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ENGLISH / CHINESE

3/31/1998



PEKING CAPITAL INTERNATIONAL

GROUP LIMITED

(Incorporated in Bermuda with limited liability)

Annual Report 1998

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CORPORATE INFORMATION

Board of Directors

Executive directors

Char On Man (*Chairman and Managing Director*)
So Choi Hing, Stella
Ka Kong Wah, Henry
Li Wing Tak

Independent non-executive directors

Chan Cheuk, Christopher
Woo, Michael
Ho Wai Chi, Paul

Company Secretary

Li Wing Tak

Auditors

Ernst & Young
Certified Public Accountants
15th Floor
Hutchison House
10 Harcourt Road
Central
Hong Kong

Principal Bankers

The Yien Yieh Commercial Bank Limited
24–28 Carnarvon Road
Tsimshatsui
Kowloon
Hong Kong

Belgian Bank
Shop 14-19, Upper G/F
South Seas Centre
75 Mody Road
Tsimsha
tsui
Kowloon
Hong Kong

Hong Kong Branch Share Registrars, Warrant Registrars And Transfer Office

Tengis Limited
1601 Hutchison House
10 Harcourt Road
Central
Hong Kong

Hong Kong Legal Advisers

Woo Kwan Lee & Lo
27th Floor
Jardine House
1 Connaught Place
Central
Hong Kong

Bermuda Legal Advisers

Conyers Dill & Pearman
3408 Two Exchange Square
8 Connaught Place
Central
Hong Kong

Registered Office

Clarendon House
2 Church Street
Hamilton HM 11
Bermuda

Head Office And Principal Place of Business

Unit 1, 5th Floor
Tower 1, North Wing
Harbour Centre
1 Hok Cheung Street
Hung Hom
Kowloon
Hong Kong

NOTICE OF ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that an Annual General Meeting of the Members of Peking Apparel International Group Limited (the "Company") will be held at Unit 1, 5/F, Tower 1, North Wing, Harbour Centre, 1 Hok Cheung Street, Hung Hom, Kowloon, Hong Kong on Wednesday, 23 September 1998 at 9:45 a.m. for the following purposes:

1. To receive and consider the Audited Financial Statements and the Reports of the Directors and of the Auditors for the year ended 31 March 1998;
2. To elect Directors and to authorise the Board of Directors to fix Directors' remuneration;
3. To appoint Auditors and to authorise the Board of Directors to fix their remuneration;
4. To consider as Special Business and, if thought fit, pass with or without amendments, the following resolution as an Ordinary Resolution:

"THAT

- (a) the exercise by the Directors during the Relevant Period of all the powers of the Company to purchase its shares and warrants issued by the Company to subscribe for such shares, subject to and in accordance with the applicable laws, be and is hereby generally and unconditionally approved;
 - (b) the total nominal amount of shares to be purchased pursuant to the approval in paragraph (a) above shall not exceed 10% of the total nominal amount of the share capital of the Company in issue on the date of this Resolution, and the subscription rights attached to the warrants to be purchased pursuant to such approval shall not exceed 10% of the total subscription rights attached to all warrants outstanding on such date, and the said approval shall be limited accordingly; and
 - (c) for the purpose of this Resolution, "Relevant Period" means the period from the passing of this Resolution until whichever is the earlier of:
 - (i) the conclusion of the next Annual General Meeting of the Company;
 - (ii) the revocation or variation of the authority given under this Resolution by Ordinary Resolution of the shareholders in general meetings; or
 - (iii) the expiration of the period within which the next Annual General Meeting of the Company is required by the Bye-laws of the Company or any applicable laws to be held.";
5. To consider as Special Business and, if thought fit, pass with or without amendments, the following resolution as an Ordinary Resolution:

"THAT

- (a) the exercise by the Directors during the Relevant Period of all the powers of the Company to issue, allot and deal with additional shares of the Company and to make or grant offers, agreements and options which would or might require shares to be allotted, issued or dealt with during or after the end of the Relevant Period, in addition to any shares which may be issued on the exercise of the subscription rights under the warrants issued by the Company, be and is hereby generally and unconditionally approved, provided that, otherwise than pursuant to a rights issue where shares are offered to shareholders on a

NOTICE OF ANNUAL GENERAL MEETING

fixed record date in proportion to their then holdings of shares (subject to such exclusions or other arrangements as the Directors 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 in any territory outside Hong Kong) or any option scheme or similar arrangement for the time being adopted for the grant or issue to officers and/or employees of the Company and/or any of its subsidiaries of shares or rights to acquire shares of the Company, or any scrip dividend scheme or similar arrangement providing for the allotment of shares in lieu of the whole or part of a dividend on shares of the Company in accordance with the Bye-laws of the Company, the total nominal amount of additional shares issued, allotted, dealt with or agreed conditionally or unconditionally to be issued, allotted or dealt with shall not in total exceed 20% of the total nominal amount of the share capital of the Company in issue on the date of this Resolution and the said approval shall be limited accordingly; and

- (b) for the purpose of this Resolution, “Relevant Period” means the period from the passing of this Resolution until whichever is the earlier of:
 - (i) the conclusion of the next Annual General Meeting of the Company;
 - (ii) the revocation or variation of the authority given under this Resolution by Ordinary Resolution of the shareholders in general meetings; or
 - (iii) the expiration of the period within which the next Annual General Meeting of the Company is required by the Bye-laws of the Company or any applicable laws to be held.”;

6. To consider as Special Business and, if thought fit, pass with or without amendments, the following resolution as an Ordinary Resolution:

“**THAT** the general mandate granted to the Directors of the Company pursuant to Resolution 5 above and for the time being in force to exercise the powers of the Company to allot shares and to make or grant offers, agreements and options which might require the exercise of such powers be and is hereby extended by the total nominal amount of shares in the capital of the Company repurchased by the Company since the granting of such general mandate pursuant to the exercise by the Directors of the Company of the powers of the Company to purchase such shares, provided that such amount shall not exceed 10% of the total nominal amount of the share capital of the Company in issue on the date of this Resolution.”.

By order of the Board

Li Wing Tak

Secretary

Hong Kong, 20 August 1998

NOTICE OF ANNUAL GENERAL MEETING

Notes:

- (a) The Register of Members will be closed from Thursday, 17 September 1998 to Wednesday, 23 September 1998 (both days inclusive), during which period no transfer of shares will be registered. In order to qualify for attending the Meeting, all transfers documents accompanied by the relevant share certificates and, in the case of warrant holders, all duly completed subscription forms accompanied by the relevant warrant certificates and the appropriate subscription monies must be lodged with the Company's Share Registrar in Hong Kong, Tengis Limited, 1601 Hutchison House, 10 Harcourt Road, Central, Hong Kong not later than 4:00 p.m. on Wednesday, 16 September 1998.
- (b) A member entitled to attend and vote at the Meeting is entitled to appoint one or more proxies to attend and vote on his behalf. A proxy need not be a member of the Company.
- (c) The instrument appointing a proxy and the power of attorney or other authority, if any, under which it is signed, or a notarially certified copy of such power or authority, must be lodged with the Company's Share Registrar in Hong Kong, Tengis Limited, 1601 Hutchison House, 10 Harcourt Road, Central, Hong Kong not less than 48 hours before the time fixed for holding the Meeting.
- (d) The annual report of the Company for the year ended 31 March 1998 also containing this notice together with a circular setting out further information regarding Resolutions 4 to 6 above will be despatched to shareholders and, for information only, warrant holders as soon as practicable.

