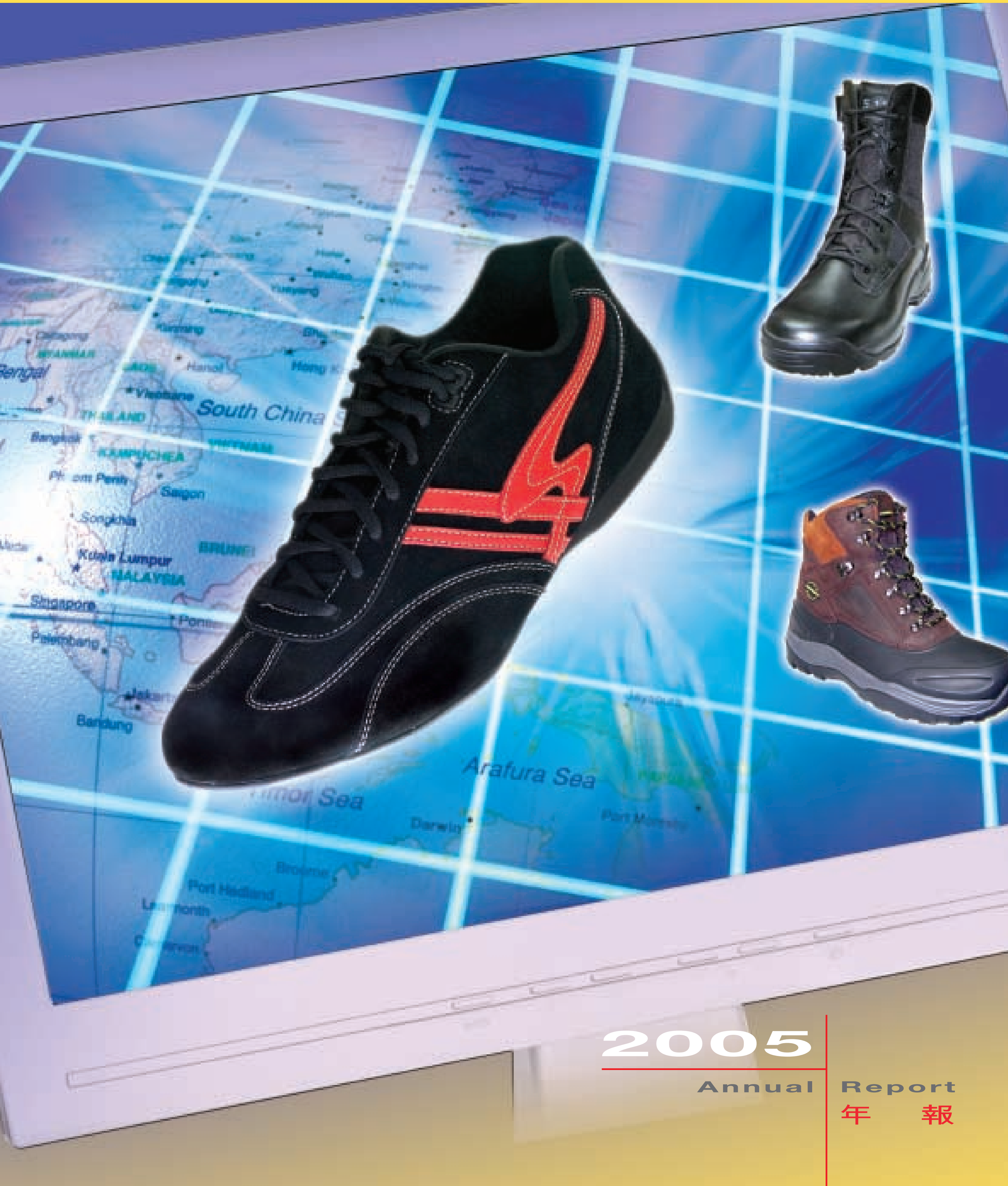
PEGASUS INTERNATIONAL HOLDINGS LIMITED
創 信 國 際 控 股 有 限 公 司

(Incorporated in Bermuda with limited liability)
(於百慕達註冊成立之有限公司)

(股份代號 Stock Code：676)



2005

Annual Report
年 報

Contents

Corporate Information

DIRECTORS

EXECUTIVE DIRECTORS

Wu Chen San, Thomas , *Chairman*
Wu Jenn Chang, Michael , *Deputy Chairman*
Wu Jenn Tzong, Jackson
Yang Chih Chieh, Arthur
Ho Chin Fa, Steven

NON-EXECUTIVE DIRECTORS

Fang Yen Ling
Liu Chung Kang, Helios
Lai Jenn Yang, Jeffrey

COMPANY SECRETARY

Lee Yiu Ming

AUDIT COMMITTEE

Fang Yen Ling, *Chairman*
Liu Chung Kang, Helios
Lai Jenn Yang, Jeffrey

REMUNERATION COMMITTEE

Lai Jenn Yang, Jeffrey, *Chairman*
Fang Yen Ling
Liu Chung Kang, Helios

NOMINATION COMMITTEE

Liu Chung Kang, Helios, *Chairman*
Lai Jenn Yang, Jeffrey
Fang Yen Ling

REGISTERED OFFICE

Clarendon House
2 Church Street
Hamilton HM11
Bermuda

HEAD OFFICE AND PRINCIPAL PLACE OF BUSINESS

Room 1517, Tower 3
China Hong Kong City
33 Canton Road
Tsimshatsui
Kowloon
Hong Kong

AUDITORS

Deloitte Touche Tohmatsu
26th Floor
Wing On Centre
111 Connaught Road Central
Hong Kong

PRINCIPAL SHARE REGISTRARS

Butterfield Corporate Services Limited
Rosebank Centre
11 Bermudiana Road
Pembroke
Bermuda

HONG KONG BRANCH SHARE REGISTRARS

Secretaries Limited
26/F, Tesbury Centre,
28 Queen's Road East,
Hong Kong

Stock Code

676

PRINCIPAL BANKERS

Bank of East Asia, Limited
Bank of Tokyo-Mitsubisui UFJ
BNP Paribas
China Construction Bank
Chinatrust Commercial Bank, Ltd
DBS Bank (Hong Kong) Limited
Hang Seng Bank Limited
Natexis Banques Populaires
Rabobank
Standard Chartered Bank
The Hong Kong and Shanghai Banking Corporation Limited

PEGASUS INTERNATIONAL

Notice of Annual General Meeting

NOTICE IS HEREBY GIVEN that the Annual General Meeting of the Company will be held at Imperial Room III, Towers Wing, Mezzanine Floor, The Royal Pacific Hotel & Towers, China Hong Kong City, 33 Canton Road, Tsimshatsui, Kowloon, Hong Kong on Wednesday, 17th May, 2006 at 9:30 a.m. for the following purposes:

1. To receive and consider the audited financial statements and the directors' report and auditors' report for the year ended 31st December, 2005.

2. To approve and declare a final dividend for the year ended 31st December, 2005.

3. To re-elect retiring Directors and authorise the Board of Directors to fix their remuneration.

4. To re-appoint the Auditors and authorise the Board of Directors to fix their remuneration.

As special business

5. To consider and, if thought fit, to pass, with or without modifications, the following Resolutions as ordinary resolutions:

(A) "**THAT**:

(a) subject to paragraph (b) below, the exercise by the Directors of the Company during the Relevant Period (as hereinafter defined) of all the powers of the Company to purchase shares in the capital of the Company, subject to and in accordance with all applicable laws and the requirements of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited as amended from time to time, be and is hereby generally and unconditionally approved;

(b) the aggregate nominal amount of shares of the Company which may be purchased by the Company pursuant to the approval in paragraph (a) above shall not exceed 10 per cent. of the aggregate nominal amount of the share capital of the Company in issue as at the date of passing of this Resolution, 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 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 law to be held; and

(iii) the revocation or variation of authority given under this Resolution by an ordinary resolution of the shareholders of the Company in general meeting."

(B) "**THAT**:

(a) subject to paragraph (c) below, the exercise by the Directors of the Company during the Relevant Period (as hereinafter defined) of all the powers of the Company to allot, issue and deal with additional shares in the capital of the Company and to make or grant offers, agreements and options which would or might require the exercise of such powers, be and is hereby generally and unconditionally approved;

(b) the approval in paragraph (a) above shall authorise the Directors of the Company during the Relevant Period to make or grant offers, agreements and options which would or might require the exercise of such powers after the end of the Relevant Period;

(c) the aggregate nominal amount of the share capital allotted or agreed conditionally or unconditionally to be allotted (whether pursuant to an option or otherwise) by the Directors of the Company pursuant to the approval in paragraph (a) above, otherwise than pursuant to (1) a Rights

Issue (as hereinafter defined); (2) an issue of shares as scrip dividends pursuant to the Bye-laws of the Company; (3) an issue of shares by the exercise of options granted under the share option scheme of the Company, shall not exceed 20 per cent. of the aggregate nominal amount of the share capital of the Company in issue as at the date of passing of this Resolution, and the said approval shall be limited accordingly; and

(d) 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 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 law to be held; and

(iii) the revocation or variation of authority given under this Resolution by an ordinary resolution of the shareholders of the Company in general meeting; and

"Rights Issue" means an offer of shares open for a period fixed by the Directors of the Company to the holders of shares of the Company on the register on a fixed record date in proportion to their then holdings of such shares (subject to such exclusion or other arrangements as the Directors of the Company may deem necessary or expedient in relation to fractional entitlements or having regard to any restrictions or obligations under the laws of, or the requirements of any recognised regulatory body or any stock exchange, in any territory outside Hong Kong applicable to the Company)."

(C) "**THAT** conditional upon the Resolutions numbered 5A and 5B set out in the notice convening this meeting being passed, the aggregate nominal amount of shares in the capital of the Company which is purchased by the Company under the authority granted to the Directors of the Company by Resolution numbered 5A (up to a maximum of 10 per cent. of the aggregate nominal amount of the share capital of the Company in issue as at the date of passing of such Resolution) shall be added to the aggregate nominal amount of shares in the capital of the Company that may be allotted or agreed conditionally or unconditionally to be allotted by the Directors of the Company pursuant to Resolution numbered 4B set out in the notice convening this meeting."

6. As special business, to consider and, if thought fit, to pass, with or without modification, the following resolution as special resolution:

SPECIAL RESOLUTION

"**THAT** the Bye-laws be amended as follows:

(A) By deleting the full-stop at the end of Bye-law 66(d) and replacing herewith a semi-colon and the word "or" immediately thereafter by inserting the following as new Bye-law 66(e):

"(e) by any Director or Directors (including the chairman of a general meeting of the Company) who, individually or collectively, hold proxies in respect of shares representing 5 per cent. or more of the total voting rights at such meeting and if on a show of hands such meeting votes in the opposite manner to that instructed in those proxies. If a poll is required under these circumstances, the chairman of the meeting should disclose to the meeting of the Company the total number of votes represented by all proxies held by Directors indicating an opposite vote to the votes cast at the meeting on a show of hands".

(B) By inserting a new Bye-law 66A as follows:

"66A The chairman should at the commencement of the meeting ensure that an explanation is provided of:

(a) the procedures for demanding a poll by Members before putting a resolution to the vote on a show of hands; and

(b) the detailed procedures for conducting a poll and then answer any questions from Member whenever voting by way of poll is required."

(C) By deleting Article 67 in its entirety and substituting therefor the following:

"67 Unless a poll is so required or demanded and, in the latter case, not withdrawn:

(i) the chairman of the meeting should indicate to the meeting of the Company the level of proxies lodged on each resolution and the balance for and against the resolution, after it has been dealt with on a show of hands. All proxy votes must be counted and recorded; and

(ii) a declaration by the chairman that a resolution has on a show of hands been carried, or carried unanimously, or by a particular majority, or lost, and an entry to that effect in the Company's book containing the minutes of proceedings of meetings of the Company shall be conclusive evidence of that fact without proof of the number or proportion of the votes recorded in favour of or against such resolution."

(D) By replacing the second sentence in Bye-law 68 in its entirety.

(E) By deleting the word "annual" before the words "general meeting" in the first sentence of Bye-law 86(2).

(F) By replacing the word "special" in Bye-law 86(4) by "ordinary" immediately after the word "by"."

(G) By replacing the words "the chairman of the Board and/or the managing director of the Company shall not, whilst holding such office, be subject to retirement by rotation or be taken into account in determining the number of Directors to retire in each year" in Bye-law 87(1) by the words "every Director shall be subject to retirement by rotation at least once every three years" immediately after the words "notwithstanding anything herein".

(H) By replacing the word "greater" in Bye-law 87(1) by the word "lesser" immediately after the words "nearest to but not".

(I) By inserting in the first sentence of Bye-law 87(2) immediately after the word "re-election" the words "and shall continue to act as a Director throughout the meeting at which he retires".

By Order of the Board
Lee Yiu Ming
Company Secretary

Hong Kong, 20th April, 2006

Notes:

(1) Any member entitled to attend and vote at the meeting is entitled to appoint one or more proxies to attend and, on a poll, vote in his stead. A proxy need not be a member of the Company.

