Arts Group

ARTS OPTICAL INTERNATIONAL HOLDINGS LIMITED

雅視光學集團有限公司*

(Incorporated in Bermuda with limited liability)

(Stock Code: 1120)

FINAL RESULTS
FOR THE YEAR ENDED 31ST DECEMBER, 2005

FINAL RESULTS

The Board of Directors (the "Board") of Arts Optical International Holdings Limited (the "Company") is pleased to announce that the audited consolidated results of the Company and its subsidiaries (the "Group") for the year ended 31st December, 2005 together with last year's comparative figures are as follows:

CONSOLIDATED INCOME STATEMENT

FOR THE YEAR ENDED 31ST DECEMBER, 2005

	NOTES	2005 HK$'000	2004 HK$'000 (restated)
Turnover	4	**791,624**	684,959
Cost of sales		**(569,555)**	(456,996)
Gross profit		**222,069**	227,963
Other income	5	**11,117**	9,830
Distribution costs		**(33,075)**	(38,540)
Administrative expenses		**(91,938)**	(84,054)
Other expenses		**(2,207)**	(3,191)
Finance costs	7	**(21)**	(53)
Profit before taxation		**105,945**	111,955
Taxation	8	**(10,217)**	(9,195)
Profit for the year	9	**95,728**	102,760
Attributable to:			
Equity holders of the parent		**95,961**	102,408
Minority interests		**(233)**	352
		95,728	102,760
Dividends	10		
– Declared		**68,650**	90,653
– Proposed		**26,856**	34,122
		95,506	124,775
Earnings per share	11		
– Basic		**25.2 cents**	27.1 cents
– Diluted		**25.1 cents**	26.8 cents

CONSOLIDATED BALANCE SHEET

AT 31ST DECEMBER, 2005

	2005 HK$'000	2004 HK$'000 (restated)
Non-current Assets		
Investment property	**3,600**	3,200
Property, plant and equipment	**254,745**	213,028
Prepaid lease payments	**40,598**	41,245
Loan receivable	**17,589**	19,851
Goodwill	**1,274**	1,274
Available-for-sale investments	**13,358**	–
Deferred tax assets	**53**	47
Investment securities	**–**	13,653
	331,217	292,298
Current Assets		
Inventories	**162,300**	119,360
Debtors, deposits and prepayments	**248,385**	209,328
Loan receivable	**2,262**	1,131
Prepaid lease payments	**972**	970
Taxation recoverable	**263**	1,980
Pledged bank deposits	**–**	2,187
Bank balances and cash	**65,006**	108,309
	479,188	443,265
Current Liabilities		
Creditors and accrued charges	**170,206**	129,709
Taxation payable	**425**	85
	170,631	129,794
Net Current Assets	**308,557**	313,471
Total Assets less Current Liabilities	**639,774**	605,769
Capital and Reserves		
Share capital	**38,365**	37,913
Reserves	**584,844**	554,354
Equity attributable to equity holders of the parent	**623,209**	592,267
Minority Interests	**3,256**	3,489
Total equity	**626,465**	595,756
Non-current Liability		
Deferred tax liabilities	**13,309**	10,013
	639,774	605,769

Notes:

1. **APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS/CHANGES IN ACCOUNTING POLICIES**

In the current year, the Group has applied, for the first time, a number of new and revised Hong Kong Financial Reporting Standards ("HKFRS(s)"), Hong Kong Accounting Standards ("HKAS(s)") and Interpretations ("INTs") (hereinafter collectively referred to as "new HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") that are effective for accounting periods beginning on or after 1st January, 2005. The application of the new HKFRSs has resulted in a change in the presentation of the consolidated income statement, consolidated balance sheet and consolidated statement of changes in equity. In particular, the presentation of minority interests has been changed. The changes in presentation have been applied retrospectively. The adoption of the new HKFRSs has resulted in changes to the Group's accounting policies in the following areas that have an effect on how the results for the current or prior accounting years are prepared and presented.

