaries | – | – | 68,109 | 45,777 |
| Loan to a fellow subsidiary | 8,300 | – | – | – |
| | 168,393 | 204,572 | 143,202 | 145,559 |

The fair values of trade and other receivables approximate their carrying values.

Amounts due from ultimate holding company, a related company, fellow subsidiaries, associates and subsidiaries are unsecured, interest-free and repayable on demand.

Loan to a fellow subsidiary is unsecured, interest-bearing at 7.5% per annum and repayable on 31 May 2008.

Notes to the Financial Statements

For the year ended 31 December 2007

14 Trade and other receivables (Continued)

At 31 December 2007 and 2006, the aging analysis of the trade receivables was (net of provision for impairment) as follows:

| | Group | | Company | |
|---|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Current | 85,718 | 102,395 | 58,914 | 73,879 |
| 1 to 3 months | 16,239 | 17,470 | 6,291 | 10,550 |
| More than 3 months but less than 1 year | 5,711 | 19,125 | 951 | 6,574 |
| Over 1 year | 799 | 778 | 289 | 149 |
| | 108,467 | 139,768 | 66,445 | 91,152 |

The credit quality of trade receivables that are neither past due nor impaired can be assessed by reference to historical information about counterparty default rates:

| | Group | | Company | |
|---|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Counterparties without external credit rating | | | | |
| Group 1 | – | – | – | – |
| Group 2 | 90,183 | 112,157 | 62,060 | 82,560 |
| | 90,183 | 112,157 | 62,060 | 82,560 |

Group 1 – new customers (less than 6 months).

Group 2 – existing customers (more than 6 months) with no defaults in the past.

As of 31 December 2007, the Group's trade receivables of HK\$18,284,000 (2006: HK\$27,612,000) were past due but not impaired. These relate to a number of independent customers for whom there is no recent history of default. The aging analysis of these trade receivables is as follows:

| | Group | | Company | |
|--------------------------------------|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Overdue less than and up to 3 months | 11,774 | 8,467 | 3,145 | 1,869 |
| Overdue by 3 months to 1 year | 5,711 | 18,367 | 951 | 6,574 |
| Overdue by more than 1 year | 799 | 778 | 289 | 149 |
| | 18,284 | 27,612 | 4,385 | 8,592 |

Notes to the Financial Statements

For the year ended 31 December 2007

14 Trade and other receivables (Continued)

The carrying amounts of these trade receivables were denominated in the following currencies:

| | Group | | Company | |
|------------------|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| HK dollar | 1,516 | 2,450 | – | – |
| US dollar | 98,737 | 120,816 | 66,445 | 85,017 |
| Renminbi | 8,214 | 10,367 | – | – |
| Other currencies | – | 6,135 | – | 6,135 |
| | 108,467 | 139,768 | 66,445 | 91,152 |

Movements on the provision for impairment of trade receivables were as follows:

| | Group | | Company | |
|--------------------------|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| At 1 January | 7,353 | 42,512 | – | 21,157 |
| Provision for impairment | 3,163 | – | – | – |
| Receivables written off | (7,210) | (33,633) | – | (17,814) |
| Write back of provision | (462) | (1,526) | – | (3,343) |
| Exchange differences | 111 | – | – | – |
| At 31 December | 2,955 | 7,353 | – | – |

The provision and reversal for impaired receivables have been included in administrative expenses in income statement (Note 24). The Group does not hold any collateral as security.

The other classes within trade and other receivables do not contain impaired assets.

The maximum exposure to credit risk at the reporting date is the fair value of each class of receivable mentioned above.

The Group does not hold any collateral as security.

Notes to the Financial Statements

For the year ended 31 December 2007

15 Cash and cash equivalents

| | Group | | Company | |
|---------------------------------|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Cash at bank and in hand | 79,316 | 80,545 | 16,899 | 11,769 |
| Short-term bank deposits | 27,906 | 2,253 | 17,162 | – |
| | <u>107,222</u> | <u>82,798</u> | <u>34,061</u> | <u>11,769</u> |
| Maximum exposure to credit risk | <u>106,205</u> | <u>81,709</u> | <u>33,726</u> | <u>11,607</u> |

The effective interest rate on short-term bank deposits was 3.2% (2006: 4.7%); these deposits have an average maturity of 5 days (2006: 4 days).

Included in the balances of approximately HK\$14,422,000 (2006: HK\$10,734,000) represented Renminbi deposits placed with banks in the PRC by the Group. The remittance of these funds out of the PRC is subject to the exchange control restrictions imposed by the PRC government.

Cash, cash equivalents and bank overdrafts include the following for the purposes of the cash flow statement:

| | Group | |
|---------------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 |
| Cash and cash equivalents | 107,222 | 82,798 |
| Bank overdrafts (Note 19) | – | (7,962) |
| | <u>107,222</u> | <u>74,836</u> |

Notes to the Financial Statements

For the year ended 31 December 2007

16 Share capital

| | Company | |
|----------------------------------|---------------------------------------|--------------------------------|
| | Number of shares (in thousands) | Ordinary shares HK\$'000 |
| Authorised: | | |
| Ordinary shares of US\$0.01 each | | |
| At 31 December 2007 and 2006 | 5,000,000 | 390,000 |
| Issued and fully paid: | | |
| Ordinary shares of US\$0.01 each | | |
| At 31 December 2007 and 2006 | 668,529 | 52,019 |

Share options

The Company has a share option scheme which was adopted on 22 January 2002 whereby the directors of the Company are authorised, at their discretion, to invite employees of the Group, including directors of any company in the Group, to take up options to subscribe for shares of the Company. The exercise price of the options is the highest of (i) the nominal value of the shares, (ii) the closing price of the shares on the SEHK on the date of grant and (iii) the average closing price of the shares on the SEHK for the five business days immediately preceding the date of grant. The options are exercisable progressively after one to three years from the date of grant and are exercisable for a period to be notified by the directors to each option holder upon the grant of option. Such period will not exceed ten years from the date on which the option is granted.