(2) In order to be valid, a form of proxy together with the power of attorney or other authority (if any) under which it is signed or a notarially certified copy thereof must be deposited at the head office and principal place of business of the Company at Room 1517, Tower 3, China Hong Kong City, 33 Canton Road, Tsimshatsui, Kowloon, Hong Kong not less than 48 hours before the time appointed for holding the meeting or any adjournment thereof.

(3) An explanatory statement containing further details regarding the Resolutions set out in items 5 and 6 will be sent to the shareholders of the Company together with the annual report of the Company for the year ended 31st December, 2005.

PEGASUS INTERNATIONAL

Chairman's Statement

RESULTS

The Group's performance for 2005 is highlighted as follows:

- Turnover was US$141,242,000 (2004: US$143,704,000)
- Profit for the year US$2,467,000 (2004: loss for the year US$900,000)

During the year, the Group has rigidly controlled its quality and delivery of products, as well as cut down both administrative and sales costs, whilst gross profit still maintained at 16.5% amidst the rise of staff costs.

INDUSTRY REVIEW

Overall business was approximately the same as that of 2004, with neither obvious fall nor growth.

BUSINESS REVIEW

PRODUCT MIX

In 2005, the Group's product mix comprised sports scandals (13%), casual shoes (22%), athletic shoes (60%) and others (5%). The Group will strive to develop new products so as to further step forward for product diversification.

GEOGRAPHICAL MARKET SEGMENTS

North America remained the largest export market of the Group, accounting for 62% of its turnover for 2005. Turnover contribution from the European and Asian markets were 17% and 15% respectively.

DOMESTIC SALES IN THE PRC

The Group's domestic sales was approximately the same as that of 2004 and the number of sales outlets of Group in the PRC stood at around 120.

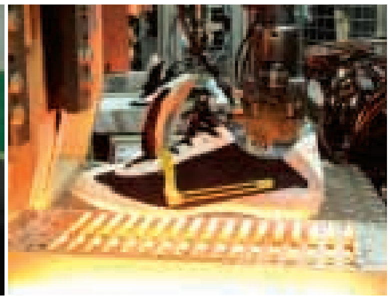
LEAN MANAGEMENT

To further strengthen its internal management, the Group implemented the concept of lean operation system with an emphasis on its production process and segmented management, with a view to enhance its administration and production efficacy. By the end of 2005, the Group increased the number of production lines based on the concept of lean operating system to 22. It is intended that the transformation of all traditional production lines will be completed by the end of October 2006. Through transformation of production lines and lean management of each production process, flow and segment, the overall efficacy has been greatly enhanced.

SOCIAL RESPONSBILITY

The Group has emphasized the physical and psychological needs of its staff. The Group has not only provided a better living and working environment than its competitors for its staff, but also






offered them with chances to learn and grow up through training and internal appraisal in order to attract and retain calibers and to actively manage the issue of the increasingly deficiency in workforce. In addition, the Group has particularly emphasized on the nurture of corporate culture, the establishment of learning-based organization as well as an efficient and harmonious team, thereby further strengthened the centripetal and cohesion within the Group.

OBJECTIVE AND RESULTS MANAGEMENT

During the year, the Group devoted to its objective and results management by setting objectives and defining responsibilities on group, departmental and individual basis and through assessment and incentives, aiming to enhance its overall operating results.

FUTURE PROSPECTS

According to the order placement in 2006, the Group expects the turnover from future exports to North American market will grow steadily. With the discrepancy in staff costs and the enhancement of the shoes production expertise in the PRC, European brands are increasingly tended to purchase shoes products from the PRC market. However, Europe's anti-dumping investigation has impeded the expansion of the Group's turnover from the European market. In light of the rapid and unpredictable market changes, continued rise in staff costs and unstable material prices, the shoes industry is still facing great challenges so that the Group has to maintain a prudent business operation by exploring more sources of income and adopting cost-saving measures. Moreover, the Group has to respond swiftly to the market in order to maintain a reasonable profit growth.

CONCLUSION

The Group is committed to enhance its competitiveness on product quality, efficiency, efficacy, delivery and speed and customer services, and to build up a higher standard within the industry by nurturing calibers, lean operating system and objective and results management, with a view to becoming the leading enterprise in the industry and realizing its objective of long-term development.

On behalf of the Board, I would like to express my deepest gratitude to the staff for their dedication and diligence, and our suppliers and customers for their continued support.

By Order of the Board
Wu Chen San, Thomas
CHAIRMAN

Hong Kong, 20th April, 2006

Management Discussion and Analysis

FINANCIAL REVIEW

The Group achieved a turnover of US$141,242,000 for the year ended 31 the December, 2005. Compared with 2004, the turnover decreased slightly by US$2,462,000 or 1.7%.

The Group's net profit attributable to shareholders in 2005 is US$2,467,000 which has turned from a net loss attributable to shareholders of US$900,000 in 2004. Due to the continued surge of labour cost, the operating environment in 2005 was challenging, which is reflected by the slight decrease in gross profit margin (16.5% in 2005 compared to 17.4% in 2004). Despite the fact, the Group had exercised very tight cost control and had successfully reduced much of the distribution and administrative expenses in 2005.

The basic earnings per share in 2005 is 0.34 US cent, compared to -0.12 US cent in 2004. The Group's net asset value increased mildly from 13 US cent per share in last year to 14 US cent per share in this year.

The Board proposes a final dividend of Hong Kong 1 cent per ordinary share for the year ended 31st December, 2005. Subject to approval at the forthcoming annual general meeting by shareholders, the final dividend will be paid to shareholders whose names appear on the Register of Members on 17th May, 2006.

LIQUIDITY AND FINANCIAL RESOURCES

The Group generally finances its business needs with internal cash flows. Total assets as at 31st December, 2005 amounted to US$146,089,000, 2.7% or US$3,843,000 higher than 2004. The Group's shareholders' funds increased by 3.7% or US$3,657,000 to US$102,086,000. The ratio of net bank borrowings to shareholders' funds remained at a healthy level of approximately 16.9%. As at 31st December, 2005, the Group had a strong financial liquidity position as revealed by a current ratio of 2.6 times. There was no charge on the fixed assets of the Group.

CAPITAL EXPENDITURE

During the year, the Group invested US$4,346,000 in fixed assets, of which 64% was used for the purchase of new plant and machinery.

Corporate Governance Report

The Company is committed to adopting the high standards of corporate governance. The board of directors of the Company believes that good governance is essential to achieving the Group's objectives of maximizing shareholders' value and safeguarding the interests of the shareholders.

In November, 2004, The Stock Exchange of Hong Kong Limited (the "Stock Exchange") promulgated the Code on Corporate Governance Practices (the "Code"), which became effective on 1st January, 2005. The Code provides the code provisions and recommended best practices for corporate governance.

During the financial year ended 31st December, 2005, the Company complied with all requirements set out in the Code contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"), with deviation from Code provision A.4.1, A.4.2 and B.1.1 in respect of the independent non-executive directors should be appointed under a specific terms, the rotation of directors and setting up of a Remuneration Committee with specific terms, respectively. Relevant amendment to the Bye-Laws of the Company to comply with Code provision A.4.2 will be proposed and approved by shareholders of the Company at the forthcoming annual general meeting of the Company to be held in May 2006. A service contract was signed with each of the independent non-executive directors with specific terms in early 2006. Remuneration Committee was set up in early 2006 with specific written terms of reference.

PEGASUS INTERNATIONAL

A. DIRECTORS

A.1 THE BOARD

The Board has the collective responsibility for leadership and control of, and for promoting the success of, the Company by directing and supervising the Company's affairs. The Board sets strategies for the Company and monitors the performance of the management.

During the financial year ended 31st December, 2005, the Board held four regular meetings at approximately quarterly intervals according to the Code. The attendance of each director is set out as follows:–

Name of Director	Number of attendance
Mr. Wu Chen San, Thomas	4/4
Mr. Wu Jenn Chang, Michael	4/4
Mr. Wu Jenn Tzong, Jackson	4/4
Mr. Yang Chih Chieh, Arthur	4/4
Mr. Ho Chin Fa, Steven	4/4
Ms. Fang Yen Ling	2/4
Mr. Lai Jenn Yang, Jeffrey	1/2
Mr. Liu Chung Kang, Helios	2/4

A.2 CHAIRMAN AND MANAGING DIRECTOR

The Company segregates the role of Chairman from the Managing Director. Mr. Wu Chen San, Thomas is the Chairman of the Company and Mr. Wu Jenn Chang, Michael is the Managing Director of the Company. They are brothers. The Chairman provides leadership to the Board and is responsible for the overall strategic planning and corporate development, whereas the Managing Director is responsible for policy making and corporate management in order to implement the strategies approved by the Board.

A.3 BOARD COMPOSITION

The Board consists of five executive directors and three independent non-executive directors:–

Executive directors
Mr. Wu Chen San, Thomas
Mr. Wu Jenn Chang, Michael
Mr. Wu Jenn Tzong, Jackson
Mr. Yang Chih Chieh, Arthur
Mr. Ho Chin Fa, Steven

Independent non-executive directors
Ms. Fang Yen Ling
Mr. Lai Jenn Yang, Jeffrey
Mr. Liu Chung Kang, Helios

The Board has met the recommended best practice under the Code that the number of independent non-executive directors is at least three. One independent non-executive director posses recognized professional qualifications in accounting. The independent non-executive directors bring independent judgement, knowledge and experience to the Board.

The Company has received, from each of the independent non-executive directors, an annual confirmation of his independence pursuant to Rule 3.13 of the Listing Rules. The Company considered all of the independent non-executive directors are independent within the definition of the Listing Rules.

A.4 APPOINTMENT, RE-ELECTION AND REMOVAL

The code provision A.4.1 provides that non-executive directors should be appointed for a specific terms, subject to re-election. A service contract was signed with each of the independent non-executive director with specific terms in early 2006. During the financial year ended 31st December, 2005, the non-executive directors are not appointed for a specific terms but they are subject to retirement by rotation in accordance with the Bye-Law of the Company.

Each of the non-executive directors has enter into a service contract with the Company for a term of one year and continuing thereafter until terminated by either party giving to the other party a period of advance notice in writing one month.

The code provision A.4.2 provides that every director, including those appointed for a specific term, should be subject to retirement by rotation at least once every three years. According to the Bye-Laws of the Company, before the relevant amendment to be approved in the forthcoming annual general meeting of the Company to be held in May 2006, at each annual general meeting, one-third of the Directors for the time being (or, if their number is not a multiple of three (3), the number nearest to but not greater than one-third) shall retire from the office by rotation provided that notwithstanding anything herein, the Chairman of the Board and/or the Managing Director of the Company shall not, whilst holding such office, be subject to retirement by rotation or be taken into account in determining the number of Directors to retire in each year. As the Chairman of the Board and the Managing Director of the Company are not subject to retirement by rotation under the Bye-Laws of the Company, this constitutes a deviation from code provision A.4.2 of the Code.

To comply with the code provision A.4.2 of the Code, the relevant amendment to the Bye-Laws of the Company will be proposed and will be approved by shareholders at the forthcoming annual general meeting of the Company to be held on 17th May, 2006. Accordingly, the Chairman of the Board and the Managing Director shall also be subject to retirement by rotation as with other directors.

A.5 RESPONSIBILITIES OF DIRECTORS

The directors are continually updated with the regulatory requirements, business activities and development of the Group to facilitate the discharge of their responsibilities.

The independent non-executive directors participate actively in the board meetings. They bring an independent judgement on issues of strategy, policy, performance, accountability, resources, key appointments and standards of conduct. They will lead where potential conflicts of interests arise in connected transaction. They are also members of Audit Committee.

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Companies (the "Model Code") as set out in Appendix 10 to the Listing Rules as its own code of conduct regarding securities transactions by the directors. Having made specific enquiry of all directors, all directors declared that they have complied with the Model Code throughout the year.

A.6 SUPPLY OF AND ACCESS TO INFORMATION

In respect of regular board meetings, an agenda and accompanying board papers of the meeting are sent in full to all directors at least 3 days before the intended date of a meeting.

The management has the obligation to supply the Board and the various Committees with adequate information in a timely manner to enable the members to make informed decisions. Each director has separate and independent access to the Group's senior management to acquire more information than is volunteered by management and to make further enquiries if necessary.

A.7 NOMINATION COMMITTEE

The Company set up a Nomination Committee in early 2006. The Nomination Committee comprises the three independent non-executive directors. Mr. Liu Chung Kang, Helios is the chairman of the Nomination Committee.

The primary function of the Nomination Committee is to review the structure, size and composition (including the skills, knowledge and experience) of the Board on a regular basis and make recommendations to the Board regarding any proposed changes.

The chairman of the Nomination Committee will report the findings and recommendations of the Nomination Committee to the Board after each meeting. The minutes of all meetings of Nomination Committee will be circulated to the Board for information.

For the financial year ended 31st December, 2005, the Board of directors considered its structure, size and composition (including the skills, knowledge and experience) possesses of a diversity of skills, expertise, experience and qualifications and believed that Board would perform its duties competently.

