FONG'S INDUSTRIES COMPANY LIMITED

(Incorporated in Bermuda with limited liability)

(Stock Code : 641)

Annual Report 2006

CORPORATE INFORMATION

EXECUTIVE DIRECTORS

Mr. Fong Sou Lam *(Chairman)*
Mr. Wan Wai Yung *(Managing Director)*
Mr. Fong Kwok Leung, Kevin
Mr. Fong Kwok Chung, Bill
Mr. Tsui Wai Keung
Dr. Tsui Tak Ming, William
Ms. Poon Hang Sim, Blanche
Mr. Tou Kit Vai

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Cheung Chiu Fan
Dr. Yuen Ming Fai
Dr. Keung Wing Ching

COMPANY SECRETARY

Mr. Lee Che Keung

AUTHORISED REPRESENTATIVES

Mr. Fong Sou Lam
Mr. Fong Kwok Chung, Bill

QUALIFIED ACCOUNTANT

Ms. Poon Hang Sim, Blanche

AUDIT COMMITTEE

Mr. Cheung Chiu Fan *(Committee Chairman)*
Dr. Yuen Ming Fai
Dr. Keung Wing Ching

REMUNERATION COMMITTEE

Mr. Fong Sou Lam *(Committee Chairman)*
Mr. Wan Wai Yung
Mr. Cheung Chiu Fan
Dr. Yuen Ming Fai
Dr. Keung Wing Ching

SOLICITORS

Richards Butler
Gallant Y. T. Ho & Co.

AUDITORS

Deloitte Touche Tohmatsu

PRINCIPAL BANKERS

Standard Chartered Bank (Hong Kong) Limited
The Hongkong and Shanghai Banking Corporation Limited
Hang Seng Bank Limited
Bank of China (Hong Kong) Limited
The Bank of East Asia Limited
DBS Bank (Hong Kong) Limited

BERMUDA PRINCIPAL REGISTRARS AND TRANSFER OFFICE

Butterfield Fund Services (Bermuda) Limited
Rosebank Centre,
11 Bermudiana Road,
Hamilton,
Bermuda

HONG KONG BRANCH REGISTRARS AND TRANSFER OFFICE

Secretaries Limited
26th Floor, Tesbury Centre,
28 Queen's Road East,
Hong Kong

REGISTERED OFFICE

Canon's Court,
22 Victoria Street,
Hamilton HM12, Bermuda

HEAD OFFICE AND PRINCIPAL PLACE OF BUSINESS

8th Floor,
22-28 Cheung Tat Road,
Tsing Yi,
Hong Kong
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WEBSITE ADDRESS

http://www.fongs.com

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CHAIRMAN'S STATEMENT

On behalf of Fong's Industries Company Limited (the "Company", together with its subsidiaries, the "Group"), I am pleased to present the Group's annual results for the year ended December 31, 2006.

For the year under review, the Group achieved a 18% growth in consolidated revenue to approximately HK$2,380 million (2005: HK$2,012 million) and a 19% increase in profit attributable to shareholders to approximately HK$260 million (2005: HK$219 million) despite the delays in the turnaround of the European divisions and the addition of Goller Textilmaschinen GmbH for the textile machinery division during the year. In particular, the Group's overall results were aided by the strong performances in its other divisions of stainless steel trading, stainless steel casting and the Joint Venture of Monforts Fong's Textile Machinery Co. Limited.

Looking ahead, firstly, it is clear stringent laws and regulations as well as awareness of environmental protection in most countries worldwide, including such major markets as China and India, will be enforced onto the textile industry. Although this has caused some volatility in machinery sales during the year under review, we nevertheless expect that the demand for the latest and more technologically environmentally friendly dyeing and finishing machines will increase to support the sales growth of our core business.

Secondly, it appears that the global textile price deflation over the recent years as a result of unraveling of the quota system has run its course and that global textile prices have now stabilized and there are even signs of increase in certain regions. Consequently, the textile industry worldwide, and in particularly Asia, is expected to be much healthier and profitable which should help induce continued investments of textile machinery in the foreseeable future.