Notes to the Financial Statements

For the year ended 31 December 2007

16 Share capital (Continued)

Share options (Continued)

Share options outstanding at the end of the year have the following terms:

| Exercisable period | Exercise price per share | Number of options | |
|------------------------------------|-----------------------------|------------------------|------------------------|
| | | 2007 (in thousands) | 2006 (in thousands) |
| Directors: | | | |
| 7 February 2003 to 7 February 2012 | HK\$1.18 | 2,400 | 1,880 |
| 15 April 2004 to 15 April 2013 | HK\$1.43 | — | 1,365 |
| 2 January 2005 to 2 January 2014 | HK\$1.87 | 3,500 | 3,500 |
| | | 5,900 | 6,745 |
| Employees: | | | |
| 7 February 2003 to 7 February 2012 | HK\$1.18 | 3,641 | 4,681 |
| 15 April 2004 to 15 April 2013 | HK\$1.43 | 455 | 455 |
| 2 January 2005 to 2 January 2014 | HK\$1.87 | 4,350 | 5,350 |
| | | 14,346 | 17,231 |

In respect of the options granted, the maximum percentage of the share options which may be exercised is determined in stages as follows:

| | |
|----------------------------------|-------------|
| On or after 1st year anniversary | 30% |
| On or after 2nd year anniversary | another 30% |
| On or after 3rd year anniversary | another 40% |

Notes to the Financial Statements

For the year ended 31 December 2007

16 Share capital (Continued)

Share options (Continued)

Movements in the number of share options outstanding during the year are as follows:

| | 2007 | | 2006 | |
|----------------|---|--|---|--|
| | Weighted average exercise price per share | Number of options (in thousands) | Weighted average exercise price per share | Number of options (in thousands) |
| At 1 January | HK\$1.56 | 17,231 | HK\$1.56 | 22,631 |
| Lapsed | HK\$1.54 | (2,885) | HK\$1.54 | (5,400) |
| At 31 December | HK\$1.57 | 14,346 | HK\$1.56 | 17,231 |

Notes to the Financial Statements

For the year ended 31 December 2007

17 Reserves

| | Group | | | | | Total |
|---|------------------|--------------------|---------------|---------------|---------------------|----------------|
| | Share premium | Capital reserve | General | | Retained profits | |
| | | | reserve | Exchange | | |
| | | | fund | reserve | | |
| HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | |
| Balance at 1 January 2006 | 176,893 | 5,969 | 15,045 | 8,393 | 284,630 | 490,930 |
| Currency translation differences | – | – | – | 7,499 | – | 7,499 |
| Loss for the year | – | – | – | – | (129,671) | (129,671) |
| Equity settled share-based transactions | – | 860 | – | – | – | 860 |
| Balance at 31 December 2006 | 176,893 | 6,829 | 15,045 | 15,892 | 154,959 | 369,618 |
| Balance at 1 January 2007 | 176,893 | 6,829 | 15,045 | 15,892 | 154,959 | 369,618 |
| Currency translation differences | – | – | – | 15,185 | – | 15,185 |
| Loss for the year | – | – | – | – | (4,831) | (4,831) |
| Appropriation to general reserve fund | – | – | 3,382 | – | (3,382) | – |
| Balance at 31 December 2007 | 176,893 | 6,829 | 18,427 | 31,077 | 146,746 | 379,972 |

| | Company | | | | |
|---|------------------|--------------------|---------------------|----------------|---------|
| | Share premium | Capital reserve | Retained profits | Total | |
| | | | | | reserve |
| | | | | | fund |
| HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | | |
| Balance at 1 January 2006 | 176,893 | 5,969 | 210,411 | 393,273 | |
| Loss for the year | – | – | (103,092) | (103,092) | |
| Equity settled share-based transactions | – | 860 | – | 860 | |
| Balance at 31 December 2006 | 176,893 | 6,829 | 107,319 | 291,041 | |
| Balance at 1 January 2007 | 176,893 | 6,829 | 107,319 | 291,041 | |
| Profit for the year | – | – | 25,462 | 25,462 | |
| Balance at 31 December 2007 | 176,893 | 6,829 | 132,781 | 316,503 | |

Notes to the Financial Statements

For the year ended 31 December 2007

17 Reserves (Continued)

(i) Share premium

The application of the share premium account is governed by Sections 48B of the Hong Kong Companies Ordinance.

(ii) Capital reserve

The capital reserve comprises the fair value of the actual or estimated number of unexercised share options granted to directors and employees of the Group recognised in accordance with the accounting policy adopted for share-based payments in Note 2.18(b).

(iii) General reserve fund

According to the PRC laws applicable to wholly-owned foreign investment enterprises, the PRC subsidiaries of the Company are required to set up a general reserve fund and appropriate at least 10% of their annual net profits after taxation, as determined under PRC accounting regulations, to the general reserve fund until the balance of the fund equals to 50% of the respective enterprise's registered capital. This fund can be used to make good losses and to convert into paid-up capital. Appropriations to the general reserve fund are at the discretion of the respective board of directors of the subsidiaries.

(iv) Exchange reserve

The exchange reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations. The reserve is dealt with in accordance with the accounting policies set out in Note 2.4.

18 Trade and other payables

| | Group | | Company | |
|--|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Trade payables and accrued charges | 146,310 | 153,011 | 23,754 | 24,729 |
| Amount due to ultimate holding company | — | 36 | — | — |
| Amounts due to fellow subsidiaries | 2,635 | 4,425 | — | — |
| Amounts due to associates | — | 43 | — | — |
| Amounts due to subsidiaries | — | — | 73,078 | 102,580 |
| | 148,945 | 157,515 | 96,832 | 127,309 |

Notes to the Financial Statements

For the year ended 31 December 2007

18 Trade and other payables (Continued)

Amount due to ultimate holding company, fellow subsidiaries, associates and subsidiaries are unsecured, interest free and repayable on demand.

The fair values of trade and other payables approximate their carrying values.