CHAIRMAN'S STATEMENT

On behalf of the Board of Directors (the "Board"), I am pleased to present the 1998 annual report of Peking Apparel International Group Limited and its subsidiaries (together the "Group").

Results

Turnover for the year ended 31 March 1998 amounted to approximately HK\$201 million, representing a decrease of approximately 36 per cent as compared to that of last year. Loss for the year after taxation amounted to approximately HK\$6 million.

Business Review

During the year under review, the Asia financial turmoil happened during our major sales seasons had affected the consumer spending and the collection of the accounts receivable. With the market competitors seriously cutting their selling prices in order to dispose of stocks to generate cash to meet their financial liabilities, the Group had difficulties both in maintaining the sales margin and liquidating the stocks. The Directors have critically reviewed the recoverability of the Group's outstanding accounts receivable and the net realisable values of stocks as at 31 March 1998 and has made appropriate general provisions for accounts receivable and stocks, respectively for the year.

The Group has developed non-leather garments sales, obtained a license to manufacture and sell leather garments using "MICKEY & CO." and established showrooms in major cities in the PRC during the year ended 31 March 1998 which incurred additional set-up and advertising costs. Apart from this, the Group's property value had devalued by approximately HK\$6 million for the year ended 31 March 1998.

Future Plan

The Group will continue to focus on leather garment manufacturing as its core business. With the current economic turmoil, the Group will adopt careful and aggressive marketing strategies to enhance the relationship with customers, so as to maintain as well as increase the market shares.

In order to expand its customer base, the Group will continue to seek for prime locations in suitable cities in the PRC and in Russia to establish representative offices and showrooms.

The Group will actively take measures to control its production cost, improve its productivity and launch new designs in order to improve its profitability. We believe that with the support of our customers and dedication of our staff, the Group's market leader position in the leather garment sector will enhance further and will be able to improve the results in the coming year.

CHAIRMAN'S STATEMENT

Dividends

The Directors do not recommend the payment of any dividend in respect of the year ended 31 March 1998.

Resignation of Directors

Subsequent to the balance sheet date, on 20 August 1998, Mr Ka Kong Wah, Henry and Mr Chan Cheuk, Christopher resigned as Directors of the Company. On behalf of the Board, I take this opportunity to thank both of them for their valuable contribution and support to the Group.

Year 2000 Issue

The Year 2000 Issue has an impact on the computer system using two-digit year presentation caused by '00' being recognised as '1900' instead of '2000'. The Group has made an assessment of the Year 2000 Issue and it is believed that this issue will not have material impact on the Group's business operations and flow of information. For the Hong Kong operations, a new software package, which can resolve the Year 2000 Issue, has been installed and is in the progress of program modification, testing and documentation update. For the PRC operations, the Group is in liaison with the software house to upgrade the software packages in order to resolve the Year 2000 Issue. The program modification and data migration is expected to be completed by mid 1999.

Estimated total costs of the Group of these new computer systems including hardware upgrade would not exceed HK\$500,000. As at 31 March 1998, approximately 60 per cent of the total estimated costs had been incurred and recorded as fixed assets and deposits in the financial statements. The aggregate amount of commitments authorised by the Directors and contracted for as at 31 March 1998 in respect of the Year 2000 Issue modification costs which has not been provided for in the financial statements is approximately HK\$100,000. As at 31 March 1998, the aggregate amount of commitments in respect of the Year 2000 modification costs which the Directors plan to authorise but not yet contracted for is approximately HK\$100,000.

Nevertheless, it is believed that the Year 2000 Issue will not pose material operational problems to the Group.

Conclusion

Finally, on behalf of the Board, I would like to extend my appreciation to our customers for their support, our management for their hardwork and our staff for their dedication.

Char On Man

Chairman

20 August 1998

MANAGEMENT DISCUSSION AND ANALYSIS

Financial Review

Turnover for the year ended 31 March 1998 amounted to approximately HK\$201 million, representing a decrease of approximately 36 per cent as compared to that of last year. The downturn of turnover for the year was due to the fact that the Asia financial crisis has seriously affected the consumer spending and the overall retail market.

Loss for the year after taxation amounted to approximately HK\$6 million. It is mainly due to the fact that market competitors seriously cutting their selling prices in order to dispose of stocks to generate cash to meet their financial liabilities and thus the Group had difficulties both in maintaining the sales margin and liquidating the stocks. As a result of this, the Group has made appropriate general provisions for accounts receivable and stocks, respectively for the year. Apart from this, the Group's property value had devalued by approximately HK\$6 million for the year ended 31 March 1998.

Furthermore, the launching of non-leather garments, the use of "MICKEY & CO." brand and the set up of representative offices and showrooms in the PRC has incurred additional set-up and advertising costs.

Liquidity and Financial Resources

The Group generally finances its operations with internally generated cash flows and banking facilities provided by its principal bankers in Hong Kong. The Group currently has aggregate composite banking facilities of approximately HK\$110 million.

Application of Proceeds of New Issue

The Group raised approximately HK\$51.6 million net of related expenses from the issue of 64.75 million new shares in connection with the listing of the Company's shares on The Stock Exchange of Hong Kong Limited on 7 March 1997.

The net proceeds from the new issue have been applied as follows:

	Planned amount	Amount utilised
	HK\$'000	up to 20 August 98
		HK\$'000
– for repaying bank loans	10,000	10,000
– for upgrading the Group's manufacturing facilities and office premises	3,000	3,000
– for setting up representative offices and showrooms in the PRC	15,000	1,300
– for additional working capital for the Group	13,600	13,600
– for setting up or acquiring an interest in a tannery	10,000	–
	<u>51,600</u>	<u>27,900</u>

The balance of the proceeds of approximately HK\$23,700,000 has been placed on fixed deposits with a bank.

MANAGEMENT DISCUSSION AND ANALYSIS

Employees and Remuneration Policies

As at 31 March 1998, the Group employed 444 full time employees, of which 427 were in the PRC and 17 in Hong Kong.