Thirdly, during the past years, the gradual consolidation in the dyeing and finishing machinery industry has been taking place due to the inability of smaller players to match the ever-increasing demand for product quality, technology, price and scale. In contrast, the Group has seized market opportunities that arose by capitalizing on its strong balance sheet and thus making acquisitions and to further invest in research and development ("R & D"). And to further ensure the medium to long-term R & D capabilities of the Group, during the year the Group donated HK$15 million to the Hong Kong University of Science and Technology to support the University as well as to further strengthen our mutual research projects by establishing the "Fong's Institute of Advanced Materials and Processing". The donation will be matched 2 to 1 by the Government under the Third Matching Grant Scheme.

CHAIRMAN'S STATEMENT

In addition, the Group will further leverage on its resources and strategy for offering a one-stop-shop business model which covers R & D and manufacturing and sales of a wide spectrum of textile machinery ranging from yarn treatment to dyeing and finishing. Our strong and well established brands of "**FONG'S**", "**THEN**", "**GOLLER**" and "**XORELLA**" coupled with an extensive client base and sales and service network have enabled us to maintain and to further expand our market leadership position in the textile machinery industry over the years.

And given that the Group anticipates the continued growth of our businesses, the Board has decided that a new production plant located within Guangdong Province will be actively planned and constructed once an appropriate site can be secured. Consequently, as part of this planning, on 10 May 2006 the Company successfully issued HK$800 million zero coupon convertible bonds due 2011.

The directors are confident of the Group's future development and growth. We are committed to seizing the opportunities in the industry to solidify our leadership and to achieving new business heights through continuous innovation and bringing added value to both customers and shareholders.

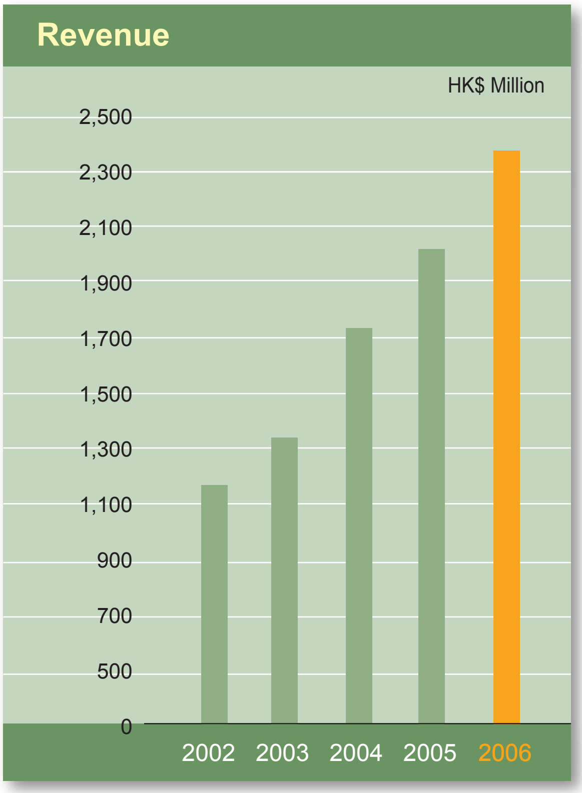
APPRECIATION

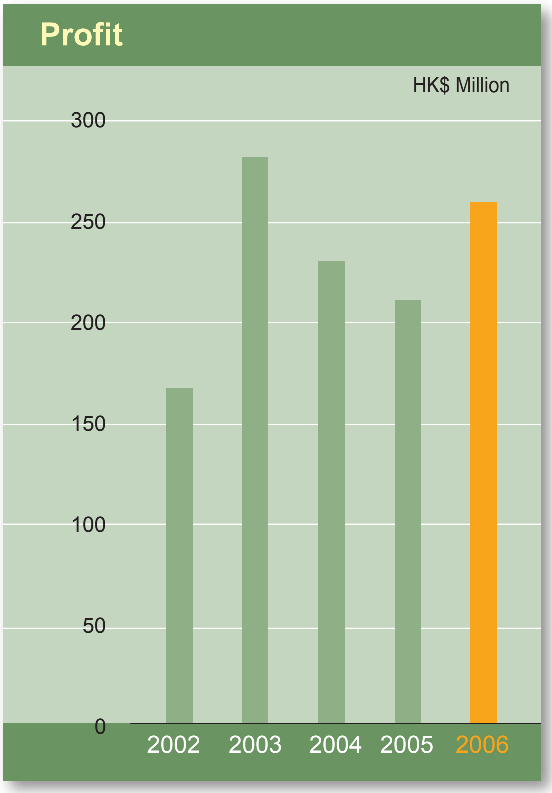
Finally, I would like to take this opportunity to express my sincere gratitude to all members of the Group for their invaluable contribution, diligence and loyalty over the past year. A final word of thanks goes to our customers, suppliers, business partners, bankers and shareholders for all their ongoing trust and support.