At 31 December 2007 and 2006, the aging analysis of the trade payables was as follows:

| | Group | | Company | |
|-----------------------------------|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Within 1 month | 42,216 | 51,357 | 4,373 | 5,289 |
| After 1 month but within 3 months | 17,726 | 23,897 | 700 | 1,554 |
| After 3 month but within 6 months | 8,718 | 5,641 | 10 | 1,181 |
| After 6 month but within 1 year | 713 | 2,988 | – | 2,018 |
| Over 1 year | 903 | 1,164 | – | 223 |
| | 70,276 | 85,047 | 5,083 | 10,265 |

The carrying amounts of trade payables are denominated in the following currencies:

| | Group | | Company | |
|------------------|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| HK dollar | 6,547 | 10,425 | 4,122 | 7,870 |
| US dollar | 7,121 | 8,859 | 961 | 2,395 |
| Renminbi | 55,537 | 63,109 | – | – |
| Other currencies | 1,071 | 2,654 | – | – |
| | 70,276 | 85,047 | 5,083 | 10,265 |

Notes to the Financial Statements

For the year ended 31 December 2007

19 Borrowings

| | Group | | Company | |
|------------------------------|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Non-current | | | | |
| – Bank borrowings, secured | 780 | 4,800 | – | 4,800 |
| – Loan from a third party | – | 3,884 | – | – |
| | <u>780</u> | <u>8,684</u> | <u>–</u> | <u>4,800</u> |
| Current | | | | |
| – Bank overdrafts | – | 7,962 | – | – |
| – Bills payables | – | 18,393 | – | – |
| – Bank borrowings, secured | 109,084 | 78,635 | 54,604 | 18,525 |
| – Bank borrowings, unsecured | 4,800 | 25,800 | 4,800 | 25,800 |
| | <u>113,884</u> | <u>130,790</u> | <u>59,404</u> | <u>44,325</u> |
| | <u>114,664</u> | <u>139,474</u> | <u>59,404</u> | <u>49,125</u> |

At 31 December 2007, the borrowings were repayable as follows:

| | Group | | Company | |
|-----------------------|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Within 1 year | 113,884 | 130,790 | 59,404 | 44,325 |
| Between 1 and 2 years | 780 | 8,684 | – | 4,800 |
| | <u>114,664</u> | <u>139,474</u> | <u>59,404</u> | <u>49,125</u> |

Notes to the Financial Statements

For the year ended 31 December 2007

19 Borrowings (Continued)

The effective interest rates at the balance sheet date were as follows:

| | Group | | Company | |
|-------------------------|-------|-------|---------|-------|
| | 2007 | 2006 | 2007 | 2006 |
| Bank overdrafts | N/A | 7.50% | N/A | N/A |
| Bills payables | N/A | 4.50% | N/A | N/A |
| Bank borrowings | 5.66% | 5.75% | 4.61% | 5.07% |
| Loan from a third party | N/A | 7.83% | N/A | N/A |

The fair values of borrowings approximate their carrying values.

The carrying amounts of the borrowings are denominated in the following currencies:

| | Group | | Company | |
|------------|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| HK dollar | 43,800 | 29,684 | 43,800 | 25,800 |
| US dollar | 38,764 | 47,436 | 15,604 | 23,325 |
| Renminbi | 32,100 | 54,393 | – | – |
| Korean Won | – | 7,961 | – | – |
| | 114,664 | 139,474 | 59,404 | 49,125 |

Notes to the Financial Statements

For the year ended 31 December 2007

20 Deferred income tax

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The offset amounts are as follows:

| | Group | | Company | |
|---|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Deferred income tax asset to be recovered after more than 12 months | (3,826) | (3,180) | – | – |
| Deferred income tax liabilities to be settled after more than 12 months | 248 | 322 | 248 | 322 |
| | (3,578) | (2,858) | 248 | 322 |

The gross movement on the deferred income tax account is as follows:

| | Group | | Company | |
|------------------------------------|------------------|------------------|------------------|------------------|
| | 2007 HK\$'000 | 2006 HK\$'000 | 2007 HK\$'000 | 2006 HK\$'000 |
| Balance at 1 January | (2,858) | (6,719) | 322 | 741 |
| Exchange differences | (199) | (76) | – | – |
| Recognised in the income statement | (521) | 3,937 | (74) | (419) |
| Balance at 31 December | (3,578) | (2,858) | 248 | 322 |

Notes to the Financial Statements

For the year ended 31 December 2007

20 Deferred income tax (Continued)

The movement in deferred income tax assets and liabilities during the year, without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

| | Group | | | | Total |
|------------------------------------|------------------------------------|--------------|---------------------------------|----------------|----------------|
| | Accelerated tax depreciation | Tax losses | Defined benefit liability | Others | |
| | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | |
| At 1 January 2006 | 937 | (5,198) | (782) | (1,676) | (6,719) |
| Exchange differences | (10) | (13) | (23) | (30) | (76) |
| Recognised in the income statement | (191) | 4,521 | 283 | (676) | 3,937 |
| At 31 December 2006 | <u>736</u> | <u>(690)</u> | <u>(522)</u> | <u>(2,382)</u> | <u>(2,858)</u> |
| At 1 January 2007 | 736 | (690) | (522) | (2,382) | (2,858) |
| Exchange differences | (53) | – | (29) | (117) | (199) |
| Recognised in the income statement | (755) | (43) | 824 | (547) | (521) |
| At 31 December 2007 | <u>(72)</u> | <u>(733)</u> | <u>273</u> | <u>(3,046)</u> | <u>(3,578)</u> |
| | Company | | | | |
| | Accelerated tax allowance | Tax losses | Others | Total | |
| | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | |
| At 1 January 2006 | 1,031 | – | (290) | 741 | |
| Recognised in the income statement | (19) | (690) | 290 | (419) | |
| At 31 December 2006 | <u>1,012</u> | <u>(690)</u> | <u>–</u> | <u>322</u> | |
| At 1 January 2007 | 1,012 | (690) | – | 322 | |
| Recognised in the income statement | (31) | (43) | – | (74) | |
| At 31 December 2007 | <u>981</u> | <u>(733)</u> | <u>–</u> | <u>248</u> | |

Deferred income tax assets are recognised for tax loss carry-forwards to the extent that the realisation of the related tax benefit through the future taxable profits is probable. The Group did not recognise deferred income tax assets of HK\$29,870,000 (2006: HK\$16,731,000) in respect of losses amounting to HK\$115,867,000 (2006: HK\$68,199,000) that can be carried forward against future taxable income. Approximately HK\$4,687,000 (2006: HK\$4,690,000) of the unrecognised tax losses have no expiry date and the remaining balance will expire at various dates up to and including 2012 (2006: 2011).