The Group remunerates its employees largely based on industry's practice. In the PRC, the Group provides staff welfare and bonus to its employee in accordance with prevailing labour law. In Hong Kong, the Group provides staff benefits including performance related bonus and other subsidies.

REPORT OF THE DIRECTORS

The directors herein present their report and the audited financial statements of the Company and the Group for the year ended 31 March 1998.

Principal activities

The principal activity of the Company is investment holding. The principal activities of the subsidiaries are set out in note 13 to the financial statements.

There have been no significant changes in these activities during the year.

Segmented information

The analysis of the Group's turnover and contribution to operating loss by principal activity and the Group's turnover by geographical area of operation for the year ended 31 March 1998 is as follows:

	Turnover HK\$'000	Contribution HK\$'000
By activity:		
Trading of tanned leather	40,827	(3,499)
Trading of fur pelts	51,422	(8,267)
Manufacture and sales of leather garments	89,588	4,740
Manufacture and sales of microfibre garments	8,675	664
Manufacture and sales of fur garments	6,923	(438)
Others	3,162	394
	<u>200,597</u>	<u>(6,406)</u>
		Turnover HK\$'000
By geographical area:		
The People's Republic of China:		
Hong Kong		19,976
Elsewhere		124,925
United States of America		30,230
Germany		11,958
Others		13,508
		<u>200,597</u>

No analysis of the contribution to trading results by geographical area has been prepared as no contribution to the Group's trading results from any of the above geographical areas is substantially out of line with the overall ratio to turnover.

REPORT OF THE DIRECTORS

Results and dividends

The Group's loss for the year ended 31 March 1998 and the state of affairs of the Company and the Group at that date are set out in the financial statements on pages 20 to 40.

The directors do not recommend the payment of any dividend in respect of the year.

Summary financial information

A summary of the results of the Group for the last five financial years and of the assets and liabilities as at the last three financial year ends, reclassified as appropriate, is set out below:

RESULTS

	Year ended 31 March				
	1998 HK\$'000	1997 HK\$'000	1996 HK\$'000	1995 HK\$'000	1994 HK\$'000
Turnover	<u>200,597</u>	<u>312,714</u>	<u>290,905</u>	<u>224,731</u>	<u>166,875</u>
Operating profit/(loss) before exceptional item	(6,406)	38,068	31,523	22,394	27,135
Exceptional item	—	5,163	—	—	—
Profit/(loss) before taxation	(6,406)	43,231	31,523	22,394	27,135
Taxation	<u>161</u>	<u>(2,753)</u>	<u>(3,600)</u>	<u>(2,800)</u>	<u>(3,003)</u>
Net profit/(loss) attributable to shareholders	<u>(6,245)</u>	<u>40,478</u>	<u>27,923</u>	<u>19,594</u>	<u>24,132</u>

ASSETS AND LIABILITIES

	As at 31 March		
	1998 HK\$'000	1997 HK\$'000	1996 HK\$'000
Fixed assets	44,560	45,394	23,870
Long term investments	3,364	3,364	4,581
Current assets	<u>178,788</u>	<u>186,441</u>	<u>97,642</u>
Total assets	<u>226,712</u>	<u>235,199</u>	<u>126,093</u>
Current liabilities	62,733	68,271	46,026
Bank loan, secured	—	—	3,737
Deferred taxation	<u>72</u>	<u>300</u>	<u>300</u>
Total liabilities	<u>62,805</u>	<u>68,571</u>	<u>50,063</u>
Net assets	<u>163,907</u>	<u>166,628</u>	<u>76,030</u>

REPORT OF THE DIRECTORS

Summary financial information (continued)

Note: The Company was incorporated on 8 August 1996 and became the holding company of the Group on 18 February 1997 pursuant to a Group reorganisation in preparation for the public listing of the Company's shares on The Stock Exchange of Hong Kong Limited on 7 March 1997. The results of the Group in respect of the three years ended 31 March 1996, which were extracted from the Company's prospectus dated 25 February 1997, are presented on a combined basis as if the Group reorganisation had taken place at the commencement of the three-year period.

Fixed assets

Details of movements in the fixed assets of the Group are set out in note 11 to the financial statements.

Subsidiaries

Particulars of the Company's subsidiaries are set out in note 13 to the financial statements.

Borrowings

Details of the Group's borrowings at the balance sheet date are set out in note 17 to the financial statements.

Share capital, warrants and share options

Details of movements in the Company's share capital and the reasons for the issues of shares, together with the particulars of warrants and share options, are set out in note 19 to the financial statements.

There are no provisions for pre-emptive rights under the Company's bye-laws or the laws of Bermuda which would oblige the Company to offer new shares on a pro rata basis to existing shareholders.

Reserves

Details of movements in the reserves of the Company and the Group during the year are set out in note 20 to the financial statements.

REPORT OF THE DIRECTORS

Directors

The directors of the Company during the year were:

Executive directors:

Char On Man

So Choi Hing, Stella

Ka Kong Wah, Henry

Li Wing Tak

Independent non-executive directors:

Chan Cheuk, Christopher

Woo, Michael

Ho Wai Chi, Paul

Subsequent to the balance sheet date, on 20 August 1998, Ka Kong Wah, Henry and Chan Cheuk, Christopher resigned as directors of the Company.

In accordance with the Company's bye-laws, Li Wing Tak will retire and, being eligible, will offer himself for re-election at the forthcoming annual general meeting.

The non-executive directors are not appointed for specific terms and are subject to retirement by rotation and re-election at the annual general meeting of the Company in accordance with the Company's bye-laws.

Directors' remuneration and five highest paid employees' remuneration

Details of the directors' remuneration and the five highest paid employees' remuneration disclosed pursuant to Section 161 of the Companies Ordinance and the Rules governing the listing of securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") are set out in notes 4 and 5 to the financial statements, respectively.

Directors' service contracts

Each of the executive directors of the Company has entered into a service contract with the Company for a term of three years with effect from 1 March 1997 and continuing thereafter on an annual basis until terminated by either party giving to the other not less than six months' notice.

Save as disclosed above, no director proposed for re-election at the forthcoming annual general meeting has a service contract with the Company which is not determinable by the Company within one year without payment other than statutory compensation.

REPORT OF THE DIRECTORS

Directors' rights to acquire shares

Apart from the share option scheme as described in note 19 to the financial statements, at no time during the year was the Company, its holding company or any of its subsidiaries a party to any arrangements to enable the Company's directors, their respective spouse or children under 18 years of age to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate.

No options were granted pursuant to the existing share option scheme during the year.