Business Combinations

In the current year, the Group has applied HKFRS 3 "Business Combinations" which is effective for business combinations for which the agreement date is on or after 1st January, 2005. The principal effects of the application of HKFRS 3 to the Group are summarised below:

Goodwill

In previous years, goodwill arising on acquisitions prior to 1st January, 2001 was held in reserves, and goodwill arising on acquisitions after 1st January, 2001 was capitalised and amortised over its estimated useful life. The Group has applied the relevant transitional provisions in HKFRS 3. Goodwill previously recognised in reserves of HK$1,173,000 has been transferred to the Group's retained earnings on 1st January, 2005. With respect to goodwill previously capitalised on the balance sheet, the Group on 1st January, 2005 eliminated the carrying amount of the related accumulated amortisation of HK$1,275,000 with a corresponding decrease in the cost of goodwill. The Group has discontinued amortising such goodwill from 1st January, 2005 onwards and such goodwill will be tested for impairment at least annually. Goodwill arising on acquisitions after 1st January, 2005 is measured at cost less accumulated impairment losses (if any) after initial recognition. As a result of this change in accounting policy, no amortisation of goodwill has been charged in the current year. Comparative figures for 2004 have not been restated.

Excess of the Group's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities over cost (previously known as "negative goodwill")

In accordance with HKFRS 3, any excess of the Group's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities over the cost of acquisition ("discount on acquisition") is recognised immediately in profit or loss in the period in which the acquisition takes place. In previous periods, negative goodwill arising on acquisitions prior to 1st January, 2001 was held in reserves. In accordance with the relevant transitional provisions in HKFRS 3, the Group derecognised all negative goodwill on 1st January, 2005 of which negative goodwill of HK$173,000 was previously recorded in reserves, with a corresponding increase to the Group's retained earnings.

Share-based Payments

In the current year, the Group has applied HKFRS 2 "Share-based Payment" which requires an expense to be recognised where the Group buys goods or obtains services in exchange for shares or rights over shares ("equity-settled transactions"), or in exchange for other assets equivalent in value to a given number of shares or rights over shares ("cash-settled transactions"). The principal impact of HKFRS 2 on the Group is in relation to the expensing of the fair value of share options granted to directors and employees of the Company, determined at the date of grant of the share options, over the vesting period. Prior to the application of HKFRS 2, the Group did not recognise the financial effect of these share options until they were exercised. In relation to share options granted before 1st January, 2005, the Group has not applied HKFRS 2 to share options granted on or before 7th November, 2002 and share options that were granted after 7th November, 2002 and had vested before 1st January, 2005 in accordance with the relevant transitional provisions. This change has had no material effect on the results for the current or prior years.

Financial Instruments

In the current year, the Group has applied HKAS 32 "Financial Instruments: Disclosure and Presentation" and HKAS 39 "Financial Instruments: Recognition and Measurement". HKAS 32 requires retrospective application. The application of HKAS 32 has had no material effect on the presentation of financial instruments in the financial statements of the Group. HKAS 39, which is effective for annual periods beginning on or after 1st January, 2005, generally does not permit the recognition, derecognition or measurement of financial assets and liabilities on a retrospective basis. The principal effects resulting from the implementation of HKAS 39 are summarised below:

Classification and measurement of financial assets and financial liabilities

The Group has applied the relevant transitional provisions in HKAS 39 with respect to the classification and measurement of financial assets and financial liabilities that are within the scope of HKAS 39.

By 31st December 2004, the Group classified and measured its debt and equity securities in accordance with the benchmark treatment of Statement of Standard Accounting Practice 24 ("SSAP 24"). Under SSAP 24, investments in debt or equity securities are classified as "investment securities", "other investments" or "held-to-maturity investments" as appropriate. "Investment securities" are carried at cost less impairment losses (if any) while "other investments" are measured at fair value, with unrealised gains or losses included in profit or loss. "Held-to-maturity investments" are carried at amortised cost less impairment losses (if any). From 1st January, 2005 onwards, the Group has classified and measured its debt and equity securities in accordance with HKAS 39. Under HKAS 39, financial assets are classified as "financial assets at fair value through profit or loss", "available-for-sale financial assets", "loans and receivables", or "held-to-maturity financial assets". "Financial assets at fair value through profit or loss" and "available-for-sale financial assets" are carried at fair value, with changes in fair values recognised in profit or loss and equity respectively. Available-for-sale equity investments that do not have quoted market prices in an active market and whose fair value cannot be reliably measured and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments are measured at cost less impairment after initial recognition. "Loans and receivables" and "held-to-maturity financial assets" are measured at amortised cost using the effective interest method after initial recognition.