Notes to the Financial Statements

For the year ended 31 December 2007

21 Retirement benefit obligations

The Group participates in a defined benefit retirement plan which covers the Group's Korean employees.

(i) The amounts recognised in the balance sheet are determined as below:

| | Group | | Company | |
|--|---------|---------|---------|-------|
| | 2007 | 2006 | 2007 | 2006 |
| Present value of the defined benefit obligations | 19,536 | 17,903 | 9,073 | 6,537 |
| Fair value of plan assets | (6,282) | (6,608) | – | – |
| | 13,254 | 11,295 | 9,073 | 6,537 |
| Unrecognised actuarial loss | (2,565) | (592) | – | – |
| | 10,689 | 10,703 | 9,073 | 6,537 |

(ii) Reconciliation of the present value of defined benefit obligations is as follows:

| | Group | |
|-----------------------|----------|----------|
| | 2007 | 2006 |
| | HK\$'000 | HK\$'000 |
| At 1 January | 17,903 | 15,081 |
| Current services cost | 3,200 | 3,167 |
| Interest cost | 902 | 819 |
| Benefits paid | (5,144) | (4,047) |
| Actuarial losses | 2,016 | 2,295 |
| Exchange differences | 659 | 588 |
| At 31 December | 19,536 | 17,903 |

Notes to the Financial Statements

For the year ended 31 December 2007

21 Retirement benefit obligations (Continued)

(iii) Reconciliation of the fair value of plan asset is as follows:

| | Group | |
|--------------------------------|----------|----------|
| | 2007 | 2006 |
| | HK\$'000 | HK\$'000 |
| At 1 January | 6,608 | 5,907 |
| Employer contributions | 1,428 | 2,048 |
| Expected return on plan assets | 159 | 184 |
| Benefits paid | (2,227) | (1,778) |
| Actuarial gains | 60 | 17 |
| Exchange differences | 254 | 230 |
| At 31 December | 6,282 | 6,608 |

As at 31 December 2007 and 2006, the Group's liability under this plan is covered by deposits with several insurance companies. There is no plan asset invested in the Company's own financial instruments or any property occupied or other assets used by the Group.

(iv) The amounts recognised in the income statement are as follows:

| | Group | |
|--|----------|----------|
| | 2007 | 2006 |
| | HK\$'000 | HK\$'000 |
| Current service cost | 3,200 | 3,167 |
| Interest cost | 902 | 819 |
| Expected return on plan assets | (159) | (184) |
| Net actuarial gains recognised during the year | — | (24) |
| Expenses recognised in the income statement | 3,943 | 3,778 |

Notes to the Financial Statements

For the year ended 31 December 2007

21 Retirement benefit obligations (Continued)

(iv) The amounts recognised in the income statement are as follows: (Continued)

The principal actuarial assumptions used were as follows:

| | 2007 | 2006 |
|--------------------------------|------|------|
| Discount rate | 7.0% | 5.5% |
| Expected return on plan assets | 3.5% | 3.5% |
| Future salary increases | 5.0% | 4.0% |

22 Other gains/(losses) – net

| | 2007 HK\$'000 | 2006 HK\$'000 |
|---|------------------|------------------|
| Net gain on sale of property, plant and equipment | 469 | 985 |
| Other financial assets (Note 12): | | |
| – fair value gains/(losses) | 5,947 | (616) |
| Net foreign exchange losses | (3,982) | (5,907) |
| Others | (39) | (535) |
| | <u>2,395</u> | <u>(6,073)</u> |

23 Other income

| | 2007 HK\$'000 | 2006 HK\$'000 |
|---|------------------|------------------|
| Interest income from other financial assets (Note 12) | 1,659 | 2,561 |
| Reversal of trade and other payables | 1,065 | – |
| Interest income from tax certificates | 846 | – |
| Commission income | 341 | – |
| Sales of scrap materials | 163 | – |
| Sundry income | <u>2,283</u> | <u>1,464</u> |
| | <u>6,357</u> | <u>4,025</u> |

Notes to the Financial Statements

For the year ended 31 December 2007

24 Expenses by nature

| | 2007 HK\$'000 | 2006 HK\$'000 |
|--|------------------|------------------|
| Changes in inventories of finished goods and work in progress | 1,332 | (6,728) |
| Raw materials and consumables used | 515,021 | 640,040 |
| Water and electricity | 16,834 | 17,743 |
| Freight and transportation | 21,809 | 20,169 |
| Depreciation | 30,105 | 26,070 |
| Amortisation of prepaid operating lease payments | 440 | 297 |
| Operating lease payments | 22,684 | 27,363 |
| Auditors' remuneration | 3,922 | 3,823 |
| Commission charges | 9,572 | 10,946 |
| Provision for inventories | 1,132 | 3,459 |
| Provision/(write back) for trade receivables | 2,701 | (1,526) |
| Telephone and communications | 5,748 | 6,049 |
| Postage and courier charges | 3,749 | 5,206 |
| Employee benefit expenses | 229,699 | 249,206 |
| Others | 105,515 | 97,730 |
| | | |
| Total cost of sales, selling and distribution expenses and administrative expenses | 970,263 | 1,099,847 |