Fong Sou Lam
Chairman

Hong Kong, April 16, 2007

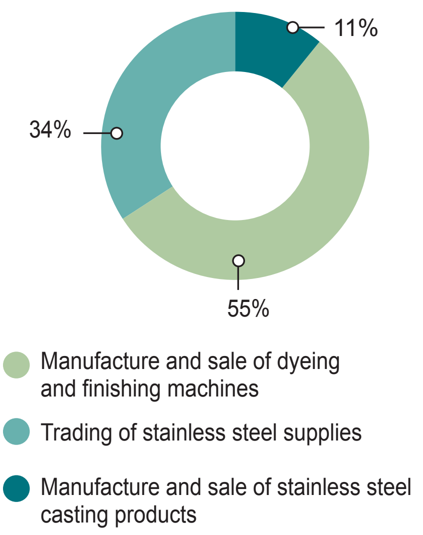
FINANCIAL HIGHLIGHTS



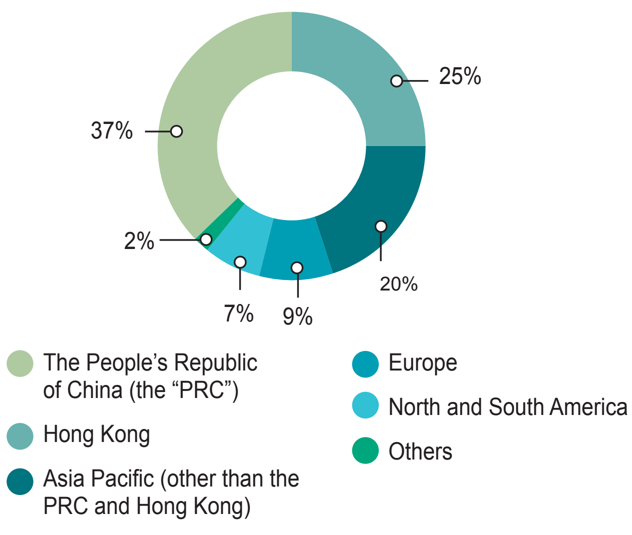


ANALYSIS OF REVENUE FOR THE YEAR

By principal activity



By geographical region



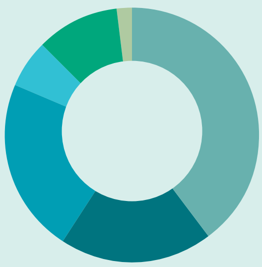
FINANCIAL HIGHLIGHTS

Revenue by Business Segment (HK$ Million)

Manufacture and Sale of Dyeing and Finishing Machines

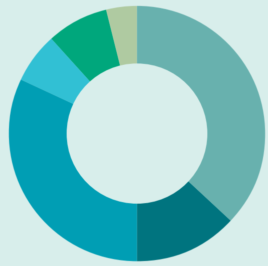
By geographical region

2005



PRC	462
Hong Kong	228
Asia Pacific	258
Europe	72
North and South America	123
Others	20

2006

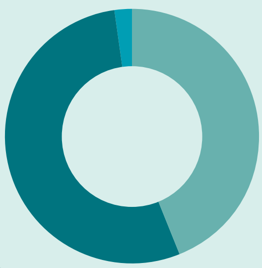


PRC	486
Hong Kong	173
Asia Pacific	420
Europe	81
North and South America	103
Others	50