On 1st January, 2005, the Group reclassified its investment securities of HK$13,653,000 which are unlisted equity securities whose fair value cannot be measured reliably to available-for-sale investments and are stated at cost less impairment losses. This change in accounting policy has had no material effect on the financial statements for the current or prior accounting periods.

Derecognition

HKAS 39 provides more rigorous criteria for the derecognition of financial assets than the criteria applied in previous periods. Under HKAS 39, a financial asset is derecognised, when and only when, either the contractual rights to the asset's cash flows expire, or the asset is transferred and the transfer qualifies for derecognition in accordance with HKAS 39. The decision as to whether a transfer qualifies for derecognition is made by applying a combination of risks and rewards and control tests. The Group has applied the relevant transitional provisions and applied the revised accounting policy prospectively to transfers of financial assets from 1st January, 2005 onwards. As a result, the Group's bill receivables discounted with full recourse which were derecognised prior to 1st January, 2005 have not been restated. This change in accounting policy has had no material effect on results for the current year.

Leases

Owner-occupied Leasehold Interest in Land

In previous years, owner-occupied leasehold land and buildings were included in property, plant and equipment and measured using the cost model. In the current year, the Group has applied HKAS 17 "Leases". Under HKAS 17, the land and buildings elements of a lease of land and buildings are considered separately for the purposes of lease classification, unless the lease payments cannot be allocated reliably between the land and buildings elements, in which case, the entire lease is generally treated as a finance lease. To the extent that the allocation of the lease payments between the land and buildings elements can be made reliably, the leasehold interests in land are reclassified to prepaid lease payments under operating leases, which are carried at cost and amortised over the lease term on a straight-line basis. This change in accounting policy has been applied retrospectively (see note 2 for the financial impact).

Investment Properties
In the current year, the Group has, for the first time, applied HKAS 40 "Investment Property". The Group has elected to use the fair value model to account for its investment properties which requires gains or losses arising from changes in the fair value of investment properties to be recognised directly in profit or loss for the year in which they arise. In previous years, investment properties under the SSAP 13 "Accounting for Investment Properties" were measured at open market values, with revaluation surplus or deficits credited or charged to investment property revaluation reserve unless the balance on this reserve was insufficient to cover a revaluation decrease, in which case the excess of the revaluation decrease over the balance on the investment property revaluation reserve was charged to the income statement. Where a decrease had previously been charged to the income statement and revaluation increase subsequently arose, that increase was credited to the income statement to the extent of the decrease previously charged. This change in accounting policy has had no material effect on the financial statements for the current or prior accounting periods. Accordingly, no prior year adjustment has been required.

Deferred Taxes related to Investment Properties
In previous years, deferred tax consequences in respect of revalued investment properties were assessed on the basis of the tax consequence that would follow from recovery of the carrying amount of the properties through sale in accordance with the predecessor Interpretation. In the current year, the Group has applied HK(SIC) Interpretation 21 *Income Taxes – Recovery of Revalued Non-Depreciable Assets* which removes the presumption that the carrying amount of investment properties is to be recovered through sale. Therefore, the deferred tax consequences of the investment properties are now assessed on the basis that reflect the tax consequences that would follow from the manner in which the Group expects to recover the property at each balance sheet date. In the absence of any specific transitional provisions in HK(SIC) Interpretation 21, this change in accounting policy has been applied retrospectively. Comparative figures for 2004 have been restated (see note 2 for the financial impact).