Directors' interests in shares and warrants of the Company, its subsidiaries and associated corporations

At the balance sheet date, the interests of the directors and their associates in the share capital and warrants of the Company, its subsidiaries and associated corporations as recorded in the register required to be kept under Section 29 of the Securities (Disclosure of Interests) Ordinance ("SDI Ordinance") were as follows:

(i) The Company

Shares

Name of director	Number of shares held and nature of interest		
	Corporate interests	Personal interests	Total
Char On Man	167,832,000*	18,425,000	186,257,000
So Choi Hing, Stella	—	3,885,000	3,885,000
Ka Kong Wah, Henry	—	3,108,000	3,108,000
	<u> </u>	<u> </u>	<u> </u>

Warrants

Name of director	Number of warrants held and nature of interest		
	Corporate interests	Personal interests	Total
Char On Man	33,566,400*	3,685,000	37,251,400
So Choi Hing, Stella	—	777,000	777,000
Ka Kong Wah, Henry	—	621,600	621,600
	<u> </u>	<u> </u>	<u> </u>

* These shares and warrants are held through Wellglow Investments Limited, a company in which Char On Man has total interests of 89.58%.

REPORT OF THE DIRECTORS

Directors' interests in shares and warrants of the Company, its subsidiaries and associated corporations (continued)

(ii) Subsidiary — Peking Fur Factory (Hong Kong) Limited

Name of director	Nature of interest	Number of non-voting deferred shares held
Char On Man	Personal	11,444
Ka Kong Wah, Henry	Personal	556
		<u> </u>

(iii) Associated corporation — Wellglow Investments Limited

Name of director	Number of ordinary shares held and nature of interest		
	Personal interests	Family interests	Total
Char On Man	674	100	774
So Choi Hing, Stella	60	—	60
Ka Kong Wah, Henry	30	—	30
	<u> </u>	<u> </u>	<u> </u>

Save as disclosed above, none of the directors, chief executives or their associates had any personal, family, corporate or other interests in the equity or debt securities of the Company, its subsidiaries or any of its associated corporations (as defined in the SDI Ordinance) as recorded in the register required to be kept under Section 29 of the SDI Ordinance at the balance sheet date.

Directors' interests in contracts

No director had a beneficial interest, either direct or indirect, in any contract of significance to the business of the Company to which the Company, its holding company or any of its subsidiaries was a party at the balance sheet date or at any time during the year.

Substantial shareholders

At the balance sheet date, according to the register kept under Section 16(1) of the SDI Ordinance, the only shareholder with an interest in 10% or more of the issued share capital of the Company was as follows:

Name	Number of shares held
Wellglow Investments Limited	167,832,000
	<u> </u>

This interest has also been disclosed as an interest of Char On Man under the directors' interests in shares above.

Save as disclosed above, no person had registered an interest in the share capital of the Company that was required to be recorded under Section 16(1) of the SDI Ordinance.

REPORT OF THE DIRECTORS

Biographical details of directors and senior management

Executive directors

Mr. Char On Man, aged 45, is the Group founder and has been the chairman and managing director of the Group since August 1978. He is responsible for the overall management of the Group's operations, in particular the procurement and trading of tanned leather and fur pelts, as well as overseeing the overall operation of the fur garment business. He is also a director of the Federation of Fur Manufacturers and Dealers (H.K.) Ltd.. He has over 20 years' experience in the leather and fur industries.

Ms. So Choi Hing, Stella, aged 44, is the director of sales for the Group. She is responsible for the sales and marketing of leather garments and for the Group's overall administrative operations. She has been with the Group since September 1981.

Mr. Ka Kong Wah, Henry, aged 41, is the director of administration for the Group. He is responsible for, and has over 10 years' experience in, office administration and inventory control operations in Hong Kong. He joined the Group in March 1986 and is a younger brother of Char On Man.

Mr. Li Wing Tak, aged 40, is the director of finance for the Group. He has over 10 years' experience in finance and accounting. He holds a bachelor's degree in economics from Macquarie University in Australia and is a fellow of the Hong Kong Society of Accountants and an associate member of the Australian Society of Certified Practising Accountants. He also served as the regional financial controller in two multinational trading and manufacturing companies for five years prior to joining the Group in March 1994.

Independent non-executive directors

Mr. Chan Cheuk, Christopher, aged 57, is a practising solicitor, a consultant of Woo, Kwan, Lee & Lo and currently Council Member of the Law Society of Hong Kong. He is also a non-executive director of Oriental Press Group Limited, Pak Fah Yeow International Limited and Tern Properties Company Limited. He joined the Group as a director in August 1996.

Mr. Woo, Michael, aged 53, is the managing director of Europe Fur Co., Ltd., Europe Fashions Ltd., Dongguan Mayfair Fashions Ltd. and Mayfur Canada Inc. He was the chairman of the Federation of Fur Manufacturers and Dealers (H.K.) Ltd. during the period from 1995 to 1996. He joined the Group as a director in August 1996.

Mr. Ho Wai Chi, Paul, aged 47, is currently a director of Yorkee Company Limited and China Star Entertainment Limited. He is the sole proprietor of Paul W.C. Ho & Company, Certified Public Accountants, and is an associate member of the Institute of Chartered Accountants in England and Wales, the United Kingdom and the Hong Kong Society of Accountants. He joined the Group as a director in February 1997.

REPORT OF THE DIRECTORS

Biographical details of directors and senior management (continued)

Senior management

Mr. Au Hung, aged 43, is the general manager of the Group's factory in the People's Republic of China ("PRC"). He has more than 20 years' experience in the leather and fur industries and has an in-depth knowledge of the manufacture, distribution and trading of leather and fur products in the PRC market. He joined the Group in October 1975.

Mr. Chan Ching Kwan, aged 46, is the manager of the Group's factory in the PRC. He joined the Group in March 1988 and has more than 20 years' experience in the production of leather garments. He is responsible for the Group's manufacturing operations of leather garments.

Mr. Choi Hing Yee, aged 40, is the sales manager of the Group in the PRC. He joined the Group in August 1991 as a supervisor for the manufacturing operations of fur garments and was promoted to his current position in July 1993. He has over 20 years' experience in the marketing of fur and leather products.

Mr. Chu Yee On, Ian, aged 46, is the assistant general manager of the Group. He joined the Group in October 1989 and has been engaged in the manufacture and distribution of fur garments for over 20 years. He is responsible for the overall manufacturing and sales operations of the Group's fur garments.

Major customers and suppliers

In the year under review, sales to the Group's five largest customers accounted for approximately 37% of the total sales for the year and sales to the largest customer included therein amounted to approximately 13%.

The purchases attributable to the Group's five largest suppliers accounted for approximately 38% of the total purchases for the year and purchases from the largest supplier included therein amounted to approximately 12%.

Neither the directors, their associates, nor those shareholders of the Company which to the knowledge of the directors own more than 5% of the Company's share capital had any interest in the five largest customers and suppliers.

Distributable reserves

At the balance sheet date, the Company's reserves available for cash distribution and/or distribution in specie amounted to HK\$106,439,000.