PEGASUS INTERNATIONAL

B. REMUNERATION OF DIRECTORS AND SENIOR MANAGEMENT

B.1 THE LEVEL AND MAKE-UP OF REMUNERATION AND DISCLOSURE

The code provision B.1.1 provides that the Company should establish a remuneration committee with specific written terms of reference which deal clearly with its authority and duties. A majority of the members of the remuneration committee should be independent non-executive directors.

The Company set up a remuneration committee in early 2006. The Remuneration Committee comprises the three independent non-executive directors. Mr. Lai Jenn Yang, Jeffrey is the chairman of the Remuneration Committee.

For the financial year ended 31st December, 2005, the emolument of the directors of the Company are decided by the Board of directors, having regard to the Company's operation results, individual performance and comparable market statistics.

The Group adopts a competitive remuneration package for its employees. Promotion and salary increments are assessed based on a performance related basis.

C. ACCOUNTABILITY AND AUDIT

C.1 FINANCIAL REPORTING

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

The directors acknowledge their responsibility to prepare the financial statements that give a true and fair view of the state of affairs of the Group. The Board was not aware of any material uncertainties relating to events or conditions that might cast significant doubt upon the Group's ability to continue as a going concern, the Board has prepared the accounts on a going concern basis.

The Company has announced its annual and interim results in a timely manner within approximately four months and three months, respectively, after the end of the relevant periods in order to enhance high level of corporate transparency.

C.2 INTERNAL CONTROLS

The Board is responsible for the Group's internal control system and for reviewing its effectiveness. Through the Audit Committee, the Board has reviewed the effectiveness of the system. No material deficiencies have been identified so far. The Board considered the Group's internal control system effective and that there were no significant areas of concern, which might affect the shareholders of the Company.

C.3 AUDIT COMMITTEE

An Audit Committee was established by the Company in 1999. The Audit Committee comprises the three independent non-executive directors, one of them possess recognized professional qualifications in accounting and has wide experience in audit and accounting. Ms. Fang Yin Ling is the chairman of the Audit Committee.

The primary function of the Audit Committee is to review and supervise the Group's financial reporting process and internal controls.

Two audit Committee meetings were held during the financial year ended 31st December, 2005. The attendance of each member is set out as follows:–

Name of Member	Number of attendance
Ms. Fang Yen Ling	2/2
Mr. Lai Jenn Yang, Jeffrey	1/1
Mr. Liu Chung Kang, Helios	2/2

The chairman of the Audit Committee will report the findings and recommendations of the Audit Committee to the Board after each meeting. The minutes of all meetings of Audit Committee are circulated to the Board for information.

A summary of the work performed by the Audit Committee for the financial year ended 31st December, 2005 is set out in "Audit Committee Report" on page 16.

C.4 FEE PAID/PAYABLE TO GROUP'S AUDITORS

For the financial year ended 31st December, 2005, the fee paid/payable to the Group's auditors, Messrs. Deloitte Touche Tohmatsu, is set out as follows:–

Services rendered	Fee paid/payable *HK$'000*
Audit services	780
Non-audit services	–
Taxation services	30

D. DELEGATION BY THE BOARD

D.1 MANAGEMENT FUNCTIONS

The Board is responsible for determining the overall strategy and corporate development and ensuring the business operations are properly monitored. The Board reserves the right to decide all policy matters of the Group and material transactions.

The Board delegates the day-to-day operations to general managers and department heads who are responsible for different aspects of the operations of the Group.

D.2 BOARD COMMITTEES

The Company has maintained the Audit Committee throughout the year to oversee particular aspects of the Group's affairs. The Audit Committee, Remuneration Committee and Nomination Committee have specific written terms of reference which deal clearly with their authority and duties. The chairman of the Committees will report the findings and recommendations to the Board after each meeting. The minutes of all meetings of the committee are circulated to the Board for information.

E. COMMUNICATION WITH SHAREHOLDERS

E.1 EFFECTIVE COMMUNICATION

The annual general meeting enables the shareholders of the Company to exchange views with the Board. The chairman of the Board and the Managing Director have attended at the annual general meeting to be available to answer the questions of the shareholders of the Company.

Separate resolutions are proposed at the annual general meeting on each substantially separate issue, including the election of individual director.

E.2 VOTING BY POLL

The right to demand a poll was set out in the circular to shareholders of the Company dispatched together with the Annual Report for the year ended 31st December, 2005.

Audit Committee Report

The Audit Committee (the "Committee") has three members; three of them are independent non-executive director.

The Committee oversees the financial reporting process. In this process, management is responsible for the preparation of the Group financial statements including the selection of suitable accounting policies. External auditors are responsible for auditing and attesting to Group financial statements and evaluating Group system of Internal controls. The Committee oversees the respective work of management and external auditors to endorse the processes and safeguards employed by them. The Committee presents a report to the Board on its findings after each Committee meeting.

The Committee reviewed and discussed with management and external auditors the 2005 consolidated financial statements included in 2005 Annual Report. In the regard, the Committee had discussions with management with regard to new or changes in accounting policies as applied, and significant judgments affecting the Group financial statements. The Committee also received reports and met with the external auditors to discuss the general scope of their audit work (including the impact of new or changes in accounting policies as applied), their assessment of Group internal controls.

Based of these review and discussion, and the report of the external auditors, the Committee recommended to the Board approval of the consolidated financial statements for the year ended 31st December, 2005, with the Auditors' Report thereon.

The Committee also reviewed and recommended to the Board approval of the unaudited financial statements for the six months ended 30th June, 2005, prior to public announcement and filing.

The Committee recommended to the Board that the shareholders be asked to re-appointed Deloitte Touche Tohmatsu as the Group's external auditors for 2006.

The Committee has also reviewed and revised its terms of reference.

MEMBERS OF THE AUDIT COMMITTEE

Ms. Fang Yen Ling
Mr. Lai Jenn Yang, Jeffrey
Mr. Liu Chung Kang, Helios

Hong Kong, 20th April, 2006

Biographical Data of Directors and Senior Management

EXECUTIVE DIRECTORS

Mr. Wu Chen San, Thomas , aged 55, is the Chairman of the Group and is responsible for the Group's sales, marketing and strategic planning. Mr. Wu joined the footwear business founded by his father, Mr. Wu Suei, in the early 1970's and has 36 years' experience in the footwear manufacturing business.

Mr. Wu Jenn Chang, Michael, aged 48, is the Deputy Chairman of the Group and is responsible for the Group's finance, production and purchasing. Mr. Wu is a director of the Taiwan Footwear Manufacturing Association and the Chairman of the Taiwanese-invested Enterprises Association of Guangzhou. Mr. Wu joined the footwear business founded by his father, Mr. Wu Suei, in 1983 and has 23 years' experience in the footwear manufacturing business.

Mr. Wu Jenn Tzong, Jackson, aged 50, is responsible for the Group's sourcing functions conducted in Taiwan through the Group's subsidiary, Tospstair International (Taiwan) Ltd. Mr. Wu joined the footwear business founded by his father, Mr. Wu Suei, in 1977 and has 29 years' experience in the footwear manufacturing business.

Mr. Yang Chih Chieh, Arthur, aged 41, holds a Master's degree in international finance from Northrop University, California, the United States of America.

Mr. Ho Chin Fa, Steven, age 53, is a Deputy General Manager of the Group. He is responsible for production management and staff training. Mr. Ho joined the Group in 1990 and has 23 years' experience in the footwear manufacturing business.

NON-EXECUTIVE DIRECTORS

Ms. Fang Yen Ling, aged 48, is a partner of KPMG Peat Marwick, Certified Public Accountants, Taipei, Taiwan. She has 29 years of accounting and auditing experience. She is currently a member of the Taiwan Provincial CPA Association.

Mr. Liu Chung Kang, Helios, aged 55, is currently a director of a Taiwan listed company, Fast Technologies Inc. and its subsidiary company, Shanghai Netup Management Software Co., Ltd. He graduated from Chiao Tung University in Taiwan. He obtained a bachelor degree in Electricity Engineering and a master degree in Management Science. Prior to joining the Company, he had more than 20 years of experience in managing software development.

Mr. Lai Jenn Yang, Jeffrey, aged 48, is currently an Executive Director of Nicematch International Co., Ltd, which is incorporated in Taiwan. Mr. Lai graduated from Tamkang University in Taiwan and obtained a bachelor degree in Civil Engineering. He also holds a master degree in Engineering from Ohio University is the USA. Prior to joining to the Company, he had more than 20 years of experience in operation and engineering management.

Biographical Data of Directors and Senior Management

PEGASUS INTERNATIONAL

SENIOR MANAGEMENT

Mr. Lee Yiu Ming, aged 41, graduated from Hong Kong Polytechnic University and holds a Master's degree in business administration from the Queen's University of Belfast, Northern Ireland. He is an associate member of the Hong Kong Institute of Certified Public Accountants and a fellow member of the Association of Chartered Certified Accountants. Mr. Lee is a Deputy General Manager of the Group and the company secretary of the Company. He is responsible for the financial, accounting and company secretarial functions of the Group. Prior to joining the Group in May 1996, he worked for an international accounting firm for over seven years.

Mr. Yeh Ming Chieh, aged 49, is a manager of the chemical plant of Panyu Pegasus Footwear Co. Ltd. ("Panyu Pegasus"). He has 36 years' experience in footwear manufacturing and sole unit production. Prior to joining the Group in 1994, Mr. Yeh worked as a technical consultant in Taiwan, Indonesia and the PRC. He is responsible for the production management and research and development.

Ms. Lin Hui Fan, aged 55, is a senior quality assurance inspector and oversees the quality of uppers. Ms. Lin joined the Group in 1991 and has 30 years' experience in footwear manufacturing. Ms. Lin is responsible for quality control of the Group's footwear products and has extensive experience in training quality control staff.

Mr. Hsieh Hsin Lee, aged 45, is a manager of Panyu Pegasus. Mr. Hsieh joined the Group in 1991 and has 26 years' experience in footwear manufacturing. He is responsible for the Group's production management and quality control process. He is also responsible for staff training.

Mr. Chang Ho Hsi, aged 51, is a senior manager of administration in Panyu Pegasus. He studied Japanese in Tamkang University, and obtained a bachelor degree in literature. Mr. Chang is also a member of Taiwan Footwear Manufacturers Association in the Republic of China.

Mr. Choi Jae Deng, aged 48, is a quality assurance manager of Panyu Pegasus. Mr. Choi joined the Group in 2004 and has over 24 years' experience in footwear manufacturing and product development.

Mr. Yu Hung Hing, aged 41, is a production manager of Panyu Pegasus. Mr. Yu joined the Group in 2004 and has over 21 years' experience in footwear manufacturing and quality control.

Jong Wook Sun, aged 55, graduated from Busan National University. He is a Deputy General Manager Chemical Division of Panyu Pegasus. Mr. Sun joined the Group in November 2003. He has 28 years' experience in sole development and manufacture.

Mr. Lee Kuo Hwa, aged 49, is a Deputy General Manager of Panyu Pegasus. Mr. Lee graduated from East Texas State University, Texas, the US and holds a Master' s degree in computer science. He is responsible for production management of the Group. Mr. Lee has 12 years' experience in footwear manufacturing business.

Directors' Report

The directors present the annual report and audited financial statements for the year ended 31st December, 2005.

PRINCIPAL ACTIVITIES

The Company is an investment holding company. The Group is engaged principally in the manufacture and sale of footwear products. The activities of its associates, jointly controlled entities and principal subsidiaries are set out in notes 16, 17 and 34, respectively, to the financial statements.

RESULTS AND APPROPRIATIONS

The results of the Group for the year ended 31st December, 2005 are set out in the consolidated income statement on page 26.

The directors did not recommend the payment of an interim dividend. The directors recommend the payment of a final dividend of Hong Kong 1cent per ordinary share to the shareholders on the register of members on 17th May, 2006, amounting to US$943,000.

PROPERTY, PLANT AND EQUIPMENT

Certain of the Group's buildings were revalued at 31st December, 2005. The revaluation resulted in a surplus over book values amounting to US$1,630,000, which has been credited directly to the revaluation reserve.

The Group continued its plant replacement policy and expended US$2,773,000 on new plant and machinery during the year.

Details of these and other movements during the year in the property, plant and equipment of the Group are set out in note 14 to the financial statements.

SHARE CAPITAL

Details of the share capital of the Company are set out in note 25 to the financial statements.

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

DISTRIBUTABLE RESERVES OF THE COMPANY

As at 31st December, 2005, the Company's reserves available for distribution to shareholders consisted of accumulated profits, dividend reserve and contributed surplus, totalling approximately US$22,683,000 (2004: US$23,088,000).

Under the Companies Act 1981 of Bermuda (as amended), the contributed surplus account of the Company is available for distribution. However, a Company cannot declare or pay a dividend, or make a distribution out of contributed surplus if:

(a) the Company is, or would after the payment be, unable to pay its liabilities as they become due; or

(b) the realisable value of the Company's assets would thereby be less than the aggregate of its liabilities and its issued share capital and share premium accounts.