2. SUMMARY OF THE EFFECTS OF THE CHANGES IN ACCOUNTING POLICIES

The effects of the changes in the accounting policies described above on the results for the current and prior years are as follows:

	2005	2004
	HK$'000	*HK$'000*
Non-amortisation of goodwill	**510**	–
Decrease in depreciation of property, plant and equipment	**83**	83
Increase in release of prepaid lease payments	**(32)**	(32)
Increase in deferred tax expenses relating to property, plant and equipment and investment property	**(41)**	(91)
Increase (decrease) in profit for the year	**520**	(40)

The cumulative effects of the application of the new HKFRSs as at 31st December, 2004 and 1st January, 2005 are summarised below:

	As at 31st December, 2004 (originally stated)	**Retrospective adjustments Effect of HKAS 17 & INT-21**	**As at 31st December, 2004 (restated)**	**Prospective adjustments Effect of HKAS 39**	**Effect of HKFRS 3**	**As at 1st January, 2005 (restated)**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Balance sheet items						
Property, plant and equipment	254,926	(41,898)	213,028	–	–	213,028
Prepaid lease payments	–	42,215	42,215	–	–	42,215
Investment securities	13,653	–	13,653	(13,653)	–	–
Available-for-sale investments	–	–	–	13,653	–	13,653
Deferred tax assets	–	47	47	–	–	47
Deferred tax liabilities	(10,116)	103	(10,013)	–	–	(10,013)
Total effects on assets and liabilities	258,463	467	258,930	–	–	258,930
Retained earnings	447,225	467	447,692	–	(1,000)	446,692
Goodwill reserve	(1,000)	–	(1,000)	–	1,000	–
Total effects on equity	446,225	467	446,692	–	–	446,692

The financial effects of the application of the new HKFRSs to the Group's equity on 1st January 2004 are summarised below:

	As originally stated	**Adjustments**	**As restated**
	HK$'000	*HK$'000*	*HK$'000*
Retained earnings	435,430	507	435,937

3. POTENTIAL IMPACT ARISING ON THE NEW OR REVISED ACCOUNTING STANDARDS NOT YET EFFECTIVE

The Group has not early applied the following new standards and interpretations that have been issued but are not yet effective. The directors of the Company anticipate that the application of these new HKFRSs will have no material impact on the financial statements of the Group except for HKAS 39 and HKFRS 4 (Amendment) Financial guarantee contracts which requires financial guarantee contracts within the scope of HKAS 39 to be initially recognised at fair value for which the directors are still in the process of assessing the impact.

HKAS 1 (Amendment)	Capital disclosures[1]
HKAS 19 (Amendment)	Actuarial gains and losses, group plans and disclosures[2]
HKAS 21 (Amendment)	Net investment in a foreign operation[2]
HKAS 39 (Amendment)	Cash flow hedge accounting of forecast intragroup transactions[2]
HKAS 39 (Amendment)	The fair value option[2]
HKAS 39 & HKFRS 4 (Amendments)	Financial guarantee contracts[2]
HKFRS 6	Exploration for and evaluation of mineral resources[2]
HKFRS 7	Financial instruments: Disclosures[1]
HK(IFRIC) – INT 4	Determining whether an arrangement contains a lease[2]
HK(IFRIC) – INT 5	Rights to interests arising from decommissioning, restoration and environmental rehabilitation funds[2]
HK(IFRIC) – INT 6	Liabilities arising from participating in a specific market, waste electrical and electronic equipment[3]
HK(IFRIC) – INT 7	Applying the restatement approach under HKAS 29 Financial Reporting in Hyperinflationary Economies[4]

[1] Effective for annual periods beginning on or after 1st January, 2007.
[2] Effective for annual periods beginning on or after 1st January, 2006.
[3] Effective for annual periods beginning on or after 1st December, 2005.
[4] Effective for annual periods beginning on or after 1st March, 2006.

4. SEGMENT INFORMATION

Turnover
Turnover represents the net amounts received and receivable for goods sold to outside customers during the year.

Business segments
The Group is principally engaged in the design, manufacture and sales of optical products. No business segment analysis is presented as management considers this as one single business segment.

Geographical segments
The Group's operations and assets are located in Hong Kong and elsewhere in the People's Republic of China.