Purchase, redemption or sale of listed securities

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

REPORT OF THE DIRECTORS

Code of Best Practice

In the opinion of the directors, the Company has complied with the Code of Best Practice as set out in Appendix 14 of the Listing Rules throughout the accounting period covered by the annual report except that the non-executive directors of the Company are not appointed for specific terms but are subject to retirement by rotation and re-election at the annual general meeting of the Company in accordance with the Company's bye-laws.

Auditors

Ernst & Young retire and a resolution for their reappointment as auditors of the Company will be proposed at the forthcoming annual general meeting.

ON BEHALF OF THE BOARD

Char On Man

Chairman and Managing Director

Hong Kong
20 August 1998

REPORT OF THE AUDITORS



安永會計師事務所

To the members

Peking Apparel International Group Limited

(Incorporated in Bermuda with limited liability)

We have audited the financial statements on pages 20 to 40 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

Respective responsibilities of directors and auditors

The Company's directors are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes an examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's and the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion the financial statements give a true and fair view, in all material respects, of the state of affairs of the Company and of the Group as at 31 March 1998 and of the loss and cash flows of the Group for the year then ended and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Ernst & Young

Certified Public Accountants

Hong Kong

20 August 1998

CONSOLIDATED PROFIT AND LOSS ACCOUNT

Year ended 31 March 1998

	Notes	1998 HK\$'000	1997 HK\$'000
TURNOVER	2	<u>200,597</u>	<u>312,714</u>
OPERATING PROFIT/(LOSS) BEFORE EXCEPTIONAL ITEM	3	(6,406)	38,068
Exceptional item	6	<u>—</u>	<u>5,163</u>
PROFIT/(LOSS) BEFORE TAXATION		(6,406)	43,231
Taxation	7	<u>161</u>	<u>(2,753)</u>
NET PROFIT/(LOSS) ATTRIBUTABLE TO SHAREHOLDERS	8	(6,245)	40,478
Retained profits at beginning of year		<u>89,838</u>	<u>74,560</u>
		83,593	115,038
Dividends	9	<u>—</u>	<u>(25,200)</u>
RETAINED PROFITS AT END OF YEAR		<u>83,593</u>	<u>89,838</u>
EARNINGS/(LOSS) PER SHARE	10	<u>(2.4) cents</u>	<u>20.4 cents</u>

CONSOLIDATED BALANCE SHEET

31 March 1998

	Notes	1998 HK\$'000	1997 HK\$'000
FIXED ASSETS	11	44,560	45,394
LONG TERM INVESTMENTS	12	3,364	3,364
CURRENT ASSETS	14	178,788	186,441
CURRENT LIABILITIES	17	(62,733)	(68,271)
NET CURRENT ASSETS		<u>116,055</u>	<u>118,170</u>
TOTAL ASSETS LESS CURRENT LIABILITIES		163,979	166,928
DEFERRED TAXATION	18	(72)	(300)
		<u>163,907</u>	<u>166,628</u>
SHARE CAPITAL	19	26,704	25,900
RESERVES	20	53,610	50,890
RETAINED PROFITS		<u>83,593</u>	<u>89,838</u>
		<u>163,907</u>	<u>166,628</u>

Char On Man
Director

Li Wing Tak
Director

CONSOLIDATED CASH FLOW STATEMENT

Year ended 31 March 1998

	Note	1998 HK\$'000	1997 HK\$'000
NET CASH INFLOW/(OUTFLOW) FROM OPERATING ACTIVITIES	21(a)	<u>9,698</u>	<u>(3,321)</u>
RETURNS ON INVESTMENTS AND SERVICING OF FINANCE			
Interest received		2,547	601
Interest paid		(4,656)	(5,520)
Dividends received from long term unlisted investments		873	490
Dividends paid		<u>—</u>	<u>(31,200)</u>
Net cash outflow from returns on investments and servicing of finance		<u>(1,236)</u>	<u>(35,629)</u>
TAXATION			
Hong Kong profits tax refunded/(paid)		(328)	41
Overseas tax paid		<u>(22)</u>	<u>(55)</u>
Taxes paid		<u>(350)</u>	<u>(14)</u>
INVESTING ACTIVITIES			
Purchases of fixed assets		(7,725)	(1,229)
Proceeds from disposal of fixed assets		20	2
Proceeds from disposal of a long term investment		—	1,217
Increase in pledged time deposits		<u>(1,931)</u>	<u>(32,471)</u>
Net cash outflow from investing activities		<u>(9,636)</u>	<u>(32,481)</u>
NET CASH OUTFLOW BEFORE FINANCING ACTIVITIES		(1,524)	(71,445)

CONSOLIDATED CASH FLOW STATEMENT

Year ended 31 March 1998

	Note	1998 HK\$'000	1997 HK\$'000
FINANCING ACTIVITIES	21(b)		
Repayment of bank loans		—	(10,806)
Issue of new shares		8,836	64,753
Share issue expenses		—	(11,432)
Interest received on application monies from new issue of shares		—	5,163
Net cash inflow from financing activities		<u>8,836</u>	<u>47,678</u>
INCREASE / (DECREASE) IN CASH AND CASH EQUIVALENTS		7,312	(23,767)
Cash and cash equivalents at beginning of year		(22,650)	1,115
Foreign exchange adjustment		—	2
CASH AND CASH EQUIVALENTS AT END OF YEAR		<u>(15,338)</u>	<u>(22,650)</u>
ANALYSIS OF THE BALANCES OF CASH AND CASH EQUIVALENTS			
Cash and bank balances		2,924	685
Bank overdrafts		(20,142)	(25,096)
Time deposits		1,880	1,761
		<u>(15,338)</u>	<u>(22,650)</u>

BALANCE SHEET

31 March 1998

	Notes	1998 HK\$'000	1997 HK\$'000
INTERESTS IN SUBSIDIARIES	13	170,611	164,125
CURRENT ASSETS			
Bank balance		8	3
CURRENT LIABILITIES			
Accrued expenses		<u>(80)</u>	<u>(1,395)</u>
NET CURRENT LIABILITIES		<u>(72)</u>	<u>(1,392)</u>
		<u>170,539</u>	<u>162,733</u>
SHAREHOLDERS' EQUITY			
Share capital	19	26,704	25,900
Reserves	20	139,709	131,677
Retained profits		<u>4,126</u>	<u>5,156</u>
		<u>170,539</u>	<u>162,733</u>

Char On Man
Director

Li Wing Tak
Director

NOTES TO FINANCIAL STATEMENTS

31 March 1998

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of accounting

These financial statements have been prepared in accordance with Hong Kong Statements of Standard Accounting Practice and the disclosure requirements of the Hong Kong Companies Ordinance.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended 31 March 1998. The results of subsidiaries acquired or disposed of during the year are consolidated from or to their effective dates of acquisition or disposal, respectively. All significant intercompany transactions and balances within the Group are eliminated on consolidation.