Trading of Stainless Steel Supplies

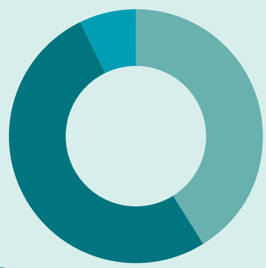
By geographical region

2005



PRC	284
Hong Kong	349
Asia Pacific	14

2006

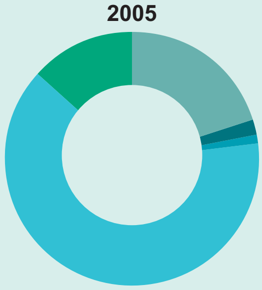


PRC	333
Hong Kong	418
Asia Pacific	58

Manufacture and Sale of Stainless Steel Casting Products

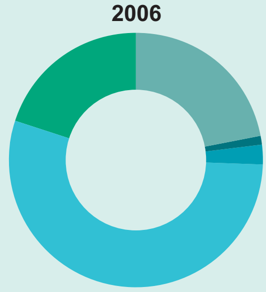
By geographical region

2005



PRC	41
Hong Kong	4
Asia Pacific	2
Europe	129
North and South America	27

2006



PRC	57
Hong Kong	3
Asia Pacific	6
Europe	141
North and South America	51

DIRECTORS AND SENIOR MANAGEMENT PROFILE

EXECUTIVE DIRECTORS

Mr. Fong Sou Lam, aged 72, is the founder and Chairman of the Group. Mr. Fong established the dyeing and finishing machine manufacturing business in 1963 and has over 40 years of business experience in that industry. Mr. Fong is responsible for formulating and implementing the overall corporate directions, corporate strategies and policies of the Group. Mr. Fong is also the Chairman of the Remuneration Committee of the Company. Mr. Fong is the father of Mr. Fong Kwok Leung, Kevin and Mr. Fong Kwok Chung, Bill.

Mr. Wan Wai Yung, aged 56, is the Managing Director and a member of the Remuneration Committee of the Company. Mr. Wan is responsible for the overall supervision of the Group's operations and assisting the Chairman in strategic planning and business development. Mr. Wan first joined the Group in 1978 and has over 20 years of experience with excellent customer relationships in the textile and dyeing industry.

Mr. Fong Kwok Leung, Kevin, aged 45, is the eldest son of Mr. Fong Sou Lam and joined the Group in 1986. Mr. Kevin Fong has been involved in the business of stainless steel trading since 1988 and is currently responsible for overseeing the stainless steel trading and stainless steel casting businesses of the Group. Mr. Kevin Fong holds a Bachelor's degree in Business Administration from the Simon Fraser University, Canada.

Mr. Fong Kwok Chung, Bill, aged 37, is the second son of Mr. Fong Sou Lam and joined the Group in 1994. Mr. Bill Fong is responsible for overseeing business development projects of the Group. In addition, since October 2005, Mr. Bill Fong has been responsible for the European operations of the overseas subsidiaries of the Group. Mr. Bill Fong studied at the Simon Fraser University, Canada with concentration on Accounting and Finance.

Mr. Tsui Wai Keung, aged 49, is responsible for the operation management of the Group's production base in Shenzhen, the PRC. Mr. Tsui joined the Group in 1980 and has over 25 years of extensive experience in dyeing and finishing machinery manufacturing.

Dr. Tsui Tak Ming, William, aged 48, is a chartered engineer and chartered I.T. professional, and he is in charge of the research & development team of the Group. Dr. Tsui holds a bachelor of science degree and a doctorate degree in Aeronautical Engineering and is a corporate member of the British Royal Aeronautical Society and a member of the Institution of Mechanical Engineers in the United Kingdom, the Hong Kong Institution of Engineers, the Hong Kong Computer Society and the British Computer Society. Dr. Tsui joined the Group in 1989 and has over 25 years of experience in research and development on mechanical engineering and information technology.