Segment information of the Group by location of customers is presented as below:

For the year ended 31st December, 2005

	Europe	**United States**	**Asia**	**Other regions**	**Consolidated**
	HK$'000	***HK$'000***	***HK$'000***	***HK$'000***	***HK$'000***
Turnover					
External sales	**464,088**	**232,167**	**65,537**	**29,832**	**791,624**
Result					
Segment result	**69,444**	**31,598**	**4,330**	**3,578**	**108,950**
Unallocated corporate expenses					**(4,178)**
Interest income on bank deposits					**1,194**
Finance costs					**(21)**
Profit before taxation					**105,945**
Taxation					**(10,217)**
Profit for the year					**95,728**

For the year ended 31st December, 2004

	Europe	United States	Asia	Other regions	Consolidated
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000* (restated)
Turnover					
External sales	348,563	246,584	59,305	30,507	684,959
Result					
Segment result	63,622	44,840	2,576	4,727	115,765
Unallocated corporate expenses					(4,463)
Interest income on bank deposits					706
Finance costs					(53)
Profit before taxation					111,955
Taxation					(9,195)
Profit for the year					102,760

5. OTHER INCOME

Included in other income are:

	2005	2004
	HK$'000	*HK$'000*
Sales of scrap materials	**6,333**	3,815
Revaluation increase in investment property	**400**	700
Interest income on bank deposits	**1,194**	706
Gain on disposal of property, plant and equipment	**–**	626
Property rental income less negligible outgoings	**286**	320
Dividend income from available-for-sale investments	**416**	–
Net foreign exchange gains	**1,564**	–

6. INCOME STATEMENT CLASSIFICATION

Included in cost of sales is an amount of HK$3,342,000 (2004: Nil) in respect of a write-down of raw materials, work in progress and finished goods to their estimated net realisable values.

7. FINANCE COSTS

The finance costs represent interest expense on bank borrowings wholly repayable within five years.

8. TAXATION

	2005	2004
	HK$'000	*HK$'000* (restated)
The charge comprises:		
Current taxation		
Hong Kong Profits Tax		
– Current year	**7,541**	7,209
– Overprovision in respect of prior years	**(614)**	(175)
	6,927	7,034
Deferred taxation		
Current year	**3,290**	2,161
	10,217	9,195

Hong Kong Profits Tax is calculated at 17.5% on the estimated assessable profit for the year.

A portion of the Group's profits neither arises in, nor is derived from, Hong Kong. Accordingly, that portion of the Group's profit is not subject to Hong Kong Profits Tax. Further, in the opinion of the directors, that portion of the Group's profit is not subject to taxation in any other jurisdiction in which the Group operates for both years.

9. PROFIT FOR THE YEAR

	2005	2004
	HK$'000	*HK$'000* (restated)
Profit for the year has been arrived at after charging:		
Auditors' remuneration	**1,289**	1,080
Amortisation of goodwill (include in other expenses)	**–**	510
Depreciation of property, plant and equipment	**49,105**	46,510
Total amortisation and depreciation	**49,105**	47,020
Operating lease rentals in respect of rented premises	**7,218**	7,432
Loss on disposal of property, plant and equipment	**1,400**	–
Release of prepaid lease payments	**970**	851
Staff costs		
– Directors' emoluments	**2,585**	2,818
– Other staff		
– Salaries and other allowances	**148,848**	120,868
– Retirement benefit scheme contributions	**1,010**	1,141
	152,443	124,827
and after crediting:		
Gross rental income	**286**	320
Less: outgoings	**–**	–
Net rental income	**286**	320

10. DIVIDENDS

	2005 *HK$'000*	2004 *HK$'000*
Second special dividend paid in respect of 2003 of 7 cents per share	–	26,381
Final dividend paid in respect of 2004 of 9 cents (2003: 8 cents) per share	**34,122**	30,150
Interim dividend paid in respect of 2005 of 9 cents (2004: 9 cents) per share	**34,528**	34,122
	68,650	90,653
Final dividend proposed in respect of 2005 of 7 cents (2004: 9 cents) per share	**26,856**	34,122
	95,506	124,775

The final dividend in respect of 2005 of 7 cents (2004: 9 cents) per share has been proposed by the directors and is subject to approval by the shareholders in the forthcoming annual general meeting.