25 Employee benefit expense

| | 2007 HK\$'000 | 2006 HK\$'000 |
|--|------------------|------------------|
| Wages and salaries, including other termination benefits HK\$504,000 (2006: HK\$976,000) | 220,552 | 240,344 |
| Share options granted to directors and employees | – | 860 |
| Pension costs – defined contribution plans | 5,204 | 4,224 |
| Pension costs – defined benefit plans (Note 21) | 3,943 | 3,778 |
| | 229,699 | 249,206 |

Notes to the Financial Statements

For the year ended 31 December 2007

25 Employee benefit expense (Continued)

(a) Directors' and senior management's emoluments

The remuneration of every director for the year ended 31 December 2007 is set out below:

| | Directors' fees HK\$'000 | Salaries, allowances and benefits in kind HK\$'000 | Share-based Payments HK\$'000 | Total HK\$'000 |
|--|--------------------------------|---|-------------------------------------|-------------------|
| | <u>HK\$'000</u> | <u>HK\$'000</u> | <u>HK\$'000</u> | <u>HK\$'000</u> |
| Chairman and executive director | | | | |
| Kyoo Yoon Choi | 240 | 1,123 | – | 1,363 |
| Executive director | | | | |
| Young M Lee | – | 1,507 | – | 1,507 |
| James Wang | – | 856 | – | 856 |
| Jung Kuk Lee (appointed on 31 May 2007) | – | 479 | – | 479 |
| Hyun Ho Kim (appointed on 31 May 2007) | – | 497 | – | 497 |
| Shin Hee Cha (resigned on 31 May 2007) | – | 693 | – | 693 |
| Tae Sub Choi (resigned on 31 May 2007) | – | 454 | – | 454 |
| Independent non-executive directors | | | | |
| Valiant, Kin Piu Cheung | 140 | – | – | 140 |
| Cheong Heon Yi | 127 | – | – | 127 |
| Chan Yoo | 126 | – | – | 126 |
| | <u>633</u> | <u>5,609</u> | <u>–</u> | <u>6,242</u> |

Notes to the Financial Statements

For the year ended 31 December 2007

25 Employee benefit expense (Continued)

(a) Directors' and senior management's emoluments (Continued)

The remuneration of every director for the year ended 31 December 2006 is set out below:

| | Directors' fees HK\$'000 | Salaries, allowances and benefits in kind HK\$'000 | Share-based Payments HK\$'000 | Total HK\$'000 |
|--|--------------------------------|--|-------------------------------------|-------------------|
| | <u>HK\$'000</u> | <u>HK\$'000</u> | <u>HK\$'000</u> | <u>HK\$'000</u> |
| Chairman and executive director | | | | |
| Kyoo Yoon Choi | 240 | 4,359 | – | 4,599 |
| Executive director | | | | |
| Shin Hee Cha | – | 1,536 | 247 | 1,783 |
| Tae Sub Choi | – | 1,081 | – | 1,081 |
| Young M Lee | – | 1,580 | – | 1,580 |
| James Wang | – | 1,118 | – | 1,118 |
| Independent non-executive directors | | | | |
| Valiant, Kin Piu Cheung | 139 | – | – | 139 |
| Cheong Heon Yi | 126 | – | – | 126 |
| Chan Yoo | 120 | – | – | 120 |
| | <u>625</u> | <u>9,674</u> | <u>247</u> | <u>10,546</u> |

Mr. Kyoo Yoon Choi, Mrs. Shin Hee Cha and Mr. Tae Sub Choi together waived their entitlements of retirement benefits amounted to HK\$1,851,528 (2006: HK\$1,763,360) with effect from 1 January 2004.

Notes to the Financial Statements

For the year ended 31 December 2007

25 Employee benefit expense (Continued)

(b) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for the year include two (2006: three) directors whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining three (2006: two) individuals during the year are as follows:

| | 2007 HK\$'000 | 2006 HK\$'000 |
|---|------------------|------------------|
| Basic salaries, housing allowances, share options, other allowances and benefits in kind | 4,172 | 2,484 |

The emoluments fell within the following bands:

| | 2007 No. of employee | 2006 No. of employee |
|--------------------------------|----------------------------|----------------------------|
| Emolument bands (in HK dollar) | | |
| HK\$1,000,001 – HK\$1,500,000 | 1 | 2 |
| HK\$1,500,001 – HK\$2,000,000 | 2 | – |

Notes to the Financial Statements

For the year ended 31 December 2007

26 Finance costs – net

| | 2007 HK\$'000 | 2006 HK\$'000 |
|--|------------------|------------------|
| Finance income: | | |
| Bank interest income | 3,116 | 2,842 |
| Finance cost: | | |
| Interest expense on bank borrowings wholly repayable within five years | (8,132) | (7,684) |
| | <u>(5,016)</u> | <u>(4,842)</u> |

27 Income tax credit/(expense)

Hong Kong profits tax has been provided at the rate of 17.5% (2006: 17.5%) on the estimated assessable profit for the year.

Taxation on PRC and overseas profits has been calculated on the estimated assessable profit for the year at the rates of taxation prevailing in the PRC and other countries in which the Group operates.

| | 2007 HK\$'000 | 2006 HK\$'000 |
|--|------------------|------------------|
| Current income tax | | |
| – Hong Kong profits tax | (1,140) | (1,056) |
| – PRC and overseas taxation | (337) | (3,680) |
| – Over-provision of Hong Kong profits tax in the prior years | 12,942 | – |
| Deferred income tax credit/(charge) (Note 20) | 521 | (3,937) |
| | <u>11,986</u> | <u>(8,673)</u> |

On 16 March 2007, the National People's Congress approved the Corporate Income Tax Law of the People's Republic of China (the "new CIT Law"). The new CIT Law standardises the corporate income tax rate to 25% with effect from 1 January 2008.