DIRECTORS AND SENIOR MANAGEMENT PROFILE

Ms. Poon Hang Sim, Blanche, aged 40, is the Finance Director and Qualified Accountant of the Group. Ms. Poon is responsible for overseeing the overall corporate financial management of the Group. Ms. Poon holds a Bachelor's degree in Commerce from the University of New South Wales, Australia and is an associate member of the Hong Kong Institute of Certified Public Accountants and a CPA, Australia. Before joining the Group in 1995, Ms. Poon had been working for an international accounting firm for five years.

Mr. Tou Kit Vai, aged 44, joined the Group in October, 2005 and was appointed an executive director of the Company by the Board with effect from 15 January, 2007. Mr. Tou is also directors of certain subsidiaries and associates of the Group, he is responsible for the general financial management of the Group. Mr. Tou is a fellow member of the Hong Kong Institute of Certified Public Accountants and The Association of Chartered Certified Accountants, he has extensive experiences in business operations, financial management, project management and internal audit.

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Cheung Chiu Fan, aged 53, has been appointed as an Independent Non-executive Director of the Company since August 1996. Mr. Cheung is also the Chairman of the Audit Committee and a member of the Remuneration Committee of the Company. Mr. Cheung is a professional accountant with extensive experience in public accounting and professional management. Mr. Cheung holds a Master degree in Business Administration from the Chinese University of Hong Kong and is a fellow member of the Association of Chartered Certified Accountants and an associate member of the Hong Kong Institute of Chartered Secretaries.

Dr. Yuen Ming Fai, aged 56, as been appointed as an Independent Non-executive Director of the Company since September 2004. Dr. Yuen is also a member of the Audit Committee and Remuneration Committee of the Company. Dr. Yuen is currently the Director of Technology Transfer Center at the Hong Kong University of Science and Technology and a Professor in Mechanical Engineering. Dr. Yuen holds a doctorate degree in Mechanical Engineering from the University of Bristol, the United Kingdom and is a fellow member of both the Institution of Mechanical Engineers (UK) and Hong Kong Institution of Engineers.

Dr. Keung Wing Ching, aged 56, has been appointed as an Independent Non-executive Director, a member of the Audit Committee and Remuneration Committee of the Company by the Board with effect from 1 June, 2006. Dr. Keung holds a Ph.D. in Mechanical Engineering from the University of Birmingham (United Kingdom). Dr. Keung is a fellow member of the Hong Kong Institution of Engineers and a professional member and chartered engineer of the institute of Materials, Minerals and Mining (United Kingdom). Dr. Keung has served and presently still serves on various public and community bodies including Permanent Honorary Chairman of the Hong Kong Diecasting Association, Permanent Honorary Chairman of the Hong Kong Foundry Association, Committee Member of the Hong Kong Q Mark Council and Member of Standing Provincial Committee of the Chinese People's Political Consultative Conference. Dr. Keung is currently the Vice Chairman and Chief Executive Officer of Ka Shui Holdings Co. Ltd. engaged in the manufacture of diecasting parts and has over 25 years of business experience in the field of metal forming, critical components manufacturing, new materials properties and related applications and maintains a close working relationship with the Hong Kong manufacturing industries.

DIRECTORS AND SENIOR MANAGEMENT PROFILE

SENIOR MANAGEMENT

Mr. Klaus Grenz, aged 55, is the General Manager of Goller Textilmaschinen GmbH and is responsible for its production and technical affairs. Mr. Grenz graduated from Technical College in Damstadt and has over 35 years of technical experience in wet finishing machines and technologies. Mr. Grenz joined the Group in April, 2006.

Mr. Lee Che Keung, aged 46, is the company secretary of the Group. Mr. Lee graduated from the Hong Kong Polytechnic (which was subsequently renamed the Hong Kong Polytechnic University) with a Professional Diploma in Company Secretaryship and Administration and is an associate member of the Hong Kong Institute of Chartered Secretaries. Mr. Lee is responsible for the overall corporate secretarial matters of the Group. Mr. Lee joined the Group in February 1990.