11. EARNINGS PER SHARE

The calculation of the basic and diluted earnings per share attributable to the ordinary equity holders of the Company is based on the following data:

	2005 *HK$'000*	2004 *HK$'000* (restated)
Earnings for the purposes of basic and diluted earnings per share	**95,961**	102,408
	Number of shares	
Weighted average number of shares for the purpose of basic earnings per share	**380,692,192**	377,827,104
Effect of dilutive potential shares in respect of share options	**2,015,810**	4,018,679
Weighted average number of shares for the purpose of diluted earnings per share	**382,708,002**	381,845,783

Impact of changes in accounting policies

Changes in Group's accounting policies during the year are described in details in note 1. To the extent that changes have had an impact on results reported for 2005 and 2004, they have had an impact on the amounts reported for earnings per share. The following table summarises that impact on both basic and diluted earnings per share:

	Impact on basic earnings per share		Impact on diluted earnings per share	
	2005 *HK cents*	2004 *HK cents*	2005 *HK cents*	2004 *HK cents*
Figures before changes in accounting policies	**25.1**	27.1	**24.9**	26.8
Effect on changes in accounting policies	**0.1**	–	**0.2**	–
Figures after changes in accounting policies	**25.2**	27.1	**25.1**	26.8

DIVIDENDS

The directors of the Company (the "Directors") have resolved to recommend a final dividend of 7 cents per share for the year ended 31st December, 2005. Subject to the approval of shareholders at the forthcoming annual general meeting to be held on 25th May, 2006, the final dividend will be payable on 20th June, 2006 to shareholders whose names appear on the register of members of the Company on 25th May, 2006.

CLOSURE OF REGISTER OF MEMBERS

The register of members of the Company will be closed from 22nd May, 2006 to 25th May, 2006, both days inclusive, during which period no transfer of shares will be effected. All transfers, accompanied by the relevant share certificates, must be lodged with the Company's share registrars in Hong Kong, Secretaries Limited at 26/F., Tesbury Centre, 28 Queen's Road East, Hong Kong for registration not later than 4:30 p.m. on 19th May, 2006 in order to qualify for the proposed final dividend mentioned above.

ANNUAL GENERAL MEETING

The annual general meeting of the Company will be held on Thursday, 25th May, 2006. For details of the annual general meeting, please refer to the Notice of Annual General Meeting which is expected to be published on or about 24th April, 2006.

BUSINESS REVIEW

Summary of results

The Group's consolidated turnover increased by 16% to HK$791.6 million (2004: HK$685.0 million) whereas its profit attributable to the equity holders of the Company declined by 6% to HK$96.0 million (2004: HK$102.4 million) in 2005. Basic earnings per share also decreased by 7% to 25.2 cents (2004: 27.1 cents) in 2005.

As reported in the interim results, the positive effects generated from the economies of scale were fully offset by the increases in production costs arising from higher raw material costs, labour wages and record energy prices. Increase in proportion of sales of sunglasses and handmade plastic frames in 2005 and appreciation of Renminbi since the second half of year had also adversely affected our gross margin. Gross profit margin declined by 5.2% to 28.1% (2004: 33.3%) in 2005. Although the management managed to cut the total expenses to sales ratio by 2.3% to 16.1% (2004: 18.4%), net profit margin (ratio of profit attributable to the equity holders of the Company to turnover) still decreased by 2.9% to 12.1% (2004: 15.0%) in 2005.