Subsidiaries

A subsidiary is a company in which the Company, directly or indirectly, controls more than half of its voting power or issued share capital or controls the composition of its board of directors. Interests in subsidiaries are stated at cost unless, in the opinion of the directors, there have been permanent diminutions in value, when they are written down to values determined by the directors.

Fixed assets and depreciation

Fixed assets are stated at cost or valuation less accumulated depreciation. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to working condition and location for its intended use. Expenditure incurred after the fixed assets have been put into operation, such as repairs and maintenance, is normally charged to the profit and loss account in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of the fixed asset, the expenditure is capitalised as an additional cost of the fixed asset.

For assets stated at valuation, changes in the values of fixed assets are dealt with as movements in the revaluation reserve. If the reserve is insufficient to cover a deficit, on an individual asset basis, the excess of the deficit is charged to the profit and loss account. A subsequent revaluation increase is recognised as income to the extent that it reverses a revaluation deficit of the same asset previously charged to the profit and loss account.

The gain or loss on disposal or retirement of a fixed asset recognised in the profit and loss account is the difference between the proceeds on disposition and the carrying amount of the relevant asset. The relevant portion of the fixed asset revaluation reserve realised in respect of the previous valuations is transferred to retained profits as a movement in reserves.

NOTES TO FINANCIAL STATEMENTS

31 March 1998

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fixed assets and depreciation (continued)

Depreciation is calculated on the straight-line basis to write off the cost or valuation less estimated residual value of each asset over its estimated useful life. The principal annual rates used for this purpose are as follows:

Leasehold land	Over the lease terms
Buildings	2% – 4.5%
Leasehold improvements	20%
Plant and machinery	9% – 20%
Furniture and equipment	10%
Motor vehicles and vessels	20%

Long term investments

Investments held on a long term basis are stated at cost less provisions for any permanent diminutions in values deemed necessary by the directors, on an individual investment basis.

Stocks

Stocks are stated at the lower of cost and net realisable value, after making due allowance for any obsolete or slow-moving items. Cost is determined on a specific item basis and, in the case of finished goods, comprises direct materials, direct labour and an appropriate proportion of overheads. Net realisable value is based on estimated selling price less any further costs expected to be incurred to completion and disposal.

Deferred taxation

Deferred taxation is provided, using the liability method, on all significant timing differences to the extent it is probable that the liability will crystallise in the foreseeable future. A deferred tax asset is not recognised until its realisation is assured beyond reasonable doubt.

Cash equivalents

Cash equivalents represent short term highly liquid investments which are readily convertible into known amounts of cash and which were within three months of maturity when acquired, less advances from banks repayable within three months from the date of the advance.

Operating leases

Leases where substantially all the rewards and risks of ownership of assets remain with the leasing company are accounted for as operating leases. Rentals applicable to such operating leases are charged or credited to the profit and loss account on the straight-line basis over the lease terms.



NOTES TO FINANCIAL STATEMENTS

31 March 1998

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Revenue

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

- (a) on the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;
- (b) interest income, on a time proportion basis taking into account the principal outstanding and the effective rate of interest applicable;
- (c) rental income, in the period in which the properties are let and on the straight-line basis over the lease terms; and
- (d) dividends, when the shareholders' right to receive payment is established.

Foreign currencies

Foreign currency transactions are recorded at the applicable rates of exchange ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the applicable rates of exchange ruling at that date. Exchange differences are dealt with in the profit and loss account.

On consolidation, the financial statements of overseas subsidiaries are translated into Hong Kong dollars at the applicable rates of exchange ruling at the balance sheet date. The resulting translation differences are included in the exchange fluctuation reserve.

2. TURNOVER AND REVENUE

Turnover represents revenue from the net invoiced value of goods sold, after allowances for goods returned and trade discounts, but excludes intra-group transactions. Revenue from other activities has been disclosed in note 3 to the financial statements.

NOTES TO FINANCIAL STATEMENTS

31 March 1998

3. OPERATING PROFIT/(LOSS) BEFORE EXCEPTIONAL ITEM

The operating profit/(loss) before exceptional item is arrived at after charging/(crediting):

	Group	
	1998	1997
	HK\$'000	HK\$'000
Depreciation	2,270	1,756
Auditors' remuneration	754	735
Interest on bank loans, overdrafts and trust receipt loans	4,656	5,520
Rent of land and buildings under operating leases	675	601
Loss on disposal of fixed assets	10	4
Foreign exchange losses, net	351	694
Revaluation deficit on fixed assets	947	—
Rental income, net of outgoings	(138)	(129)
Dividend income from long term unlisted investments	(873)	(490)
Bank interest income	(2,547)	(601)

4. DIRECTORS' REMUNERATION

	Executive		Independent non-executive	
	1998	1997	1998	1997
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Fees	—	—	—	—
Salaries, allowances and benefits in kind	3,575	1,985	—	—
Bonuses paid and payable	—	1,872	—	—
	<u>3,575</u>	<u>3,857</u>	<u>—</u>	<u>—</u>

The remuneration of the above directors fell within the following bands:

	Number of directors	
	1998	1997
Nil – HK\$1,000,000	6	5
HK\$1,000,001 – HK\$1,500,000	—	2
HK\$1,500,001 – HK\$2,000,000	1	—

There was no arrangement under which a director waived or agreed to waive any remuneration during the year.

NOTES TO FINANCIAL STATEMENTS

31 March 1998

5. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the year included three (1997: four) directors, details of whose remuneration are set out in note 4 above. The details of the remuneration of the remaining two (1997: one) non-director, highest paid employees are set out below:

	Group	
	1998	1997
	HK\$'000	HK\$'000
Salaries, allowances and benefits in kind	580	298
Bonuses paid and payable	3	12
	<u>583</u>	<u>310</u>

The remuneration of the non-director, highest paid employees fell within the following band:

	Number of individuals	
	1998	1997
Nil – HK\$1,000,000	<u>2</u>	<u>1</u>

6. EXCEPTIONAL ITEM

The prior year's amount represented bank interest received on application monies from the new issue of shares.

7. TAXATION

	Group	
	1998	1997
	HK\$'000	HK\$'000
Provisions for taxation in respect of profit for the year:		
Hong Kong	–	(2,698)
Elsewhere	(67)	(46)
Prior year's underprovision	–	(9)
Deferred taxation (note 18)	<u>228</u>	<u>–</u>
Taxation credit/(charge) for the year	<u>161</u>	<u>(2,753)</u>

NOTES TO FINANCIAL STATEMENTS

31 March 1998

7. TAXATION (continued)

No provision for Hong Kong taxation has been made as no assessable profits were earned in or derived from Hong Kong during the year. Prior year's Hong Kong profits tax has been provided at the rate of 16.5% on the estimated assessable profits arising in Hong Kong.