Mr. Leung Sheung Wai, Walter, aged 40, is a director of Fong's National Engineering Company, Limited and is responsible for overseeing the sales and marketing activities of the dyeing and finishing machine business of the Group in the overseas markets. Mr. Leung graduated from the Hong Kong Polytechnic (which was subsequently renamed the Hong Kong Polytechnic University) with a Higher Diploma in Textile Chemistry. Mr. Leung joined the Group in 1997.

Mr. Loo Kin Po, Boby, aged 43, is the General Manager of Goller (HK) Limited and 高樂紡織機械(深圳)有限公司 responsible for overseeing their general management and production affairs. Mr. Loo graduated from the Hong Kong Polytechnic (which was subsequently renamed the Hong Kong Polytechnic University) with a Higher Diploma in Textile Technology and holds a Master degree in Business Administration from the University of Leicester, United Kingdom, he is a member of the Associateship of Textile Institute in the United Kingdom. Mr. Loo joined the Group in February, 1994.

Mr. Hans-Eckhard Meiler, aged 56, is the General Manager of Goller Textilmaschinen GmbH and is responsible for its sales and marketing department. Mr. Meiler graduated from Regensburg University with a Diploma in Business and has over 30 years of experience in the textile machine industry. Mr. Meiler joined the Group in April, 2006.

Mr. Peter Rainer Philipp, aged 58, is responsible for the business development projects of the Group in the Americas and in Europe. Mr. Philipp is holding executive posts in certain overseas subsidiaries of the Group, namely director and chief executive officer of Xorella AG, advisory committee member of THEN Maschinen GmbH and director of Plexxor Co., Limited. Mr. Philipp holds a Bachelor's degree in Textile Engineering from the University of Reutlingen, Germany and has over 30 years of extensive business experience in the textile machinery industry in the USA and Europe. Mr. Philipp joined the Group in April, 2005.

Mr. Heinz Scheungraber, aged 51, is the Chief Financial Officer of THEN Maschinen GmbH and Goller Textilmaschinen GmbH. Mr. Scheungraber graduated from the Academy of Business and Administration in Stuttgart, Germany with a Diploma in Business Administration and has over 20 years' experience in finance and controlling management of manufacturing and machinery building companies. Mr. Scheungraber joined the Group in April, 2006.

DIRECTORS AND SENIOR MANAGEMENT PROFILE

Mr. Wong Ching Chuen, Patrick, aged 45, is a director of Fong's National Engineering Company, Limited and is responsible for overseeing the sales and marketing activities of the dyeing and finishing machine business of the Group in the woven market. Mr. Wong has been respectively educated in the Hong Kong Polytechnic (which was subsequently renamed the Hong Kong Polytechnic University) for Mechanical Engineering and Griffith University in Australia for law. Mr. Wong has over 15 years' experience in China trade for industrial equipment supplies and engineering work. He joined the Group in July, 2000.

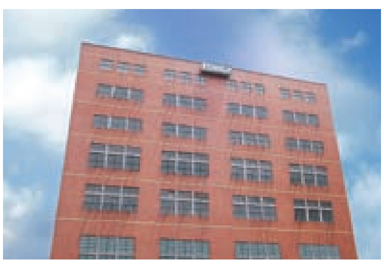
Mr. Wong Tak Man, Francis, aged 43, is a director of Fong's National Engineering Company, Limited and is responsible for overseeing the sales and marketing activities of the dyeing and finishing machine business of the Group in the China market. Mr. Wong graduated from the Hong Kong Polytechnic (which was subsequently renamed the Hong Kong Polytechnic University) with a Higher Diploma in Marine Engineering. Mr. Wong joined the Group in 1987.

Mr. Wu Wai Ip, Tony, aged 57, is the assistant to Chairman (organizational development) responsible for organizational re-engineering and development as well as human resources and administration functions of the Group. Mr. Wu graduated from the Hong Kong Polytechnic (which was subsequently renamed the Hong Kong Polytechnic University) with a Certificate in Personnel Management and holds a Master degree in Business Administration from University of East Asia, Macau. Mr. Wu is a member of the Hong Kong Institute of Human Resources Management and has over 30 years of extensive experience in human resources management. Mr. Wu joined the Group in May 2005.