DIRECTORS

The directors of the Company during the year and up to the date of this report were:

Executive directors:

Mr. Wu Chen San, Thomas *(Chairman)*
Mr. Wu Jenn Chang, Michael *(Deputy Chairman)*
Mr. Wu Jenn Tzong, Jackson
Mr. Yang Chih Chieh, Arthur
Mr. Ho Chin Fa, Steven

Independent non-executive directors:

Ms. Fang Yen Ling	
Mr. Lai Jenn Yang, Jeffrey	(appointed on 22nd June, 2005)
Mr. Liu Chung Kang, Helios	
Mr. Chang Ho Hsi	(resigned on 22nd June, 2005)

In accordance with Clause 87(1) of the Company's Bye-laws, Mr. Wu Jenn Tzong, Jackson retire by rotation and, being eligible, offer himself for re-election at the forthcoming annual general meeting.

In addition, in accordance with Clause 86(2) of the Company's Bye Law, Mr. Lai Jenn Yang, Jeffrey, the newly appointed director, also retire and being eligible, offer himself re-election at the forthcoming annual general meeting.

The terms of office of non-executive directors are subject to retirement by rotation in accordance with the provisions of the Company's Bye-laws.

The Company has received, from each of the independent non-executive directors, an annual confirmation of his independence pursuant to Rule 3.13 of the Rules Governing the Listing Securities on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). The Company considers all of the independent non-executive directors are independent.

DIRECTORS' SERVICE CONTRACTS

Each of the executive directors has entered into a service contract with the Company for a term of three years commencing 25th September, 1996 and continuing thereafter until terminated by either party giving to the other party a period of advance notice in writing ranging from three to six months.

None of the directors being proposed for re-election at the forthcoming annual general meeting has an unexpired service contract with the Company or any of its subsidiaries which is not determinable by the Group within one year without payment of compensation, other than statutory compensation.

DIRECTORS' INTERESTS IN SHARES

At 31st December, 2005, the interests of the directors and their associates in the shares, underlying shares or debentures of the Company and its associated corporation, as recorded in the register maintained by the Company pursuant to Section 352 of the Securities and Futures Ordinance (the "SFO"), or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by the Directors of Listed Companies, were as follows:

Long positions

(a) *Ordinary shares of HK$0.10 each of the Company*

Name of director	Capacity	Number of issued ordinary shares held	Percentage of the issued share capital of the Company
Wu Jenn Chang, Michael	Beneficial owner	8,000,000	1.09%
Wu Jenn Tzong, Jackson	Beneficial owner	1,000,000	0.14%
Yang Chih Chieh, Arthur	Family *(note 1)*	7,193,970	0.98%
		16,193,970	2.21%

(b) *Ordinary shares of the associated corporation of the Company*

Pegasus Footgear Management Limited *(note 2)*

Name of director	Capacity	Number of issued ordinary shares held	Percentage of the issued share capital of the associated corporation
Wu Chen San, Thomas	Beneficial owner *(note 3)*	3,235	16%
Wu Jenn Chang, Michael	Corporate *(note 4)*	6,470	32%
Wu Jenn Tzong, Jackson	Corporate *(note 5)*	6,470	32%
Yang Chih Chieh, Arthur	Corporate *(note 6)*	474	2%
		16,649	82%

Notes:

1. Mr. Yang Chih Chieh, Arthur is deemed under the SFO to be interested in the said shares held by his wife.

2. Pegasus Footgear Management Limited is the holding company of the Company.

3. The shares are jointly held by Mr. Wu Chen San, Thomas and Mrs. Peggy Wu, a married couple.

4. The shares are entirely held by M. W. Investment Limited, a company owned by Mr. Wu Jenn Chang, Michael.

5. The shares are entirely held by J. W. Investment Limited, a company owned by Mr. Wu Jenn Tzong, Jackson.

6. The shares are entirely held by A & M Management Limited, a company jointly owned by Mr. Yang Chih Chieh, Arthur and his wife.

Save as disclosed above, at 31st December, 2005, none of the directors nor their associates had any interests or short positions in the shares, underlying shares or debentures of the Company or any associated corporation.

SHARE OPTIONS

Particulars of the Company's share option scheme are set out in note 26 to the financial statements.

No share options were granted or exercised during the year ended 31st December, 2005. As at 31st December, 2005, no share options of the Company were outstanding.

ARRANGEMENTS TO ACQUIRE SHARES OR DEBENTURES

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 directors of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

DIRECTORS' INTERESTS IN CONTRACTS OF SIGNIFICANCE

No contracts of significance to which the Company, its holding company or any of its subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

SUBSTANTIAL SHAREHOLDERS

As at 31st December, 2005, the register of substantial shareholders maintained by the Company pursuant to Section 336 of the SFO shows that, other than the interests disclosed in "Directors' Interest in Shares", the following shareholder had notified the Company of relevant interest in the issued share capital of the Company.

Long position

Ordinary shares of HK$0.10 each of the Company

Name of shareholder	Capacity	Number of issued ordinary shares held	Percentage of the issued share capital of the Company %
Pegasus Footgear Management Limited *(Note)*	Beneficial owner	468,743,940	64

Note: Details of the directors' interests in Pegasus Footgear Management Limited are disclosed under the section headed "Directors' Interests in Shares".

Save as disclosed above, the Company has not been notified of any other relevant interests or short position in the issued share capital of the Company as at 31st December, 2005.

MAJOR CUSTOMERS AND SUPPLIERS

For the year ended 31st December, 2005, the largest customer of the Group accounted for approximately 56% of the Group's turnover. The five largest customers accounted for approximately 87% of the Group's turnover. For the year ended 31st December, 2005, the aggregate purchases attributable to the Group's five largest suppliers were less than 30% of total purchases.

None of the directors, their associates or any shareholder of the Company which, to the knowledge of the directors, owned more than 5% of the Company's issued share capital had any interest in the share capital of any of the five largest customers of the Group.

EMOLUMENT POLICY

The emolument policy of the employees of the Group is set up by the board of directors on the basis of their merit, qualifications and competence.

The emoluments of the directors of the Company are decided by the board of directors, as authorised by shareholders at the annual general meeting, having regard to the Group's operating results, individual performance and comparable market statistics.

The Company has adopted a share option scheme as an incentive to directors and eligible employees, details of the scheme are set out in note 26 to the financial statements.

SUFFICIENCY OF PUBLIC FLOAT

The Company has maintained a sufficient public float throughout the year ended 31st December, 2005.

PRE-EMPTIVE RIGHTS

There is no provision for pre-emptive rights under the Company's Bye Law or the laws of Bermuda, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

AUDITORS

A resolution will be submitted to the annual general meeting to re-appoint Messrs. Deloitte Touche Tohmatsu as auditors of the Company.

On behalf of the Board
Wu Chen San, Thomas
CHAIRMAN
Hong Kong, 20th April, 2006

Deloitte.
德勤

TO THE MEMBERS OF PEGASUS INTERNATIONAL HOLDINGS LIMITED

(incorporated in Bermuda with limited liability)

We have audited the consolidated financial statements of Pegasus International Holdings Limited (the "Company") and its subsidiaries (the "Group") from pages 26 to 69 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 consolidated financial statements which give a true and fair view. In preparing consolidated 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 financial statements and to report our opinion solely to you, as a body, in accordance with section 90 of the Bermuda Companies Act, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

BASIS OF OPINION

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the consolidated financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the consolidated financial statements, and of whether the accounting policies are appropriate to the circumstances of the Group, 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 consolidated financial statements are free from material misstatement. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the consolidated financial statements. We believe that our audit provides a reasonable basis for our opinion.

OPINION

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Group as at 31st December, 2005 and of the profit 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.

Deloitte Touche Tohmatsu
Certified Public Accountants
Hong Kong
20th April, 2006

Consolidated Income Statement

For the year ended 31st December, 2005

	NOTES	2005 US$'000	2004 US$'000 (restated)
Turnover	7	**141,242**	143,704
Cost of sales		**(117,946)**	(118,724)
Gross profit		**23,296**	24,980
Other income		**859**	1,156
Selling and distribution costs		**(8,506)**	(11,901)
Administrative expenses		**(11,798)**	(12,956)
Share of results of associates		**181**	313
Share of results of jointly controlled entities		**(76)**	64
Interest on bank borrowings wholly repayable within five years		**(1,199)**	(649)
Impairment loss and write-off in respect of an investment security	18	**–**	(2,328)
Profit (loss) before taxation	8	**2,757**	(1,321)
Taxation	11	**(290)**	421
Profit (loss) for the year		**2,467**	(900)
Dividends	12	**943**	943
Earnings (loss) per share	13		
Basic		**0.34 US cent**	(0.12) US cent
Diluted		**N/A**	N/A

Consolidated Balance Sheet

At 31st December, 2005

	NOTES	2005 US$'000	2004 US$'000 (restated)
Non-current assets			
Property, plant and equipment	*14*	**65,136**	67,423
Prepaid lease payments	*15*	**5,396**	5,532
Interests in associates	*16*	**1,012**	831
Interests in jointly controlled entities	*17*	**2,423**	2,499
		73,967	76,285
Current assets			
Inventories	19	**45,819**	45,045
Trade and other receivables	20	**13,634**	15,074
Prepaid lease payments	15	**136**	136
Amount due from an associate	16	**8**	14
Bank balances and cash	21	**12,525**	5,692
		72,122	65,961
Current liabilities			
Trade and other payables	22	**11,664**	11,705
Tax payable		**446**	29
Unsecured bank borrowings – due within one year	23	**15,858**	17,073
		27,968	28,807
Net current assets		**44,154**	37,154
		118,121	113,439
Capital and reserves			
Share capital	25	**9,428**	9,428
Reserves		**92,658**	89,001
Total equity		**102,086**	98,429
Non-current liabilities			
Unsecured bank borrowings – due after one year	23	**13,955**	13,370
Deferred tax liabilities	27	**2,080**	1,640
		16,035	15,010
		118,121	113,439

The financial statements on pages 26 to 69 were approved and authorised for issue by the Board of Directors on 20th April, 2006 and are signed on its behalf by:

Wu Chen San, Thomas	**Wu Jenn Chang, Michael**
DIRECTOR	*DIRECTOR*

Consolidated Statement of Changes in Equity

For the year ended 31st December, 2005

	Attributable to equity holders of the Company								
	Share capital *US$'000*	Share premium *US$'000*	Revaluation reserve *US$'000*	Merger reserve *US$'000*	Dividend reserve *US$'000*	Accumulated profits *US$'000*	Total *US$'000*	Minority interest *US$'000*	Total *US$'000*
At 1st January, 2004, as originally stated	9,428	21,644	8,081	(4,512)	1,414	70,288	106,343	1	106,344
Effect of changes in accounting policies *(note 2)*	–	–	(5,571)	–	–	920	(4,651)	–	(4,651)
At 1st January, 2004, as restated	9,428	21,644	2,510	(4,512)	1,414	71,208	101,692	1	101,693
Revaluation decrease on buildings, as restated	–	–	(8)	–	–	–	(8)	–	(8)
Reversal of deferred tax liability arising on revaluation of buildings *(note 27)*, as restated	–	–	2	–	–	–	2	–	2
Net expenses recognised directly in equity	–	–	(6)	–	–	–	(6)	–	(6)
Loss for the year, as restated	–	–	–	–	–	(900)	(900)	–	(900)
Total recognised income and expense for the year	–	–	(6)	–	–	(900)	(906)	–	(906)
Acquisition of additional interest in a subsidiary	–	–	–	–	–	–	–	(1)	(1)
Dividends paid for 2003	–	–	–	–	(1,414)	–	(1,414)	–	(1,414)
Dividends declared for 2004	–	–	–	–	943	(943)	–	–	–
Dividends paid for 2004	–	–	–	–	(943)	–	(943)	–	(943)
At 31st December, 2004	9,428	21,644	2,504	(4,512)	–	69,365	98,429	–	98,429
Revaluation increase on buildings	–	–	1,630	–	–	–	1,630	–	1,630
Deferred tax liability arising on revaluation of buildings *(note 27)*	–	–	(440)	–	–	–	(440)	–	(440)
Net income recognised directly in equity	–	–	1,190	–	–	–	1,190	–	1,190
Profit for the year	–	–	–	–	–	2,467	2,467	–	2,467
Total recognised income and expense for the year	–	–	1,190	–	–	2,467	3,657	–	3,657
Dividends declared for 2005	–	–	–	–	943	(943)	–	–	–
At 31st December, 2005	9,428	21,644	3,694	(4,512)	943	70,889	102,086	–	102,086

The merger reserve of the Group represents the difference between the nominal amount of the share capital of the subsidiaries acquired and the nominal value of the share capital of the acquiring companies issued in exchange pursuant to a corporate reorganisation prior to the listing of the Company's shares in 1996.