Taxes on profits assessable elsewhere have been calculated at the rates of taxation prevailing in the countries in which the Group operates based on existing legislation, practices and interpretations in respect thereof.

8. NET PROFIT/(LOSS) ATTRIBUTABLE TO SHAREHOLDERS

The net loss attributable to shareholders dealt with in the financial statements of the Company is HK\$1,030,000 (1997: net profit of HK\$5,156,000).

9. DIVIDENDS

	1998 HK\$'000	1997 HK\$'000
Special dividends	—	12,000
Interim dividends	—	13,200
	<u>—</u>	<u>25,200</u>

The prior year's dividends were paid by a subsidiary of the Company to its then shareholders prior to the Group reorganisation and the listing of the Company's shares on The Stock Exchange of Hong Kong Limited.

10. EARNINGS/(LOSS) PER SHARE

The calculation of earnings/(loss) per share is based on the net loss attributable to shareholders of HK\$6,245,000 (1997: net profit of HK\$40,478,000) and the weighted average of 264,699,300 (1997: 198,685,000) shares in issue during the year.

NOTES TO FINANCIAL STATEMENTS

31 March 1998

11. FIXED ASSETS

Group

	1997	Additions	Disposals	Revaluation deficit	1998
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At valuation:					
Leasehold land and buildings	41,200	4,497	—	(7,347)	38,350
At cost:					
Leasehold improvements	989	1,860	(150)	—	2,699
Plant and machinery	4,265	1,061	—	—	5,326
Furniture and equipment	1,707	259	(48)	—	1,918
Motor vehicles and vessels	3,641	48	(33)	—	3,656
	<u>51,802</u>	<u>7,725</u>	<u>(231)</u>	<u>(7,347)</u>	<u>51,949</u>
Accumulated depreciation:					
Leasehold land and buildings	—	1,088	—	(1,088)	—
Leasehold improvements	399	365	(150)	—	614
Plant and machinery	1,767	471	—	—	2,238
Furniture and equipment	1,007	175	(18)	—	1,164
Motor vehicles and vessels	3,235	171	(33)	—	3,373
	<u>6,408</u>	<u>2,270</u>	<u>(201)</u>	<u>(1,088)</u>	<u>7,389</u>
Net book value	<u>45,394</u>				<u>44,560</u>

Leasehold land and buildings with a carrying value of HK\$11,300,000 (1997: HK\$17,116,000) were pledged to secure general banking facilities granted to the Group.

NOTES TO FINANCIAL STATEMENTS

31 March 1998

11. FIXED ASSETS (continued)

The analysis of the leasehold land and buildings at the balance sheet date is as follows:

	Group	
	1998	1997
	HK\$'000	HK\$'000
Long term leasehold land and buildings situated in Hong Kong	—	18,300
Medium term leasehold land and buildings situated in:		
People's Republic of China:		
Hong Kong	12,100	—
Elsewhere	26,250	22,900
At valuation	<u>38,350</u>	<u>41,200</u>

A revaluation of the leasehold land and buildings was carried out by First Pacific Davies (Hong Kong) Limited, an independent firm of professional valuers, on an open market value, existing use basis as at 31 March 1998. Had the land and buildings not been revalued, their net book values at 31 March 1998 would have been HK\$23,101,000 (1997: HK\$19,223,000), being cost of HK\$26,555,000 (1997: HK\$22,058,000) less accumulated depreciation of HK\$3,454,000 (1997: HK\$2,835,000).

12. LONG TERM INVESTMENTS

	Group	
	1998	1997
	HK\$'000	HK\$'000
Unlisted investments, at cost	<u>3,364</u>	<u>3,364</u>

13. INTERESTS IN SUBSIDIARIES

	Company	
	1998	1997
	HK\$'000	HK\$'000
Unlisted shares, at cost	104,256	104,256
Amount due from a subsidiary	66,355	59,869
	<u>170,611</u>	<u>164,125</u>

NOTES TO FINANCIAL STATEMENTS

31 March 1998

13. INTERESTS IN SUBSIDIARIES (continued)

Details of the subsidiaries, all of which are wholly-owned, are as follows:

Name of company	Place of incorporation/ registration and operations @	Issued and paid-up share/ registered capital	Principal activities
Peking Fur and Leather Limited	British Virgin Islands	Ordinary US\$1,000	Investment holding
Peking Fur Factory (Hong Kong) Limited	Hong Kong	Ordinary HK\$200 Deferred HK\$1,200,000#	Design and sale of leather garments, fur garments and microfibre garments and the trading of tanned leather and fur pelts
Peking Leather Factory Limited	Hong Kong	Ordinary HK\$100,000	Dormant
K And K Fur Creation Limited	Hong Kong	Ordinary HK\$200,000	Trading of tanned leather and fur pelts
Shen Zhen Gangjing Fur & Leather Factory Ltd.	People's Republic of China	RMB2,700,000	Design, manufacture and sale of leather garments and fur garments
Jiayi Fashion (Shenzhen) Co., Ltd.	People's Republic of China	HK\$2,000,000	Manufacture and sale of leather garments
J & S International Equities Holdings Ltd.	British Virgin Islands/ People's Republic of China	Ordinary US\$1	Provision of agency services
Lagocircle Limited	British Virgin Islands/ People's Republic of China	Ordinary US\$1	Provision of agency services

NOTES TO FINANCIAL STATEMENTS

31 March 1998

13. INTERESTS IN SUBSIDIARIES (continued)

@ Unless otherwise stated, the place of operations is the place of incorporation or registration.

The non-voting deferred shares practically carry no rights to dividends, to receive notice of or to attend or vote at any general meeting of the company or to participate in any distribution on winding up.

All subsidiaries are indirectly held by the Company with the exception of Peking Fur and Leather Limited.

14. CURRENT ASSETS

		Group	
		1998	1997
	Notes	HK\$'000	HK\$'000
Cash and bank balances		2,924	685
Time deposits	15	40,061	38,011
Bills receivable		—	302
Trade debtors		15,128	39,478
Stocks	16	111,100	103,742
Other debtors, prepayments and deposits		9,575	4,223
		<u>178,788</u>	<u>186,441</u>

15. TIME DEPOSITS

Time deposits of HK\$38,181,000 (1997: HK\$36,250,000) were pledged to secure general banking facilities granted to the Group.