MANAGEMENT DISCUSSION AND ANALYSIS

OPERATING RESULTS

For the year ended December 31, 2006, the consolidated revenue of the Group was approximately HK$2,380 million (2005: HK$2,012 million) representing an increase of 18% as compared with the previous year. The profit for the year attributable to the shareholders was approximately HK$260 million (2005: HK$219 million) representing an increase of approximately 19% as compared with last year. Basic earnings per share for the year amounted to 46.5 cents (2005: 39.0 cents).



1. Hong Kong Headquarters

2. China Headquarters

MANAGEMENT DISCUSSION AND ANALYSIS

3. Xorella AG, Switzerland

4. THEN Maschinen GmbH, Germany

5. Goller Textilmaschinen GmbH, Germany

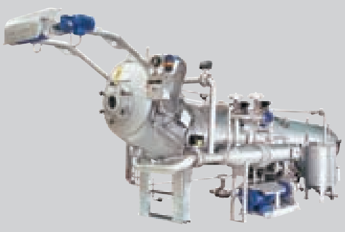
MANAGEMENT DISCUSSION AND ANALYSIS

DYEING AND FINISHING MACHINE MANUFACTURING

Fong's National Engineering Company, Limited, Fong's National Engineering (Shenzhen) Co., Ltd., THEN Maschinen GmbH, THEN Maschinen (HK) Limited, Goller Textilmaschinen GmbH, Goller (HK) Limited, Xorella AG and Xorella Hong Kong Limited

FONG'S®

1. ECO-88D
   High Temperature Dyeing Machine
2. JUMBOFLOW
   High Temperature Dyeing Machine
3. ALLWIN
   High Temperature Package Dyeing Machine

1

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THEN

1. THEN AIRFLOW® SYNERGY
2. THEN HST

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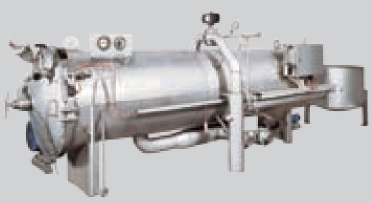
2


XORELLA

1. CONTEXXOR® Plus
2. CONTEXXOR® LTC-S

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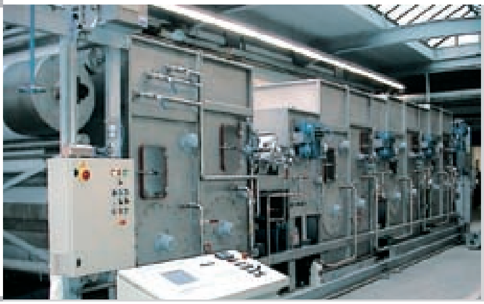
2


GOLLER

1. SINTENSA®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MANAGEMENT DISCUSSION AND ANALYSIS


ATME-1 2006


CITME 2006

The revenue of this division achieved an increase of 13% to approximately HK$1,313 million (2005: HK$1,163 million) for the year under review and accounted for 55% (2005: 58%) of the Group's consolidated revenue. However, the segment results decreased 26% to approximately HK$96 million (2005: HK$129 million) as a result of the delays in the turnaround of the European operations and the addition of Goller Textilmaschinen GmbH into this division.

In particular, the European operations (Goller, THEN, and Xorella) achieved sales of approximately HK$324 million (2005: HK$249 million) but incurred losses of approximately HK$75 million (2005: Losses of HK$33 million) during the year.

As described in our Interim Report 2006, the Group has been carrying out a series of improvement measures in re-building the sales force, streamlining the operations, optimizing the inventory levels and improving the manufacturing efficiencies of the above European operations. It is believed that with the ongoing implementation of the above various strategies of these European operations, the Group will see benefits from the synergy effects in the very near future.