Consolidated Cash Flow Statement

For the year ended 31st December, 2005

	2005 **US$'000**	2004 US$'000 (restated)
OPERATING ACTIVITIES		
Profit (loss) before taxation	**2,757**	(1,321)
Adjustments for:		
Interest income	**(107)**	(76)
Release of prepaid lease payments	**136**	101
Depreciation and amortisation of property, plant and equipment	**8,162**	8,421
Impairment loss on trade receivables	**364**	362
Share of results of associates	**(181)**	(313)
Share of results of jointly controlled entities	**76**	(64)
Loss on disposal of property, plant and equipment	**101**	6
Interest paid	**1,199**	649
Impairment loss and write off in respect of an investment security	**–**	2,328
Operating cash flows before movements in working capital	**12,507**	10,093
Increase in inventories	**(774)**	(3,216)
Decrease in trade and other receivables	**1,076**	127
Decrease (increase) in amount due from an associate	**6**	(14)
Decrease in amount due from an investee	**–**	199
Decrease in trade and other payables	**(41)**	(6,039)
Decrease in amount due to an associate	**–**	(222)
Cash generated from operations	**12,774**	928
Hong Kong Profits Tax paid	**(7)**	(6)
Taxation in other jurisdictions refund (paid)	**134**	(306)
NET CASH FROM OPERATING ACTIVITIES	**12,901**	616
INVESTING ACTIVITIES		
Purchase of property, plant and equipment	**(4,346)**	(5,069)
Interest received	**107**	79
Investment in jointly controlled entities	**–**	(300)
Acquisition of additional interests in a subsidiary	**–**	(1)
Dividend received from associates	**–**	80
Proceeds from disposal of property, plant and equipment	**–**	15
NET CASH USED IN INVESTING ACTIVITIES	**(4,239)**	(5,196)
FINANCING ACTIVITIES		
Repayment of bank loans	**(14,590)**	(17,796)
Repayment of trust receipt loans	**(9,053)**	(8,746)
Interest paid	**(1,199)**	(640)
Bank loans raised	**15,319**	13,204
Trust receipt loans raised	**7,694**	10,494
Dividends paid	**–**	(2,357)
NET CASH USED IN FINANCING ACTIVITIES	**(1,829)**	(5,841)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	**6,833**	(10,421)
CASH AND CASH EQUIVALENTS AT 1ST JANUARY	**5,692**	16,113
CASH AND CASH EQUIVALENTS AT 31ST DECEMBER, represented by bank balances and cash	**12,525**	5,692

1. GENERAL

The Company is a public limited company incorporated in Bermuda as an exempted company with limited liability and its shares are listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). The directors consider Pegasus Footgear Management Limited, a company incorporated in the British Virgin Islands, to be the ultimate holding company of the Company. The address of the registered office and principal place of business of the Company are disclosed in the corporate information.

These financial statements are presented in United States dollars ("US Dollar"), which is the same as the functional currency of the Company.

The principal activities of the Company and its subsidiaries (the "Group") are manufacture and sale of footwear products.

2. APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS

In the current year, the Group has applied, for the first time, a number of new Hong Kong Financial Reporting Standards ("HKFRSs"), Hong Kong Accounting Standards ("HKASs") and Interpretations (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 have been charged. 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 and/or prior accounting years are prepared and presented:

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. 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 application of HKAS 32 has had no material impact on how financial instruments of the Group are presented for current and prior accounting years. The principal effects resulting from the implementation of HKAS 39 are summarised below.

2. APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS *(Continued)*

FINANCIAL INSTRUMENTS *(CONTINUED)*

Financial assets and financial liabilities other than debt and equity securities
From 1st January, 2005 onwards, the Group has classified and measured its financial assets and financial liabilities other than debt and equity securities (which were previously outside the scope of Statement of Standard Accounting Practice 24 "*Accounting for Investments in Securities*" issued by the HKICPA) in accordance with the requirements of HKAS 39. Financial assets under HKAS 39 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. "Loans and receivables" and "held-to-maturity financial assets" are measured at amortised cost using the effective interest method after initial recognition. Financial liabilities are generally classified as "financial liabilities at fair value through profit or loss" or "other financial liabilities". Financial liabilities at fair value through profit or loss are measured at fair value, with changes in fair value being recognised in profit or loss directly. Other financial liabilities are carried at amortised cost using the effective interest method after initial recognition.

Derivatives and hedging
Prior to 1st January, 2005, the Group deemed its derivative as non-speculative and is used as a hedge of a net monetary asset or liability, the gain or loss and the discount or premium on the contract is taken to the income statement.

From 1st January, 2005 onwards, all derivatives that are within the scope of HKAS 39 are required to be carried at fair value at each balance sheet date regardless of whether they are deemed as held for trading or designated as effective hedging instruments. Under HKAS 39, derivatives (including embedded derivatives separately accounted for from the non-derivative host contracts) are deemed as held-for-trading financial assets or financial liabilities, unless they qualify and are designated as effective hedging instruments. The corresponding adjustments on changes in fair values would depend on whether the derivatives are designated as effective hedging instruments, and if so, the nature of the item being hedged. For derivatives that are deemed as held for trading, changes in fair values of such derivatives are recognised in profit or loss for the year in which they arise.

The Group has applied the relevant transitional provisions in HKAS 39. As the derivatives do not meet the requirements of hedge accounting in accordance with HKAS 39, the Group has, from 1st January, 2005 onwards, deemed such derivatives as held for trading. The adoption of this accounting policy has had no material effect on the results for the current year. Comparative figures are not required to be restated.

2. APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS *(Continued)*

FINANCIAL INSTRUMENTS *(CONTINUED)*

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 of US$107,000 at 31st December, 2004 which were derecognised were not restated on that date. Instead they were restated as on 1st January, 2005. As at 31st December, 2005, the Group's bills receivables discounted with full recourse of US$319,000 have not been derecognised. Instead, the related borrowings have been recognised on the balance sheet (see Note 3 for financial impact).

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 revaluation 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 3 for the financial impact).

3. SUMMARY OF THE EFFECTS OF THE APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS

The effects of the application of new HKFRSs described in note 2, on administrative expenses for the current and prior years, are as follows:

	2005	2004
	US$'000	*US$'000*
Decrease in amortisation expenses	**137**	182

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

	As at 31st December, 2004 (originally stated)	Effect of HKAS 17	As at 31st December, 2004 (restated)	Effect of HKAS 39	As at 1st January, 2005 (restated)
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
Balance sheet items					
Property, plant and equipment	79,679	(12,256)	67,423	–	**67,423**
Trade and other receivables	15,074	–	15,074	107	**15,181**
Prepaid lease payments	–	5,668	5,668	–	**5,668**
Deferred tax liabilities	(3,460)	1,820	(1,640)	–	**(1,640)**
Bank borrowings	(30,443)	–	(30,443)	(107)	**(30,550)**
Other assets and liabilities	42,347	–	42,347	–	**42,347**
Total effects on assets and liabilities	103,197	(4,768)	98,429	–	**98,429**
Accumulated profits	68,263	1,102	69,365	–	**69,365**
Revaluation reserve	8,374	(5,870)	2,504	–	**2,504**
Share capital and other reserves	26,560	–	26,560	–	**26,560**
Total effects on equity	103,197	(4,768)	98,429	–	**98,429**

3. SUMMARY OF THE EFFECTS OF THE APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS *(Continued)*

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 *US$'000*	**Effect of HKAS 17** *US$'000*	**As restated** *US$'000*
Share capital and other reserves	27,974	–	27,974
Accumulated profits	70,288	920	71,208
Asset revaluation reserve	8,081	(5,571)	2,510
Total effects on equity	106,343	(4,651)	101,692

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 standards and interpretations will have no material impact on the financial statements of the Group.

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. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared on the historical cost basis except for certain properties and financial instruments which are measured at revalued amounts or fair values, as explained in the accounting policies set out below.

The consolidated financial statements have been prepared in accordance with HKFRSs issued by the HKICPA. In addition, the consolidated financial statements include applicable disclosures required by the Rules Governing the Listing of Securities on the Stock Exchange and by the Companies Ordinance.

BASIS OF CONSOLIDATION

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Minority interests in the net assets of consolidated subsidiaries are presented separately from the Group's equity therein. Minority interests in the net assets consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

REVENUE RECOGNITION

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts and sales related taxes.

Sales of goods are recognised when goods are delivered and title has passed.

Interest income from a financial asset is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts the estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment, other than construction in progress, are stated at cost or fair value less subsequent accumulated depreciation and amortisation and accumulated impairment losses.

Buildings held for use in the production or supply of goods or services, or for administrative purposes, are stated in the balance sheet at their revalued amount, being the fair value at the date of revaluation less any subsequent accumulated depreciation and any subsequent accumulated impairment losses. Revaluations are performed with sufficient regularity such that the carrying amount does not differ materially from that which would be determined using fair values at the balance sheet date.

Any revaluation increase arising on revaluation of buildings is credited to the revaluation reserve, except to the extent that it reverses a revaluation decrease of the same asset previously recognised as an expense, in which case the increase is credited to the income statement to the extent of the decrease previously charged. A decrease in net carrying amount arising on revaluation of an asset is dealt with as an expense to the extent that it exceeds the balance, if any, on the revaluation reserve relating to a previous revaluation of that asset. On the subsequent sale or retirement of a revalued asset, the attributable revaluation surplus is transferred to accumulated profits.

Depreciation is provided to write off the cost or fair value of items of property, plant and equipment, other than construction in progress, over their estimated useful lives and after taking into account their estimated residual value, using the straight-line method.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the income statement in the year in which the item is derecognised.

Construction in progress is stated at cost which includes all development expenditure and the direct costs attributable to such projects. Construction in progress is not depreciated or amortised until completion of construction and the asset is available for use. The cost of completed construction works is transferred to the appropriate categories of property, plant and equipment.

LEASEHOLD LAND AND BUILDINGS UNDER DEVELOPMENT FOR FUTURE OWNER-OCCUPIED PURPOSE

When the leasehold land and buildings are in the course of development for production, rental or for administrative purposes, the leasehold land component is classified as a prepaid lease payment and amortised over a straight-line basis over the lease term. During the construction period, the amortisation charge provided for the leasehold land is included as part of costs of buildings under construction. Buildings under construction are carried at cost, less any identified impairment losses. Depreciation of buildings commences when they are available for use (i.e. when they are in the location and condition necessary for them to be capable of operating in the manner intended by management).

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

INVESTMENTS IN ASSOCIATES

The results and assets and liabilities of associates are incorporated in consolidated financial statements using the equity method of accounting. Under the equity method, investments in associates are carried in the consolidated balance sheet at cost as adjusted for post-acquisition changes in the Group's share of the profit or loss and of changes in equity of the associate, less any identified impairment loss. When the Group's share of losses of an associate equals or exceeds its interest in that associate (which includes any long-term interests that, in substance, form part of the Group's net investment in the associate), the Group discontinues recognising its share of further losses. An additional share of losses is provided for and a liability is recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that associate.

Where a group entity transacts with an associate of the Group, unrealised profits and losses are eliminated to the extent of the Group's interest in the associate, except to the extent that unrealised losses provide evidence of an impairment of the asset transferred, in which case, the full amount of losses is recognised.

JOINT VENTURES

Joint controlled entities

Joint venture arrangements that involve the establishment of a separate entity in which venturers have joint control over the economic activity of the entity are referred to as jointly controlled entities.

The results and assets and liabilities of jointly controlled entities are incorporated in the consolidated financial statements using the equity method of accounting. Under the equity method, investments in jointly controlled entities are carried in the consolidated balance sheet at cost as adjusted for post-acquisition changes in the Group's share of the profit or loss and of changes in equity of the jointly controlled entities, less any identified impairment loss. When the Group's share of losses of a jointly controlled entity equals or exceeds its interest in that jointly controlled entity (which includes any long-term interests that, in substance, form part of the Group's net investment in the jointly controlled entity), the Group discontinues recognising its share of further losses. An additional share of losses is provided for and a liability is recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that jointly controlled entity.

When a group entity transacts with a jointly controlled entity of the Group, unrealised profits or losses are eliminated to the extent of the Group's interest in the jointly controlled entity, except to the extent that unrealised losses provide evidence of an impairment of the asset transferred, in which case, the full amount of losses is recognised.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

IMPAIRMENT

At each balance sheet date, the Group reviews the carrying amounts of its assets to determine whether there is any indication that those assets have suffered an impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

INVENTORIES

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using the first-in, first-out method. Cost comprises direct materials and, when applicable, direct labour costs and those overhead that have been incurred in bringing the inventories to their present location and condition. Net realisable value represents the estimated selling price less any estimated costs of completion and costs to be incurred in marketing, selling and distribution.

LEASES

Leases are classified as finance leases whenever the terms of the leases transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Group as lessee
Rentals payable under operating leases are charged to profit or loss on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are recognised as a reduction of rental expense over the lease term on a straight-line basis.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

FOREIGN CURRENCIES

In preparing the financial statements of each individual group entity, transactions in currencies other than the functional currency of that entity (foreign currencies) are recorded in its functional currency (i.e. the currency of the primary economic environment in which the entity operates) at the rates of exchanges prevailing on the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the translation of monetary items, are recognised in profit or loss in the period in which they arise. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period except for differences arising on the retranslation of non-monetary items in respect of which gains and losses are recognised directly in equity, in which cases, the exchange differences are also recognised directly in equity.

For the purposes of presenting the consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated into the presentation currency of the Company (i.e. United States dollars) at the rate of exchange prevailing at the balance sheet date, and their income and expenses are translated at the average exchange rates for the year unless exchange rates fluctuate significantly during the period, in which case, the exchange rates prevailing at the dates of transactions are used. Exchange differences arising, if any, are recognised as a separate component of equity (the translation reserve). Such exchange difference are recognised in profit or loss in the period in which the foreign operation is disposed of.