Original design manufacturing (ODM) division

Sales to ODM customers increased by 17% from HK$616.8 million in 2004 to HK$719.7 million in 2005. Sales to Europe, United States, Asia and other regions accounted for 61%, 32%, 5% and 2% respectively of the sales of this division in 2005 (2004: 53%, 39%, 5% and 3% respectively). Sales to Europe registered a satisfactory growth rate of 34% to HK$438.0 million (2004: HK$326.2 million) as more customers sourced their demand from the Fast East following the gradual closing down of eyewear production facilities in Europe. Sales to the United States declined by 6% to HK$228.0 million (2004: HK$243.2 million) as a result of consolidation of the retailing and distribution sectors of the American eyewear market in recent years. The strong demand for sunglasses, especially those made of acetate plastic materials, continued throughout 2005. Sales of prescription frames recorded a marginal growth rate of 6% to HK$413.9 million (2004: HK$390.1 million) whereas sales of sunglasses registered a strong growth rate of 34% in 2005 to HK$287.8 million (2004: HK$214.4 million). Sales of metal frames, plastic frames and spare parts accounted for 52%, 46% and 2% respectively of the Group's turnover of ODM business in 2005 (2004: 59%, 39% and 2% respectively).

Distribution division

Sales of the Group's own-branded and licensed branded products (including both spectacles and lenses) increased by 14% to HK$53.1 million in 2005 (2004: HK$46.5 million). Sales to Europe, Asia, North America and other regions accounted for 49%, 20%, 14% and 17% respectively of the Group's turnover of distribution division in 2005 (2004: 48%, 14%, 20% and 18% respectively). STEPPER, the German brand wholly owned by the Group with more than 30 distributors appointed globally, continued to be the best selling brand and key driver to the growth of this business division.

Retailing division

Turnover of the retailing division decreased by 13% to HK$18.8 million in 2005 (2004: HK$21.7 million). Retail operations in Nanjing and Shanghai were closed in 2004 and no longer had any contribution in 2005. The Group operated a total of 18 shops (2004: 17 shops), including 10 shops in Beijing and 8 shops in Shenzhen, at 31st December, 2005.

Financial position and liquidity

The current ratio of the Group as at 31st December, 2005 was 2.8 to 1 (2004: 3.4:1) with HK$479.2 million of current assets (2004: HK$443.3 million) and HK$170.6 million of current liabilities (2004: HK$129.8 million). To meet the anticipated increase in delivery requirements in the first quarter of 2006, production activity was substantially increased in the last quarter of 2005 and inventory balance increased to HK$162.3 million as at 31st December, 2005 (2004: HK$119.4 million). Inventory turnover period (ratio of inventory balance to cost of sales) also increased from 95 days in 2004 to 104 days in 2005. Debtors turnover period (ratio of the total of debtor and discounted bills balances to sales) increased slightly from 105 days in 2004 to 108 days in 2005.

The Group generated HK$109.1 million net cash inflow from it operating activities in 2005 (2004: HK$84.0 million). A relatively higher level of capital expenditure of HK$92.5 million (2004: HK$69.8 million) was incurred during 2005 for the expansion of the production capacity and upgrading of the equipment. Dividend payments amounted to HK$68.7 million were also made during the year (2004: HK$90.1 million). As a result of the above factors, the net cash position of the Group (bank and cash balance plus pledged bank deposit less bank borrowing, if any) decreased from HK$110.5 million at 31st December, 2004 to HK$65.0 million at 31st December, 2005. The Group did not have any interest bearing borrowings at the end of both years of 2004 and 2005.

As at 31st December, 2005, the Group had 383,650,000 shares (2004: 379,130,000 shares) in issue with an equity attributable to equity holders of the Company amounting to HK$623.2 million (2004: HK$592.3 million). Net asset value attributable to equity holders of the Company per share was HK$1.62 (2004: HK$1.56). Total long term liabilities and debt to equity ratio (expressed as a percentage of total long term liabilities over equity were HK$13.3 million (2004: HK$10.0 million) and 2.1% (2004: 1.7%) respectively.

The Group had limited exposure to foreign exchange rate fluctuations as most of its transactions were conducted in either United States dollars, Hong Kong dollars and Renminbi and the exchange rates movements between these currencies were relatively stable during the year, except for the one-off appreciation of Renminbi against United States dollars in July 2005.

Pledge of assets

	2005 *HK$'000*	2004 *HK$'000*
Assets pledged to banks in respect of banking facilities granted to the Group – bank deposits	–	2,187

Contingent liabilities

	2005 *HK$'000*	2004 *HK$'000*
Bills discounted with recourse	–	3,922

At 31st December, 2005, the Group had given a corporate guarantee in favour of a financial institution to secure general credit facilities to the extent of HK$9,750,000 (2004: HK$9,750,000). The extent of facilities utilised at 31st December, 2005 amounted to approximately HK$9,750,000 (2004: HK$9,750,000).