Notes to the Financial Statements

For the year ended 31 December 2007

27 Income tax credit/(expense) (Continued)

The tax on the Group's loss before income tax differs from the theoretical amount that would arise using the weighted average tax rate applicable to profits of the consolidated entities as follows:

| | 2007 HK\$'000 | 2006 HK\$'000 |
|---|------------------|------------------|
| Loss before income tax | (20,215) | (122,811) |
| Tax calculated at domestic tax rates applicable to profits in the respective countries | (5,709) | (22,946) |
| Income not subject to tax | (3,199) | (3,421) |
| Expenses not deductible for tax purposes | 6,016 | 24,379 |
| Utilisation of previously unrecognised tax losses | (584) | (162) |
| Tax losses for which no deferred income tax asset was recognised | 6,176 | 10,844 |
| Over-provision in prior years | (14,686) | (21) |
| Income tax (credit)/expense | (11,986) | 8,673 |

The change in weighted average applicable tax rate is caused by a change in the profitability of the Group's subsidiaries in the respective countries.

Note a: The Company's long-standing tax dispute with the Hong Kong Inland Revenue Department ("IRD") has been settled in current year. In April 2007, the Company reached an agreement with the IRD on the tax filling basis of the Company's offshore claims for the years of assessment 1998/99 to 2005/06. Under this settlement basis, the IRD agreed that 75% of the offshore profits (which was originally claimed as 100% offshore) are not subject to Hong Kong profits tax, which resulted in a tax refund of around HK\$10 million and an overprovision of tax from prior years for around HK\$13 million.

28 Profit attributable to equity holders of the Company

The profit attributable to equity holders of the Company is dealt with in the financial statements of the Company to the extent of HK\$25,462,000 (2006: loss of HK\$103,092,000).

Notes to the Financial Statements

For the year ended 31 December 2007

29 Loss per share

(a) Basic

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

| | 2007 | 2006 |
|--|---------|-----------|
| Loss attributable to equity holders of the Company (HK\$'000) | (4,831) | (129,671) |
| Weighted average number of ordinary shares in issue (thousands) | 668,529 | 668,529 |
| Basic loss per share (HK\$ per share) | (0.007) | (0.194) |

(b) Diluted

Diluted loss per share for the years ended 31 December 2007 and 2006 is the same as the basic loss per share as the potential ordinary shares outstanding during the years were anti-dilutive.

30 Dividend

The Board of Directors do not declare or propose any dividend for the years ended 31 December 2007 and 2006.

Notes to the Financial Statements

For the year ended 31 December 2007

31 Cash generated from operations

| | 2007 | 2006 |
|--|----------|-----------|
| | HK\$'000 | HK\$'000 |
| Loss before income tax | (20,215) | (122,811) |
| Adjustments for: | | |
| – Depreciation (Note 7) | 30,105 | 26,070 |
| – Amortisation of prepaid operating lease payment (Note 6) | 440 | 297 |
| – Disposal of leasehold land and land use rights | 1,278 | – |
| – Disposal of club memberships | 32 | 431 |
| – Amortisation of intangible assets (Note 8) | 676 | 676 |
| – Impairment of intangible assets (Note 8) | 10 | – |
| – Goodwill on increase in shareholdings in a subsidiary | – | (40) |
| – Goodwill impairment charge | – | 100,194 |
| – Profit on disposal of property, plant and equipment | (469) | (985) |
| – Share-based payment and increase in retirement benefit obligations | – | 860 |
| – Fair value (gains)/losses on other financial assets (Note 22) | (5,947) | 616 |
| – Interest income from other financial assets (Note 23) | (1,659) | (2,561) |
| – Finance costs – net (Note 26) | 5,016 | 4,842 |
| – Share of loss of associates | 16 | 237 |
| – Foreign exchange losses/(gains) on operating activities | 5,083 | (2,015) |
| Changes in working capital: | | |
| – Inventories | 9,486 | (5,641) |
| – Trade and other receivables | 44,479 | (28,031) |
| – Trade and other payables | (7,670) | 48,795 |
| – Bills payables | (18,393) | 18,393 |
| Defined benefit obligations | (14) | (117) |
| Cash generated from operations | 42,254 | 39,210 |

Notes to the Financial Statements

For the year ended 31 December 2007

31 Cash generated from operations (Continued)

In the cash flow statement, proceeds from sale of property, plant and equipment comprise:

| | 2007 HK\$'000 | 2006 HK\$'000 |
|---|------------------|------------------|
| Net book amount (Note 7) | 12,185 | 2,330 |
| Net gain on sale of property, plant and equipment (Note 22) | 469 | 985 |
| Proceeds from sale of property, plant and equipment | 12,654 | 3,315 |

32 Commitments

(a) Capital commitments

Capital expenditure at the balance sheet date but not yet incurred is as follows:

| | 2007 HK\$'000 | 2006 HK\$'000 |
|---------------------------------|------------------|------------------|
| Contracted but not provided for | 13,863 | 310 |

(b) Operating lease commitments

The Group leases various properties under non-cancellable operating lease agreements. The leases have varying terms, escalation clauses and renewal rights.

Notes to the Financial Statements

For the year ended 31 December 2007

32 Commitments (Continued)

The future aggregate minimum lease payments under non-cancellable operating leases are as follows:

| | 2007 HK\$'000 | 2006 HK\$'000 |
|---|------------------|------------------|
| No later than 1 year | 15,329 | 22,192 |
| Later than 1 year and no later than 5 years | 11,212 | 13,945 |
| | <u>26,541</u> | <u>36,137</u> |

33 Related-party transactions

(a) During the year, the Group entered into the following transactions with its related parties:

(i) Sales of goods and services

| | 2007 HK\$'000 | 2006 HK\$'000 |
|----------------------------|------------------|------------------|
| – ultimate holding company | 72 | 615 |
| – a fellow subsidiary | 505 | 1,095 |
| – an associate | 732 | 975 |
| – a related company | 1,824 | – |

(ii) Purchase of goods

| | 2007 HK\$'000 | 2006 HK\$'000 |
|----------------------------|------------------|------------------|
| – ultimate holding company | – | 36 |
| – a fellow subsidiary | 8,965 | – |
| – an associate | 6,861 | 4,033 |

Notes to the Financial Statements

For the year ended 31 December 2007

33 Related-party transactions (Continued)

(a) During the year, the Group entered into the following transactions with its related parties:

(Continued)