TAXATION

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes income statement items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from the initial recognition of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

TAXATION *(Continued)*

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and interests in jointly controlled entities, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realised. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

RETIREMENT BENEFITS SCHEMES

Payments to state-managed retirement benefit schemes and the Mandatory Provident Fund Scheme are charged as an expense as they fall due.

FINANCIAL INSTRUMENTS

Financial assets and financial liabilities are recognised on the balance sheet when a group entity becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

Financial assets

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. At each balance sheet date subsequent to initial recognition, loans and receivables (including trade and other receivables, bank balances and amount due from an associate) are carried at amortised cost using the effective interest method, less any identified impairment losses. An impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. Impairment losses are reversed in subsequent periods when an increase in the asset's recoverable amount can be related objectively to an event occurring after the impairment was recognised, subject to a restriction that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

4. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Financial liabilities and equity

Financial liabilities and equity instruments issued by a group entity are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument.

An equity instrument is any contract that evidences a residual interest in the assets of the group entity after deducting all of its liabilities. The Group's financial liability are generally classified into financial liabilities at fair value through profit or loss and other financial liabilities. The accounting policies adopted in respect of financial liabilities and equity instruments are set out below.

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss has two subcategories, including financial liabilities held for trading and those designated at fair value through profit or loss on initial recognition. At each balance sheet date subsequent to initial recognition, financial liabilities at fair value through profit or loss are measured at fair value, with changes in fair value recognised directly in profit or loss in the period in which they arise.

Other financial liabilities

Other financial liabilities, including bank borrowings and trade and other payables, are subsequently measured at amortised cost, using the effective interest method.

Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

Derivative financial instruments

The Group uses derivative financial instruments (primarily foreign exchange forward contracts) to hedge its exposure against foreign currency risk. Such derivatives are measured at fair value regardless of whether they are designated as effective hedging instruments.

Derivatives of the Group that do not qualify for hedge accounting are deemed as financial assets held for trading or financial liabilities held for trading. Changes in fair values of such derivatives are recognised directly in profit or loss.

DERECOGNITION

Financial assets are derecognised when the rights to receive cash flows from the assets expire or, the financial assets are transferred and the Group has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and the cumulative gain or loss that had been recognised directly in equity is recognised in profit or loss.

For financial liabilities, they are removed from the Group's balance sheet (i.e. when the obligation specified in the relevant contract is discharged, cancelled or expires). The difference between the carrying amount of the financial liability derecognised and the consideration received or receivable is recognised in profit or loss.

5. KEY SOURCES OF ESTIMATION UNCERTAINTY

In the process of applying the Group's accounting policies which are described in note 4, management has made the following estimation that have the most significant effect on the amounts recognised in the financial statements are discussed below.

DEPRECIATION AND AMORTISATION

The Group's carrying value of property, plant and equipment as at 31st December, 2005 was approximately US$65.1 million. The Group depreciates and amortises the property, plant and equipment over their estimated useful lives, and after taking into account their estimated residual value, using the straight line method at the rates as detailed in note 14. The estimated useful life reflects the directors' estimate of the periods that the Group intend to derive future economic benefits from the use of the Group's property, plant and equipment.

IMPAIRMENT LOSS ON TRADE RECEIVABLES

The policy for doubtful receivables of the Group is based on the on-going evaluation of the collectability and aging analysis of the trade receivables and on the management's judgements. A considerable amount of judgment is required in assessing the ultimate realisation of these receivables, including the current creditworthiness, and the past collection history of each customer and the present value of estimated future cash flows discounted at the effective interest rate. If the financial conditions of the customers are to deteriorate, resulting in an impairment of their ability to make payments, additional impairment loss may be required.

ALLOWANCES FOR INVENTORIES

The management of the Group reviews an inventories listing at each balance sheet date, and makes allowance for obsolete and slow-moving inventory items identified that are no longer suitable for use in production. The management estimates the net realisable value for such items based primarily on the latest invoice prices and current market conditions. The Group carries out an inventory review on a product-by-product basis at each balance sheet date and makes allowance for obsolete items.

FAIR VALUE ESTIMATION

The fair value of financial assets and financial liabilities is estimated by discounting the future cash flows at prevailing market rate available to the Group for similar financial investments. Such assessments are based on certain assumptions, which are subject to uncertainty and might materially differ from the actual results.

6. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's major financial instruments include bank balances, borrowings, trade receivables and trade payables. Details of these financial instruments are disclosed in respective notes. The risks associated with these financial instruments and the policies on how to mitigate these risks are set out below. The management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

CURRENCY RISK

Certain trade receivables, trade payables and borrowings of the Group are denominated in foreign currencies. The Group currently does not have a foreign currency hedging policy. However, the management monitors foreign exchange exposure and will enter into foreign currency forward contracts in order to mitigate the foreign currency risk.

CREDIT RISK

The Group's maximum exposure to credit risk in the event of the counterparties failure to perform their obligations as at 31st December, 2005 in relation to each class of recognised financial assets is the carrying amount of those assets as stated in the consolidated balance sheet.

The Group's concentration of credit risk by geographical locations is mainly concentrated in the United States of America, which accounted for approximately 62% (2004: 73%) of the turnover for the year ended 31st December, 2005.

The largest customer accounted for approximately 56% (2004: 58%) of the turnover and the five largest customers in aggregate accounted for approximately 87% (2004: 91%) of the turnover for the year ended 31st December, 2005.

At the balance sheet date, the five largest receivables balances accounted for approximately 88% (2004: 81%) of the trade receivables.

In order to minimise the credit risk, the management of the Group has delegated a team responsible for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual trade receivables at each balance sheet date to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the directors of the Company consider that the Group's credit risk is significantly reduced.

The credit risk on liquid funds is limited because the counter parties are banks with high credit-rating.

6. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

CASH FLOW INTEREST RATE RISK

All borrowings of the Group are arranged at floating rates. The Group currently does not have a hedging policy on interest rate risk. However, the management monitors interest rate exposure and will consider interest rate swap contracts should the need arises.

7. SEGMENT INFORMATION

Turnover represents the amounts received and receivable for goods sold by the Group to customers, less returns and allowances, during the year.

GEOGRAPHICAL SEGMENTS

For management purposes, the Group is currently organised into three major geographical segments based on the location of its customers. These segments are the bases on which the Group reports its primary segment information.

The following is an analysis of the Group's sales by geographical market, irrespective of the origin of the goods:

2005

	North America US$'000	Asia US$'000	Europe US$'000	Others US$'000	Consolidated US$'000
TURNOVER					
External sales	**87,313**	**20,550**	**24,464**	**8,915**	**141,242**
RESULTS					
Segment results	**9,724**	**2,289**	**2,724**	**991**	**15,728**
Other income					**859**
Unallocated corporate expenses					**(12,736)**
Share of results of associates	**–**	**181**	**–**	**–**	**181**
Share of results of jointly controlled entities	**–**	**(76)**	**–**	**–**	**(76)**
Interest on bank borrowings wholly repayable within five years					**(1,199)**
Profit before taxation					**2,757**
Taxation					**(290)**
Profit for the year					**2,467**

7. SEGMENT INFORMATION *(Continued)*

2005

	North America US$'000	Asia US$'000	Europe US$'000	Others US$'000	Consolidated US$'000
BALANCE SHEET					
ASSETS					
Segment assets	7,642	1,799	2,141	779	12,361
Interests in associates	–	1,012	–	–	1,012
Interests in jointly controlled entities	–	2,423	–	–	2,423
Unallocated corporate assets					130,293
Consolidated total assets					146,089
LIABILITIES					
Unallocated corporate liabilities and consolidated total liabilities					44,003

OTHER INFORMATION

	North America US$'000	Asia US$'000	Europe US$'000	Others US$'000	Consolidated US$'000
Impairment loss on trade receivables	364	–	–	–	364
Capital additions	2,687	632	753	274	4,346

7. SEGMENT INFORMATION *(Continued)*

2004

	North America *US$'000*	Asia *US$'000*	Europe *US$'000*	Others *US$'000*	Consolidated *US$'000* (restated)
TURNOVER					
External sales	104,615	23,392	10,200	5,497	143,704
RESULTS					
Segment results	10,443	2,335	1,019	548	14,345
Other income					1,156
Unallocated corporate expenses					(14,222)
Share of results of associates	–	313	–	–	313
Share of results of jointly controlled entities	–	64	–	–	64
Interest on bank borrowings wholly repayable within five years					(649)
Impairment loss and write-off in respect of an investment security					(2,328)
Loss before taxation					(1,321)
Taxation					421
Loss for the year					(900)

	North America *US$'000*	Asia *US$'000*	Europe *US$'000*	Others *US$'000*	Consolidated *US$'000* (restated)
BALANCE SHEET					
ASSETS					
Segment assets	8,626	1,929	841	453	11,849
Interests in associates	–	831	–	–	831
Interests in jointly controlled entities	–	2,499	–	–	2,499
Unallocated corporate assets					127,067
Consolidated total assets					142,246
LIABILITIES					
Unallocated corporate liabilities and consolidated total liabilities					43,817

7. SEGMENT INFORMATION *(Continued)*

2004

OTHER INFORMATION

	North America *US$'000*	Asia *US$'000*	Europe *US$'000*	Others *US$'000*	Consolidated *US$'000*
Impairment loss on trade receivables	362	–	–	–	362
Capital additions	3,690	825	360	194	5,069

The Group's operations are located in Mainland China (the "PRC"), Hong Kong and Taiwan.

The following is an analysis of the carrying amount of segment assets, and additions to property, plant and equipment, as analysed by the geographical area in which the assets are located:

	Carrying amount of segment assets		**Additions to property, plant and equipment**	
	2005	2004	**2005**	2004
	US$'000	*US$'000* (restated)	**US$'000**	*US$'000*
PRC	**108,584**	103,128	**4,341**	4,134
Hong Kong	**35,788**	37,907	**5**	911
Taiwan	**1,717**	1,211	**–**	24
	146,089	142,246	**4,346**	5,069

BUSINESS SEGMENTS

No analysis of financial information by business segment is presented as all the Group's turnover and trading results are generated from the manufacture and sale of footwear products.

8. PROFIT (LOSS) BEFORE TAXATION

	2005	2004
	US$'000	*US$'000*
		(restated)
Profit (loss) before taxation has been arrived at after charging:		
Directors' emoluments *(note 9)*	**802**	727
Other staff costs	**32,985**	31,458
Retirement benefits scheme contributions (excluding contributions in respect of directors)	**1,462**	1,188
Total staff costs	**35,249**	33,373
Depreciation of property, plant and equipment	**8,162**	8,421
Release of prepaid lease payments	**136**	101
Auditors' remuneration	**137**	96
Loss on disposal of property, plant and equipment	**101**	6
Impairment loss on trade receivables	**364**	362
Net foreign exchange losses	**29**	–
and after crediting:		
Interest income	**107**	76
Net foreign exchange gain	**–**	225

9. DIRECTORS' EMOLUMENTS

The emoluments paid or payable to each of the 9 (2004: 10) directors were as follows:

2005

	Wu Chen San, Thomas US$'000	Wu Jenn Chang, Michael US$'000	Wu Jenn Tzong, Jackson US$'000	Yang Chih Chieh, Arthur US$'000	Ho Chin Fa, Steven US$'000	Fang Yen Ling US$'000	Lai Jenn Yang, Jeffrey US$'000	Liu Chung Kang, Helios US$'000	Chang Ho Hsi US$'000	Total US$'000
Fees	24	12	12	12	12	8	4	8	4	96
Other emoluments										
Salaries and other benefits	198	167	71	74	97	–	–	–	–	607
Bonus	33	28	–	–	38	–	–	–	–	99
	255	207	83	86	147	8	4	8	4	802

2004

	Wu Chen San, Thomas *US$'000*	Wu Jenn Chang, Michael *US$'000*	Wu Jenn Tzong, Jackson *US$'000*	Yang Chih Chieh, Arthur *US$'000*	Ho Chin Fa, Steven *US$'000*	Yang Hui Kuan *US$'000*	Fang Yen Ling *US$'000*	Chang Ho Hsi *US$'000*	Liu Chung Kang, Helios *US$'000*	Sanford Kent Dawson *US$'000*	Total *US$'000*
Fees	24	12	12	12	12	6	8	2	2	6	96
Other emoluments											
Salaries and other benefits	206	172	48	12	100	–	–	–	–	–	538
Bonus	33	28	–	1	31	–	–	–	–	–	93
	263	212	60	25	143	6	8	2	2	6	727

The performance related incentive payment is determined with reference to the Group's operating results, individual performance and the comparable market statistics.

No directors waived any emoluments in the year ended 31st December, 2005 and 2004.