PROSPECTS

ODM Division

Although the pace of rising of the cost elements seemed to have slowed down in the second half of 2005, there is no indication that they will be coming down in the near future. The management believes that the upward trend on cost burden will continue in 2006. The strengthening of Renminbi against other currencies continues to put additional pressure on our cost control efforts. Although the Group has adjusted the selling prices of its products since late 2005, the effects will be modest and only reflected in the second half of 2006. On the demand side, our customers remain bullish about the business outlook and this division currently has four months sales orders on hands. To enhance the competitiveness of the Group, substantial capital investment for expansion of production capacity and upgrading of equipment has been made in 2005 and the management expects that this will continue in 2006.

Distribution Division

The management will continue to focus on the expansion of distribution network for its house brand STEPPER and licensed brand FIORUCCI. Some new licensed and house brands for the Asian markets may be added to strengthen the brand portfolio of this division in the second half of 2006.

Retailing Division

The operational performance of this division has been improving since the Group decided to focus on the cities of Beijing and Shenzhen two years ago. Some non-performing shops will be relocated and the overall scale of operations in these two cities should remain fairly stable in 2006.

Summary

Although the demand for the Group's products remains fairly strong, the substantial capital investment required for maintaining competitiveness, the pressure on gross margin and the increase in working capital requirements have increased the operational and financial risks of the Group's business and affected the operational cash-flow. The management will continue to adopt the guiding principles of financial prudence when executing the expansion plan and carefully monitor the impact of the above factors on cash-flow management and dividend payment capability.

EMPLOYEES AND REMUNERATION POLICIES

As at 31st December, 2005, the Group employed approximately 9,500 (2004: 7,700) full time staff in mainland China, Hong Kong and Europe. The Group remunerates its employees based on their performances, experiences and prevailing market salaries while performance bonuses are granted on a discretionary basis. Other employee benefits include insurance and medical cover, subsidised educational and training programmes, mandatory provident fund scheme as well as a share option scheme.

CORPORATE GOVERNANCE

The Company has complied with all the code provisions in effect as set out in the Code on Corporate Governance Practices in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") throughout the year ended 31st December, 2005 except for the deviations as mentioned in the section "Corporate Governance" contained in the 2005 Interim Report. Detailed information will also be included in the Corporate Government Report contained in the 2005 Annual Report.

SCOPE OF WORK OF MESSRS. DELOITTE TOUCHE TOHMATSU

The figures in respect of the preliminary announcement of the Group's consolidated balance sheet, consolidated income statement and the related notes thereto for the year ended 31st December, 2005 have been agreed by the Group's auditors, Messrs. Deloitte Touche Tohmatsu, to the amounts set out in the Group's audited consolidated financial statements for the year. The work performed by Messrs. Deloitte Touche Tohmatsu in this respect did not constitute an assurance engagement in accordance with Hong Kong Standards on Auditing, Hong Kong Standards on Review Engagements or Hong Kong Standards on Assurance Engagements issued by the Hong Kong Institute of Certified Public Accountants and consequently no assurance has been expressed by Messrs. Deloitte Touche Tohmatsu on the preliminary announcement.

The Group's consolidated financial statements for the year ended 31st December, 2005 have been reviewed by the Audited Committee and audited by Messrs. Deloitte Touche Tohmatsu.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SHARES

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

DIRECTORS

The Board comprises seven Directors, four of which are executive Directors, namely Mr. Ng Hoi Ying, Michael (the "Chairman"), Ms. Hui Pui Woon, Mr. Ng Kim Ying and Mr. Lee Wai Chung, and three are independent non-executive Directors, namely Mr. Francis George Martin, Mr. Wong Chi Wai and Mr. Chung Hil Lan Eric.

By order of the Board
Ng Hoi Ying, Michael
Chairman

Hong Kong, 11th April, 2006

* *For identification purpose only*