(iii) Commission received/receivable from:

| | 2007 HK\$'000 | 2006 HK\$'000 |
|-----------------------|------------------|------------------|
| – a fellow subsidiary | 341 | – |

(iv) Interest received/receivable from:

| | 2007 HK\$'000 | 2006 HK\$'000 |
|-----------------------|------------------|------------------|
| – a fellow subsidiary | 369 | – |

(v) Rental paid/payable to:

| | 2007 HK\$'000 | 2006 HK\$'000 |
|----------------------------|------------------|------------------|
| – ultimate holding company | 3,146 | 5,079 |

(vi) Processing fees received/receivable from:

| | 2007 HK\$'000 | 2006 HK\$'000 |
|-----------------------|------------------|------------------|
| – a fellow subsidiary | 646 | – |

Notes to the Financial Statements

For the year ended 31 December 2007

33 Related-party transactions (Continued)

(a) During the year, the Group entered into the following transactions with its related parties:

(Continued)

(vii) Processing fees paid/payable to:

| | 2007 HK\$'000 | 2006 HK\$'000 |
|----------------|------------------|------------------|
| – an associate | 7,345 | – |

(viii) Sales of leasehold land and land use right and property, plant and equipment to:

| | 2007 HK\$'000 | 2006 HK\$'000 |
|----------------------------|------------------|------------------|
| – ultimate holding company | 262 | – |
| – a fellow subsidiary | 9,126 | – |

Note:

The above transactions were conducted in accordance with the terms of respective contracts.

Notes to the Financial Statements

For the year ended 31 December 2007

33 Related-party transactions (Continued)

(b) Year-end balances arising from sales/purchases of goods/services and funding

| | 2007 HK\$'000 | 2006 HK\$'000 |
|---|------------------|------------------|
| Receivables from related parties (Note 14): | | |
| – ultimate holding company | 8,194 | 13,961 |
| – fellow subsidiaries | 419 | 4,014 |
| – an associate | 283 | 213 |
| – a related company | 328 | – |
| | <u>9,224</u> | <u>18,188</u> |
| Loan to a fellow subsidiary (Note 14): | <u>8,300</u> | – |
| Payables to related parties (Note 18): | | |
| – ultimate holding company | – | 36 |
| – fellow subsidiaries | 2,635 | 4,425 |
| – an associate | – | 43 |
| | <u>2,635</u> | <u>4,504</u> |

(c) Key management compensation

| | 2007 HK\$'000 | 2006 HK\$'000 |
|---|------------------|------------------|
| Salaries and other short-term employee benefits | 10,626 | 13,669 |
| Share-based payments | – | 247 |
| | <u>10,626</u> | <u>13,916</u> |

34 Comparative figures

Certain comparative figures have been reclassified to conform to current year's presentation.

Five Year Financial Summary

Year Ended 31 December 2007

| | 2003 | 2004 | 2005 | 2006 | 2007 |
|--|-----------|-----------|-------------|-------------|-------------|
| | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| Results | | | | | |
| Turnover | 931,847 | 1,158,107 | 1,040,444 | 1,084,357 | 946,328 |
| Operating profit/(loss) | 135,410 | 62,869 | (30,367) | (117,732)* | (15,183) |
| Finance costs | (166) | (830) | (3,339) | (4,842)* | (5,016) |
| Share of (loss)/profit of associates | (850) | (142) | 652 | (237) | (16) |
| Profit/(loss) before income tax | 134,394 | 61,897 | (33,054) | (122,811) | (20,215) |
| Income tax credit/(expense) | (13,639) | (12,846) | (3,416) | (8,673) | 11,986 |
| Profit/(loss) for the year | 120,755 | 49,051 | (36,470) | (131,484) | (8,229) |
| Attributable to: | | | | | |
| Equity holders of the Company | 120,755 | 49,051 | (36,348) | (129,671) | (4,831) |
| Minority interests | – | – | (122) | (1,813) | (3,398) |
| | 120,755 | 49,051 | (36,470) | (131,484) | (8,229) |
| Earnings/(loss) per share | | | | | |
| – Basic | HK\$0.185 | HK\$0.073 | HK\$(0.054) | HK\$(0.194) | HK\$(0.007) |
| – Diluted | HK\$0.183 | HK\$0.073 | HK\$(0.054) | HK\$(0.194) | HK\$(0.007) |

* Certain comparative figures have been reclassified to conform with current year's presentation.

Five Year Financial Summary

Year Ended 31 December 2007

| | 2003 | 2004 | 2005 | 2006 | 2007 |
|--|----------------|----------------|----------------|----------------|----------------|
| Assets and liabilities | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| Non-current assets | | | | | |
| Leasehold and land use rights and property, plant and equipment | 99,411 | 120,442 | 158,359 | 216,046 | 197,175 |
| Investments in associates | 4,596 | 809 | 1,483 | 1,298 | 1,373 |
| Intangible assets | 107,609 | 102,739 | 112,659 | 17,268 | 16,623 |
| Other financial assets | 62,104 | 88,022 | 71,670* | 71,054 | 76,284 |
| Deferred income tax assets | 4,750 | 5,122 | 7,460 | 3,180 | 3,826 |
| Current assets | 481,697 | 463,431 | 440,151 | 453,493 | 432,843 |
| Current liabilities | 153,654 | 135,287 | 222,274 | 300,519 | 266,196 |
| Net current assets | 328,043 | 328,144 | 217,877 | 152,974 | 166,647 |
| Total assets less current liabilities | 606,513 | 645,278 | 569,508 | 461,820 | 461,928 |
| Deferred income tax liabilities | 11 | 926 | 741 | 322 | 248 |
| Other non-current liabilities | 11,772 | 40,363 | 10,820 | 19,387 | 11,469 |
| NET ASSETS | 594,730 | 603,989 | 557,947 | 442,111 | 450,211 |

* Certain comparative figures have been reclassified to conform with current year's presentation.