10. EMPLOYEES' EMOLUMENTS

The five highest paid individuals of the Group included 3 executive directors (2004: 3 executive directors) of the Company, whose emoluments are included in the disclosure in note 9 above. The emoluments of the two highest paid individual (2004: 2 employees), were as follows:

	2005	2004
	US$'000	*US$'000*
Basic salaries and allowances	**265**	256
Retirement benefits scheme contributions	**2**	2
	267	258

The emoluments of these highest paid employees were within the following bands:

	Number of employees	
	2005	2004
Nil to HK$1,000,000 (equivalent to Nil to US$129,032)	**1**	1
HK$1,000,001 to HK$1,500,000 (equivalent to US$129,033 to US$193,548)	**1**	1

11. TAXATION

	2005	2004
	US$'000	*US$'000*
Current taxation:		
Hong Kong	**9**	11
PRC	**256**	268
Taiwan	**27**	(2)
	292	277
Overprovision in prior years:		
Hong Kong	**(2)**	–
PRC	**–**	(7)
	(2)	(7)
Deferred taxation:		
Current year *(note 27)*	**–**	(691)
Taxation attributable to the Company and its subsidiaries	**290**	(421)

11. TAXATION *(Continued)*

Hong Kong Profits Tax is calculated at 17.5% of the estimated assessable profits for both years.

PRC income tax is charged at 27% or 33% on the assessable profits of the PRC subsidiaries. Pursuant to the relevant laws and regulations in the PRC, certain of the Company's PRC subsidiaries are eligible for certain tax holidays and concessions and were exempted from PRC income taxes.

Taxation arising in other jurisdictions is calculated at the rates prevailing in the relevant jurisdictions.

Save as disclosed above, in the opinion of the directors, the Group is not subject to taxation in any other jurisdictions.

Details of the deferred taxation are set out in note 27.

The tax charge (credit) for the year can be reconciled to the profit (loss) before taxation per the income statement as follows:

	2005	2004
	US$'000	*US$'000*
		(restated)
Profit (loss) before taxation	**2,757**	(1,321)
Tax at the domestic income tax rate of 33%	**910**	(436)
Tax effect of share of results of associates/jointly controlled entities	**(35)**	(124)
Tax effect of expenses not deductible for tax purpose	**1,145**	1,274
Tax effect of income not taxable for tax purpose	**(19)**	(1)
Overprovision in respect of prior years	**(2)**	(7)
Tax effect of tax losses/deferred tax assets not recognised	**742**	1,593
Effect of tax holidays and concessions granted to PRC subsidiaries	**(115)**	(51)
Tax effect on net income not taxable in any jurisdiction	**(2,321)**	(2,702)
Effect of different tax rates of subsidiaries operating in other jurisdictions	**(15)**	(10)
Others	**–**	43
Tax charge (credit) for the year	**290**	(421)

Note: The domestic tax rate in the jurisdiction where the operation of the Group is substantially based is used.

12. DIVIDENDS

	2005	2004
	US$'000	*US$'000*
2004 Interim, paid – HK1 cent per ordinary share	**–**	943
Final, proposed – HK1 cent (2004: Nil) per ordinary share	**943**	–
	943	943

For the year ended 31st December, 2005, the final dividend of HK1 cent per share had been proposed by the directors and was subject to approval by the shareholders in general meeting.

13. EARNINGS (LOSS) PER SHARE

The calculation of the basic earnings (loss) per share is based on the profit attributable to shareholders of the Company of approximately US$2,467,000 (2004: loss of approximately US$900,000) and on the weighted average number of 730,700,000 (2004: 730,700,000) ordinary shares in issue during the year.

No diluted earnings per share for the years ended 31st December, 2005 and 2004 have been presented because there are no potential ordinary shares outstanding.

The following table summarises the impact on basic earnings (loss) per share as a result of:

	2005	2004
	US cent	*US cent*
Reported figures before adjustments	**0.34**	(0.15)
Adjustments arising from changes in accounting policies *(see Note 3)*	**–**	0.03
	0.34	(0.12)

14. PROPERTY, PLANT AND EQUIPMENT

	Buildings	Construction in progress	Leasehold improvements	Plant and machinery	Furniture, fixtures and equipment	Motor vehicles	Total
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*
COST OR VALUATION							
At 1st January, 2004, as originally stated	47,632	126	1,468	82,835	14,305	910	147,276
Effect of changes in accounting policies *(note 2)*	(12,129)	–	–	–	–	–	(12,129)
At 1st January, 2004, as restated	35,503	126	1,468	82,835	14,305	910	135,147
Additions	146	1,067	10	3,356	386	104	5,069
Transfers	–	(29)	–	29	–	–	–
Disposals	–	–	(11)	–	(44)	–	(55)
Revaluation	(856)	–	–	–	–	–	(856)
At 31st December, 2004	34,793	1,164	1,467	86,220	14,647	1,014	139,305
Additions	32	1,302	5	2,773	214	20	4,346
Transfers	223	(2,416)	945	–	1,248	–	–
Disposals	–	–	–	(6)	(129)	(54)	(189)
Revaluation	772	–	–	–	–	–	772
At 31st December, 2005	35,820	50	2,417	88,987	15,980	980	144,234
Comprising:							
At cost	–	50	2,417	88,987	15,980	980	108,414
At valuation – December 2005	35,820	–	–	–	–	–	35,820
	35,820	50	2,417	88,987	15,980	980	144,234
DEPRECIATION							
At 1st January, 2004	–	–	1,463	51,476	10,638	766	64,343
Provided for the year	848	–	2	6,569	935	67	8,421
Eliminated on disposals	–	–	(7)	–	(27)	–	(34)
Eliminated on revaluation	(848)	–	–	–	–	–	(848)
At 31st December, 2004	–	–	1,458	58,045	11,546	833	71,882
Provided for the year	858	–	83	6,391	775	55	8,162
Eliminated on disposals	–	–	–	–	(34)	(54)	(88)
Eliminated on revaluation	(858)	–	–	–	–	–	(858)
At 31st December, 2005	–	–	1,541	64,436	12,287	834	79,098
CARRYING VALUES							
At 31st December, 2005	35,820	50	876	24,551	3,693	146	65,136
At 31st December, 2004	34,793	1,164	9	28,175	3,101	181	67,423

Property, plant and equipment are depreciated at the following rates per annum:

Buildings	2%
Leasehold improvements	20%
Plant and machinery	10%-20%
Furniture, fixtures and equipment	20%-$33^1/_3$%
Motor vehicles	20%

14. PROPERTY, PLANT AND EQUIPMENT *(Continued)*

The buildings and the construction in progress are situated in the PRC.

The buildings were revalued as at 31st December, 2005 by Messrs. RHL Appraisal Limited, on a depreciated replacement cost basis. Messrs. RHL Appraisal Limited are not connected with the Group. Messrs. RHL Appraisal Limited are members of the Institute of Valuers and have appropriate qualification and recent experiences in valuation of similar properties. The valuation, which conforms to International Valuation Standards, was arrived at reference to market evidence transaction prices of similar transaction.

If the buildings in the PRC had not been revalued, they would have been included in these financial statements at historical cost less accumulated depreciation as follows:

	2005	2004
	US$'000	*US$'000*
Cost at the end of the year	**36,127**	35,872
Accumulated depreciation	**(6,002)**	(5,253)
Net book value at the end of the year	**30,125**	30,619

15. PREPAID LEASE PAYMENTS

	2005	2004
	US$'000	*US$'000*
The Group's prepaid lease payments comprise land use rights in the PRC under medium-term lease	**5,532**	5,668
Analysed for reporting purpose as:		
Current asset	**136**	136
Non-current assets	**5,396**	5,532
	5,532	5,668

16. INTERESTS IN ASSOCIATES

	2005	2004
	US$'000	*US$'000*
Cost of unlisted investments in associates	**400**	400
Share of post-acquisition profits	**612**	431
	1,012	831
Amount due from an associate	**8**	14

The amount due from an associate is unsecured, interest-free, and repayable on demand. Its fair value approximates to the corresponding carrying amount.

Particulars of the Group's associates at 31st December, 2005 are as follows:

Name of associate	Form of business structure	Place of incorporation/ establishment	Principal place of operation	Issued and fully paid share capital/ registered capital	Proportion of nominal value of issued share capital indirectly held by the Company	Principal activities
Hi-Tech Pacific Limited	Private limited company	British Virgin Islands	Hong Kong	Ordinary US$1,000,000	40%	Trading in footwear and investment holding
廣州和仁化學塑料有限公司	Wholly-owned foreign enterprise	PRC	PRC	Registered capital US$500,000	40%	Manufacturing of footwear materials

16. INTERESTS IN ASSOCIATES *(Continued)*

The summarised financial information in respect of the Group' associates is set out below:

	2005	2004
	US$'000	*US$'000*
Total assets	**2,776**	2,639
Total liabilities	**(247)**	(560)
Net assets	**2,529**	2,079
Group's share of net assets of associates	**1,012**	831
Revenue	**4,807**	4,158
Profit for the year	**452**	783
Group's share of results of associates for the year	**181**	313

17. INTERESTS IN JOINTLY CONTROLLED ENTITIES

	2005	2004
	US$'000	*US$'000*
Cost of unlisted investments in jointly controlled entities	**2,400**	2,400
Share of post-acquisition profits	**23**	99
	2,423	2,499

Particulars of the Group's principal jointly controlled entity at 31st December, 2005 are as follows:

Name of associate	**Form of business structure**	**Place of incorporation/ establishment**	**Principal place of operation**	**Issued and fully paid share capital/ registered capital**	**Proportion of nominal value of issued share capital indirectly held by the Company**	**Principal activities**
C.P.L. International Company Limited	Private limited company	British Virgin Islands	Hong Kong	Ordinary US$8,000,000	30%	Investment holding
C.P.L. International (H.K.) Company Limited	Private limited company	Hong Kong	Hong Kong	Ordinary HK$10,000	30%	Investment holding
C.P.L. Marketing Companies Limited	Private limited company	British Virgin Islands	Hong Kong	Ordinary US$1	30%	Provision of administrative services
Sunshine Leather Industrial Limited	Wholly-owned foreign enterprise	PRC	PRC	Registered capital US$1,000,000	30%	Manufacture of leather materials
Rich Pine Investments Limited	Private Limited Company	British Virgin Islands	Hong Kong	Ordinary US$50,000	30%	Marketing of leather materials

17. INTERESTS IN JOINTLY CONTROLLED ENTITIES *(Continued)*

The summarised financial information in respect of the Group' jointly controlled entitles is set out below:

	2005	2004
	US$'000	*US$'000*
Total assets	**16,354**	18,435
Total liabilities	**(8,277)**	(10,105)
Net assets	**8,077**	8,330
Group's share of net assets of jointly controlled entities	**2,423**	2,499
Revenue	**20,914**	21,226
(Loss) profit for the year	**(253)**	213
Group's share of results of jointly controlled entities for the year	**(76)**	64

18. INVESTMENT SECURITY

	2005	2004
	US$'000	*US$'000*
Listed equity securities	**–**	4,821
Impairment loss recognised	**–**	(2,493)
Write-off of investment security	**–**	(2,328)
	–	–

The investment security of approximately US$2,328,000 at 1st January, 2004 represented investment in Secaicho Corporation ("Secaicho"), a company incorporated in Japan. The investment represented a holding of 23.83% of the ordinary shares of Secaicho. Secaicho ceased to be an associate of the Company after its corporate reorganisation since 30th July, 2003.

On 17th September, 2004, the corporate reorganisation of Secaicho, approved by the Osaka Court in Japan, was confirmed. Pursuant to the court order and subsequent to the capital reduction, the then existing shareholders experienced a loss in the legal ownership of Secaicho and no compensation would be made to the then existing shareholders of Secaicho. Accordingly, the directors determined to write off the remaining carrying amount of investment in Secaicho of approximately US$2,328,000 in the income statement for the year ended 31st December, 2004.

19. INVENTORIES

	2005	2004
	US$'000	*US$'000*
Raw materials	**33,033**	31,023
Work in progress	**5,952**	7,810
Finished goods	**6,834**	6,212
	45,819	45,045

At the balance sheet date, all inventories were carried at cost.

20. TRADE AND OTHER RECEIVABLES

The Group allows an average credit period of 30 to 60 days to its trade customers. The following is an aged analysis of the Group's trade receivables at the balance sheet date:

	2005	2004
	US$'000	*US$'000*
0-30 days	**10,529**	10,311
31-60 days	**1,316**	952
over 60 days	**516**	586
Total trade receivables	**12,361**	11,849
Other receivables	**1,273**	3,225
	13,634	15,074

The fair value of Group's trade and other receivables as at 31st December, 2005 approximates to the corresponding carrying amount.

21. BANK BALANCES AND CASH

Bank balances and cash comprises cash held by the Group and short-term bank deposits that are interest bearing and have original maturity of three months or less. The carrying amount of these assets approximates to their fair value.

The bank balances and cash of the Group are mainly denominated in United States dollars, Renminbi and Hong Kong dollars. Included in the bank balances and cash as at 31st December, 2005 was amount in Renminbi of RMB11,917,000 (2004: RMB23,105,000). Renminbi is not freely convertible into other currencies.

22. TRADE AND OTHER PAYABLES

The following is an aged analysis of the Group's trade payables at the balance sheet date:

	2005	2004
	US$'000	US$'000
0-30 days	**3,991**	3,054
31-60 days	**361**	811
Over 60 days	**574**	283
Total trade payables	**4,926**	4,148
Other payables	**6,738**	7,557
	11,664	11,705

The fair value of Group's trade and other payables as at 31st December, 2005 approximates to the corresponding carrying amount.