16. STOCKS

		Group	
		1998	1997
		HK\$'000	HK\$'000
Raw materials		83,975	85,539
Finished goods		27,125	18,203
		<u>111,100</u>	<u>103,742</u>

NOTES TO FINANCIAL STATEMENTS

31 March 1998

17. CURRENT LIABILITIES

	Group	
	1998	1997
	HK\$'000	HK\$'000
Bank overdrafts, secured	20,142	25,096
Trust receipt loans, secured	25,139	25,419
Trade creditors and accrued expenses	13,367	13,388
Taxation	4,085	4,368
	<u>62,733</u>	<u>68,271</u>

18. DEFERRED TAXATION

	Group	
	1998	1997
	HK\$'000	HK\$'000
At beginning of year	300	300
Credit for the year (note 7)	(228)	—
At end of year	<u>72</u>	<u>300</u>

The provision for deferred taxation relates wholly to timing differences arising from accelerated capital allowances. There were no other material potential deferred tax liabilities for which provision has not been made.

The revaluation of the Group's leasehold land and buildings does not constitute a timing difference and, consequently, the amount of potential deferred tax thereon has not been quantified.

NOTES TO FINANCIAL STATEMENTS

31 March 1998

19. SHARE CAPITAL

Shares

	1998 HK\$'000	1997 HK\$'000
Authorised:		
1,000,000,000 ordinary shares of HK\$0.10 each	<u>100,000</u>	<u>100,000</u>
Issued and fully paid:		
267,035,700 (1997: 259,002,900) ordinary shares of HK\$0.10 each	<u>26,704</u>	<u>25,900</u>

During the year, 8,032,800 warrants were exercised at the subscription price of HK\$1.10 per share, resulting in the issue of 8,032,800 ordinary shares of HK\$0.10 each for a total cash consideration of HK\$8,836,080.

Warrants

At the beginning of the year, the Company had 51,797,100 outstanding warrants, each entitling the holders to subscribe in cash for one ordinary share of HK\$0.10 each in the Company at an exercise price of HK\$1.10 per share (subject to adjustment) at any time between 7 March 1997 to 31 March 1999, both dates inclusive. During the year, 8,032,800 ordinary shares of HK\$0.10 each were issued on exercise of the warrant subscription rights.

At 31 March 1998, 43,764,300 warrants remained unexercised. The exercise in full of all outstanding warrants would, under the present capital structure of the Company, result in the issue of 43,764,300 new ordinary shares of HK\$0.10 each for cash proceeds of HK\$48,140,730, before related issue expenses.

Share options

On 18 February 1997, the Company adopted a share option scheme under which the directors may, at their discretion, invite any employees or executive directors of the Group to take up options to subscribe for ordinary shares of HK\$0.10 each in the Company. The maximum number of shares in respect of which options may be granted under the scheme may not exceed 10% of the issued share capital of the Company.

No share options had been granted during the year and there was no share option outstanding at the balance sheet date.

NOTES TO FINANCIAL STATEMENTS

31 March 1998

20. RESERVES

Group

	Share premium account HK\$'000	Fixed asset revaluation reserve HK\$'000	Reserve fund HK\$'000	Exchange fluctuation reserve HK\$'000	Total HK\$'000
At beginning of year	29,364	21,977	173	(624)	50,890
Issue of new shares	8,032	—	—	—	8,032
Revaluation deficit	—	(5,312)	—	—	(5,312)
At end of year	<u>37,396</u>	<u>16,665</u>	<u>173</u>	<u>(624)</u>	<u>53,610</u>

Company

	Share premium account HK\$'000	Contributed surplus HK\$'000	Total HK\$'000
At beginning of year	29,364	102,313	131,677
Issue of new shares	8,032	—	8,032
At end of year	<u>37,396</u>	<u>102,313</u>	<u>139,709</u>

The contributed surplus of the Company represents the difference between the nominal value of the Company's shares issued in exchange for the issued share capital of the subsidiaries and the net asset value of the subsidiaries acquired. Under the Companies Act 1981 of Bermuda (as amended), the contributed surplus is distributable to shareholders under certain circumstances.

NOTES TO FINANCIAL STATEMENTS

31 March 1998

21. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

(a) Reconciliation of operating profit/(loss) before exceptional item to net cash inflow/(outflow) from operating activities

	Group	
	1998	1997
	HK\$'000	HK\$'000
Operating profit/(loss) before exceptional item	(6,406)	38,068
Interest income	(2,547)	(601)
Interest expenses	4,656	5,520
Depreciation	2,270	1,756
Dividend income from long term unlisted investments	(873)	(490)
Revaluation deficit on fixed assets	947	—
Loss on disposal of fixed assets	10	4
Decrease in bills receivable	302	755
Decrease/(increase) in trade debtors	24,350	(28,578)
Increase in stocks	(7,358)	(28,222)
Increase in other debtors, prepayments and deposits	(5,352)	(2,735)
Decrease in amount due from a director	—	3,281
Increase/(decrease) in trust receipt loans	(280)	17,414
Decrease in trade creditors and accrued expenses	(21)	(9,493)
Net cash inflow/(outflow) from operating activities	<u>9,698</u>	<u>(3,321)</u>

NOTES TO FINANCIAL STATEMENTS

31 March 1998

21. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (continued)

(b) Analysis of changes in financing during the year

	Share capital and share premium account HK\$'000	Bank loans HK\$'000
Balance at 1 April 1996	1,943	10,746
Exchange realignment	—	60
Cash inflow/(outflow) from financing activities, net	53,321	(10,806)
Balance at 31 March 1997 and 1 April 1997	55,264	—
Cash inflow from financing activities, net	8,836	—
Balance at 31 March 1998	64,100	—

22. CONTINGENT LIABILITIES

At the balance sheet date, the Group and the Company had the following contingent liabilities:

- (a) Certain of the Group's employees have completed the required number of years of service under the Employment Ordinance to be eligible for long service payments on termination of their employment. The Group is only liable to make such payments where the termination meets the required circumstances specified in the Employment Ordinance. If the termination of all these employees met the circumstances required by Employment Ordinance, the Group's liability at 31 March 1998 which has not been provided for in the financial statements would be approximately HK\$1,325,000 (1997: HK\$1,653,000).
- (b) The Company had guarantees amounting to HK\$110,560,000 (1997: HK\$12,000,000) given to banks for facilities granted to a subsidiary, of which HK\$45,281,000 (1997: HK\$8,412,000) was utilised by the subsidiary at the balance sheet date.

NOTES TO FINANCIAL STATEMENTS

31 March 1998

23. COMMITMENTS

Annual commitments under non-cancellable operating leases in respect of land and buildings payable during the forthcoming year were as follows:

	Group	
	1998	1997
	HK\$'000	HK\$'000
Leases expiring within one year	96	496
Capital commitments contracted for	100	—

At the balance sheet date, the Company did not have any material commitments.

24. COMPARATIVE AMOUNTS

Certain comparative amounts have been reclassified to conform with the current year presentation.

25. ULTIMATE HOLDING COMPANY

In the opinion of the directors, the ultimate holding company is Wellglow Investments Limited, which is incorporated in the British Virgin Islands.

26. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved by the board of directors on 20 August 1998.