Notice of the Annual General Meeting

NOTICE IS HEREBY GIVEN that the Annual General Meeting of Dream International Limited will be held at Imperial Room III, Towers Wing, Mezzanine Floor, The Royal Pacific Hotel and Towers Hong Kong, 33 Canton Road, China Hong Kong City, Tsimshatsui, Kowloon, Hong Kong on 30 May 2008 at 10:30 a.m. for the following purposes:

Ordinary Business

1. To receive and adopt the Audited Accounts of the Company for the year ended 31 December 2007 and the reports of the directors and Auditor thereon.
2. To re-elect directors.
3. To approve the directors' remuneration for the year ended 31 December 2007 and authorise directors to fix the directors' remuneration for the year ending 31 December 2008.
4. To re-appoint PricewaterhouseCoopers as Auditor and authorise the directors to fix their remuneration.

Special Business

5. To consider and, if thought fit, pass the following resolutions as Ordinary Resolutions:-

(1) **“THAT:**

- (i) subject to paragraph (iii) below, the exercise by the directors of the Company during the Relevant Period (as hereinafter defined) of all the powers of the Company to allot, issue or otherwise deal with any unissued shares in the capital of the Company and to make or grant offers, agreements, options and other rights or issue warrants which may require the exercise of such powers be and is hereby generally and unconditionally approved;
- (ii) the approval in paragraph (i) above shall authorise the directors of the Company during the Relevant Period to make or grant offers, agreements and/or options which may require the exercise of the powers of the Company referred to in that paragraph at any time during or after the end of the Relevant Period;
- (iii) the aggregate nominal amount of unissued shares in the capital of the Company which may be allotted, issued or otherwise dealt with by the directors of the Company during the Relevant Period pursuant to paragraph (i) above, otherwise than pursuant to a Rights Issue or the exercise of subscription rights attaching to any warrants issued by the Company, shall not exceed the aggregate of 10 per cent. of the aggregate nominal amount of shares in the capital of the Company in issue as at the date of passing this resolution;

Notice of the Annual General Meeting

(iv) for the purpose of this resolution:

(a) “Relevant Period” means the period from the passing of this resolution until whichever is the earlier of:

- (1) the conclusion of the next annual general meeting of the Company;
- (2) the expiration of the period within which the next annual general meeting of the Company is required by the articles of association of the Company or by law to be held; and
- (3) the revocation or variation of the authority given under this resolution by an ordinary resolution of the shareholders of the Company in general meeting; and

(b) “Rights Issue” means an offer of shares in the capital of the Company, or an offer of warrants, options or other securities giving rights to subscribe for shares in the capital of the Company, open for a period fixed by the directors of the Company, to holders of shares in the capital of the Company whose names appear on the Register of Members of the Company on a fixed record date in proportion to their holdings of shares (subject to such exclusions or other arrangements as the directors of the Company may deem necessary or expedient in relation to fractional entitlements or having regard to any restrictions or obligations under the laws of or the requirements of any recognised regulatory body or any stock exchange).”

(2) **“THAT:**

- (i) subject to paragraphs (ii) and (iii) below, the exercise by the directors of the Company during the Relevant Period (as hereinafter defined) of all the powers of the Company to purchase Shares on The Stock Exchange of Hong Kong Limited be and is hereby generally and unconditionally approved;
- (ii) the aggregate nominal amount of Shares which may be purchased pursuant to the approval in paragraph (i) above shall not exceed 10 per cent. of the aggregate nominal amount of the share capital of the Company in issue at the date of passing this Resolution, and the said approval shall be limited accordingly;

Notice of the Annual General Meeting

- (iii) for the purpose of this Resolution:
- (a) “Relevant Period” means the period from the passing of this Resolution until whichever is the earlier of:
- (1) the conclusion of the next Annual General Meeting of the Company;
 - (2) the expiration of the period within which the next Annual General Meeting of the Company is required by the articles of association of the Company or by law to be held;
 - (3) the revocation or variation of the authority given under this Resolution by an ordinary resolution of the shareholders in general meeting; and
- (b) “Shares” means shares of all classes in the capital of the Company and warrants and other securities issued by the Company which carry a right to subscribe or purchase shares of the Company.”
- (3) “**THAT** the general mandate granted to the directors of the Company to exercise the powers of the Company to allot, issue and otherwise deal with shares in the capital of the Company and to make or grant offers, agreements, options and/or warrants which might require the exercise of such powers pursuant to Resolution 5(1) above be and is hereby extended by the addition to the total nominal amount of share capital which may be allotted or agreed conditionally or unconditionally to be allotted by the directors of the Company pursuant to such general mandate an amount representing the total nominal amount of shares in the capital of the Company purchased by the Company pursuant to the exercise by the directors of the Company in accordance with Resolution 5(2) above of the powers of the Company to purchase such shares, provided that such amount shall not exceed 10 per cent. of the aggregate nominal amount of the share capital of the Company in issue at the date of passing this Resolution.”
- (Note i)*

By order of the Board

Kyoo Yoon Choi

Chairman

Hong Kong, 28 April 2008

Notice of the Annual General Meeting

Notes:

- (i) This resolution will be proposed to members for approval provided that resolutions 5(1) and 5(2) are passed by the members.
- (ii) A member entitled to attend and vote at the above meeting shall be entitled to appoint more than one person as his proxy, to attend and vote for him in accordance with the Articles of Association of the Company. A proxy need not be a member.
- (iii) In the case of joint holders of a share the vote of the senior who tenders a vote, whether in person or by proxy, shall be accepted to the exclusion of the votes of the other joint holders and for this purpose seniority shall be determined by the order in which the names stand in the register in respect of the joint holding.
- (iv) To be valid, a form of proxy and the power of attorney or other authority (if any) under which it is signed (or a notarially certified copy thereof) must be deposited at 8th Floor, Tower 5, China HK City, 33 Canton Road, Tsimshatsui, Kowloon, Hong Kong not less than 48 hours before the time appointed for the holding of the above meeting or any adjournment thereof.
- (v) The Register of Members will be closed from 26 May 2008 to 30 May 2008, both dates inclusive, during which period no share transfers can be registered.