23. UNSECURED BANK BORROWINGS

	2005	2004
	US$'000	US$'000
Bank loans	**28,477**	27,748
Trust receipt loans	**1,336**	2,695
	29,813	30,443
Carrying amount repayable:		
On demand or within one year	**16,458**	17,073
More than one year, but not exceeding two years	**9,480**	10,165
More than two years, but not exceeding three years	**3,875**	3,205
	29,813	30,443
Less: Amounts due within one year shown under current liabilities	**(15,858)**	(17,073)
	13,955	13,370

23. UNSECURED BANK BORROWINGS *(Continued)*

The Group has variable-rate borrowings which carry interest at LIBOR plus a fixed percentage. Interest is repriced every three months.

The ranges of effective interest rates (which are also equal to contracted interest rates) on the Group's borrowings are as follows:

	2005	2004
Effective interest rate:		
Variable-rate borrowings	**3.17% to 5.43%**	1.11% to 3.46%

The currencies in which the Group's bank borrowings are denominated are set out below:

	2005	2004
	US$'000	*US$'000*
Hong Kong dollar	**–**	503
Euro dollar	**–**	605
Taiwan dollar	**788**	–
US Dollar	**29,025**	29,335
	29,813	30,443

The fair value of the Group's borrowings estimated by discounting their future cash flows at the prevailing market rates at the balance sheet date for similar borrowings approximates to their carrying amount.

24. DERIVATIVE FINANCIAL INSTRUMENTS

The Group uses derivative financial instruments (primarily foreign currency forward contracts) to manage its risks associated with foreign currency fluctuations relating to certain firm commitments and forecasted transactions.

The Group utilises currency derivatives to manage future transactions and cash flows. The Group is a party to foreign currency forward contracts in the management of its exchange rate exposures. The instruments purchased during the year were denominated in United Stated dollars and Renminbi. At the balance sheet date, the Group had nine foreign currency forward contracts with a total nominal amount of US$12.0 million outstanding, each with an exercisable period of one month. These contracts will expire from January 2006 to October 2006.

The foreign currency derivatives contracts are measured at fair value at each balance sheet date. Their fair values are determined based on the quoted market prices for equivalent instruments at the balance sheet date. The fair value of the currency derivatives at balance sheet is insignificant.

25. SHARE CAPITAL

	Number of shares	Amount
		US$'000
Authorised		
Ordinary shares of HK$0.10 each		
At 1st January, 2004, 31st December, 2004 and 31st December, 2005	1,500,000,000	19,355
Convertible non-voting preference shares of US$100,000 each (note)		
At 1st January, 2004, 31st December, 2004 and 31st December, 2005	150	15,000
		34,355

	Number of shares		Amount	
	2005	2004	**2005**	2004
	'000	*'000*	**US$'000**	*US$'000*
Issued and fully paid				
Ordinary shares of HK$0.10 each	**730,700**	730,700	**9,428**	9,428

Note: Convertible non-voting preference shares, when issued and outstanding, carry fixed cumulative dividend. Under certain circumstances, they are entitled to additional dividend and are convertible into shares of the Company.

26. SHARE OPTION SCHEME

The Company's share option scheme (the "Scheme") was adopted pursuant to a resolution passed on 25th September, 1996 for the primary purpose of providing incentives to directors and eligible employees and will be expired on 24th September, 2006. Under the Scheme, the board of directors of the Company may offer to any director or employee of the Company, or any of its subsidiaries, options to subscribe for shares in the Company.

Without prior approval from the Company's shareholders, the total number of shares in respect of which options may be granted under the Scheme is not permitted to exceed 10% of the shares of the Company in issue at any point in time, and the number of shares in respect of which options may be granted to any individual in any one year is not permitted to exceed 1% of the shares of the Company in issue at any point in time.

No consideration is payable on the grant of an option. Options may be exercised at any time for a period of three years commencing on the first anniversary of the date of grant. The exercise price of the option shares would be at a price equal to the higher of the nominal value of the shares and 80% of the average of the closing prices of the shares of the Company on The Stock Exchange of Hong Kong Limited on the five trading days immediately preceding the date of the offer to grant an option.

During the years ended 31st December, 2005 and 2004, no share options were granted or exercised.

At 31st December, 2005 and 2004, no share options were outstanding under the Scheme.

27. DEFERRED TAXATION

The following are the major deferred tax liabilities (assets) recognised and movements thereon during the current and prior years:

	Revaluation of buildings in the PRC	Accelerated accounting depreciation	Total
	US$'000	*US$'000*	*US$'000*
At 1st January, 2004, as originally stated	4,042	–	4,042
Effect of changes in accounting policies	(1,709)	–	(1,709)
At 1st January, 2004, as restated	2,333	–	2,333
Credit to equity	(2)	–	(2)
Charge to income statement	–	(691)	(691)
At 31st December, 2004, as restated and 1st January, 2005	2,331	(691)	1,640
Charge to equity	440	–	440
At 31st December, 2005	2,771	(691)	2,080

For the purpose of balance sheet presentation, the above deferred assets and liabilities have been offset.

At the balance sheet date, the Group had unutilised tax losses of approximately US$5,119,000 (2004: US$4,664,000) available for offset against future profits and deductible temporary difference of approximately US$11,519,000 (2004: US$9,733,000) in respect of accelerated accounting depreciation. No deferred tax assets have been recognised in respect of unutilised tax losses due to the unpredictability of future profit streams. Included in unrecognised tax losses are losses of US$2,333,000 (2004: US$1,895,000) that will expire in 2007 to 2011 (2004: 2007 to 2010). Other losses may be carried forward indefinitely.

28. CONTINGENT LIABILITIES

	2005	2004
	US$'000	*US$'000*
Discounted bills with recourse	**–**	107

29. OPERATING LEASE COMMITMENTS

THE GROUP AS LESSEE

	2005	2004
	US$'000	*US$'000*
Minimum lease payment paid by the Group under operating leases during the year in respect of:		
Minimum lease payments	**688**	612
Contingent rent	**1,153**	1,132
	1,841	1,744

At the balance sheet dates, the Group had commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

	2005	2004
	US$'000	*US$'000*
Within one year	**336**	616
In the second to fifth year inclusive	**137**	435
Over five years	**954**	928
	1,427	1,979

Operating lease payments represent rentals payable by the Group for its factories and office premises. Leases are negotiated for an average term of two years and rentals are fixed for an average term of two years.

In addition to the above, the Group had commitments for future minimum lease payments under non-cancellable operating leases in respect of certain outlets which are based on a fixed percentage of the annual gross turnover of the outlets.

30. CAPITAL COMMITMENTS

	2005	2004
	US$'000	*US$'000*
Capital expenditure in respect of the acquisition of property, plant and equipment contracted for but not provided in the financial statements	**159**	–

31. RETIREMENT BENEFITS SCHEMES

The Group operates a Mandatory Provident Fund Scheme for all qualifying employees in Hong Kong. The assets of the schemes are held separately from those of the Group in funds under the control of trustees. The Group contributes 5% of relevant payroll costs to the scheme, which contribution is matched by employees.

The employees of the Group's subsidiaries in the PRC are members of a state-managed retirement benefits scheme operated by the government of the PRC. These subsidiaries are required to contribute 11% of payroll costs to the retirement benefits scheme to fund the benefits. The only obligation of the Group with respect to the retirement benefits scheme is to make the specified contributions.

32. RELATED PARTY DISCLOSURES

(I) RELATED PARTY TRANSACTIONS

During the year, the Group had entered into the following transactions with its related parties:

Nature of transactions	2005 US$'000	2004 US$'000
Sales by the Group to Secaicho	–	4,819
Purchases by the Group from Secaicho	–	25
Purchases by the Group from an associate	**509**	850
Purchases by the Group from a jointly controlled entity	**1,334**	954

(II) REMUNERATION OF KEY MANAGEMENT PERSONNEL

The remuneration of directors and other members of key management during the year was as follows:

	2005 US$'000	2004 US$'000
Short term benefits	**1,467**	1,399
Other long term benefits	**2**	2
	1,469	1,401

The remuneration of directors and key executives is determined with reference to the Group's operating results, individual performance and comparable market statistics.

(III) RELATED PARTY BALANCES

Details of the balances with the associates as at respective balance sheet dates are set out in the consolidated balance sheet and note 16.

(IV) BANKING FACILITIES

At 31st December, 2005, certain banking facilities were secured by the guarantees jointly given by Mr. Wu Jenn Chang, Michael, a director of the Company, and his father Mr. Wu Suei to the extent of approximately US$788,000. The banking facilities was cancelled on 21st March, 2006.

33. BALANCE SHEET OF THE COMPANY

	2005	2004
	US$'000	*US$'000*
Non-current assets		
Interests in subsidiaries	**26,465**	52,194
Current assets		
Other receivables	**39**	9
Amounts due from subsidiaries	**25,286**	–
Dividend receivable from a subsidiary	**2,000**	2,000
Bank balances and cash	**3**	24
	27,328	2,033
Current liabilities		
Other payables	**38**	67
Net current assets	**27,290**	1,966
	53,755	54,160
Capital and reserves		
Share capital	**9,428**	9,428
Reserves *(note)*	**44,327**	44,732
	53,755	54,160

33. BALANCE SHEET OF THE COMPANY *(Continued)*

Note:

Reserves

	Share premium *US$'000*	Contributed surplus *US$'000*	Dividend reserve *US$'000*	Accumulated profits *US$'000*	Total *US$'000*
At 1st January, 2004	21,644	19,486	1,414	5,264	47,808
Loss for the year	–	–	–	(719)	(719)
Dividends paid for 2003	–	–	(1,414)	–	(1,414)
Dividends declared for 2004	–	–	943	(943)	–
Dividends paid for 2004	–	–	(943)	–	(943)
At 31st December, 2004	21,644	19,486	–	3,602	44,732
Loss for the year	–	–	–	(405)	(405)
Dividends declared for 2005	–	–	943	(943)	–
At 31st December, 2005	21,644	19,486	943	2,254	44,327

The contributed surplus of the Company represents the difference between the value of the underlying net assets of the subsidiaries acquired by the Company and the nominal amount of the share capital issued by the Company under a corporate reorganisation undertaken in 1996.

34. PRINCIPAL SUBSIDIARIES

Particulars of the Company's principal subsidiaries as at 31st December, 2005 are as follows:

Name of subsidiary	Place of establishment/ operations	Issued and fully paid share capital/ registered capital	Attributable equity interest held by the Company Directly	Indirectly	Principal activities
W.P.T. Development Inc.	British Virgin Islands/Hong Kong	Ordinary US$8	100%	–	Investment holding
Pacific Footgear Corporation	British Virgin Islands/Hong Kong	Ordinary US$1	–	100%	Marketing and trading in footwear
Wuco Corporation	British Virgin Islands/Hong Kong	Ordinary US$8	–	100%	Trading in footwear and investment holding
Nagano Management Limited	British Virgin Islands/Hong Kong	Ordinary US$11	–	100%	Investment holding
Topstair International (H.K.) Company Limited	Hong Kong	Ordinary HK$10,000	–	100%	Provision of administrative services to group companies
Pan Yu Fang Chun Footwear Co., Ltd.* 番禺豐群鞋業有限公司	PRC	Registered Capital US$10,600,000	–	100%	Manufacture of footwear and footwear materials
Panyu Pegasus Footwear Co. Ltd.* 番禺創信鞋業有限公司	PRC	Registered Capital US$31,100,000	–	100%	Manufacture of footwear and footwear materials
台灣松鄴國際有限公司	Taiwan	Registered Capital NT$5,000,000	–	100%	Trading in raw materials of footwear
廣州創信鞋業品服飾有限公司*	PRC	Registered Capital RMB1,000,000	–	100%	Marketing and trading in footwear in the PRC

* *These subsidiaries are established in the PRC as wholly-owned foreign enterprises.*

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

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

FINANCIAL SUMMARY

RESULTS

	Year ended 31st December,				
	2001	2002	2003	2004	**2005**
	US$'000	*US$'000*	*US$'000*	*US$'000* (restated)	**US$'000**
Turnover	127,838	115,405	129,552	143,704	**141,242**
Profit (loss) before taxation	7,674	5,715	4,389	(1,321)	**2,757**
Taxation	(163)	(223)	(172)	421	**(290)**
Profit (loss) for the year	7,511	5,492	4,217	(900)	**2,467**

ASSETS AND LIABILITIES

	At 31st December,				
	2001	2002	2003	2004	**2005**
	US$'000	*US$'000*	*US$'000*	*US$'000* (restated)	**US$'000**
Total assets	151,809	162,864	161,701	142,246	**146,089**
Total liabilities	48,671	59,652	55,358	43,817	**44,003**
Shareholders' funds	103,138	103,212	106,343	98,429	**102,086**
Minority interests	1	1	1	–	**–**
Shareholders' funds	103,139	103,213	106,344	98,429	**102,086**

The above financial summary prior to 2003 has not been adjusted to take into account the effect on the adoption of new Hong Kong Financial Reporting Standards issued by Hong Kong Institute of Certified Public Accountants, as detailed in note 2 to the financial statements, as the directors considered that it is not practicable to do so.