In addition, during the year:

> The textile machinery division added the well established brand of **Goller** with its series of continuous washing, bleaching, dyeing and mercerizing range of textile machinery into the Group's product portfolio via the asset acquisition transaction during April 2006.
>
> Xorella Hong Kong Limited launched a joint venture with Plexus Cotton Limited of the UK in April 2006. The new joint venture company Plexxor Co. Limited, which is owned as to 51% by the Group, is engaged in the marketing and sale of a new patented vacuum bale system. Three vacuum bale systems have since been sold and are currently under installation in various locations around the world. Upon the successful start up of these systems, it is anticipated that these references will generate further sales in the coming year.
>
> Xorella Hong Kong Limited and Xorella AG had become wholly-owned subsidiaries of Group following our acquisitions of the 20% equity interests from the minority shareholder in December, 2006.

With regards to the raw material costs of stainless steel, due to the acute shortage of nickel in the world market, stainless steel prices have increased by 100% in the course of the second half of 2006. On a larger perspective, stainless steel prices have increased by four folds since 2003. Fortunately, the Group has been well hedged against such an abrupt stainless steel price increases and in addition the Group has implemented a series of price increases over the course of the last several years for its textile machinery business.

Nevertheless, according to nickel industry reports, the nickel shortage situation is not likely to abate any time soon. Consequently, should stainless steel prices continue to remain at these elevated levels, the Group may have to again consider raising machinery prices in the second half of 2007 in order to mitigate the effects of the stainless steel prices.

MANAGEMENT DISCUSSION AND ANALYSIS

ShanghaiTex 2006

Furthermore, the Group will continue to focus on the various cost controls and reduction and to further leverage on its bargaining power with its suppliers due to the division's purchasing scale so as to maintain reasonable profit margins.

Lastly, Fong's National Engineering Company, Limited and Fong's National Engineering (Shenzhen) Co., Ltd. are in the process of switching to a new ERP system during 2007. Upon its successful implementation, it is foreseeable that this new ERP system will be extended to all companies in this division to further enhance operational cost savings and efficiencies in the future.

Looking ahead, the Group remains optimistic and excited for the outlook in the coming year and also in the medium and long term as the domestic consumption in Asia as a whole is accelerating to become a major driver for the demand of textiles despite the foreseeable slow down in terms of export growth from Asia in the coming years as the Group is now well positioned to further take advantage of this scenario.

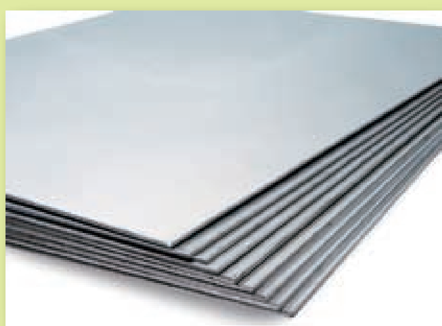
STAINLESS STEEL TRADING

Fong's Steels Supplies Company Limited

This stainless steel trading segment achieved an out performance year of good sales and profit growth as a result of the large increase in stainless steel prices during the year. For the year ended December 31, 2006, its revenue reached approximately HK$809 million (2005: HK$646 million) and accounted for 34% (2005: 32%) of the Group's consolidated revenue. The segment results grew 126% to approximately HK$145 million (2005: HK$64 million)

The management will maintain a conservative approach in conducting this trading business. It will also continue to adopt a prudent policy in selecting customers and tighten the credit control policy towards customers in order to minimize the risk associated with accounts receivables. Stainless steel prices are likely to stabilize at the present level and remain high in the near future, the management has been actively managing the inventory level based on its forecasts of stainless steel prices with an aim to minimize its risks given the volatile stainless steel market.

Warehouse



Stainless Steel Plates

MANAGEMENT DISCUSSION AND ANALYSIS

STAINLESS STEEL CASTING

Tycon Alloy Industries (Hong Kong) Co., Ltd.
and Tycon Alloy Industries (Shenzhen) Co., Ltd.

Foundry Plant of Tycon Alloy

Workshop of Tycon Alloy

Despite rising costs in both auxiliary and raw materials, this segment had a satisfactory performance with increases in both sales and profit for the year under review. The revenue amounted to approximately HK$258 million (2005: HK$203 million), representing an increase of 27% over last year. It accounted for 11% (2005 10%) of the Group's consolidated revenue. The segment results increased 28% to approximately HK$35 million (2005: HK$28 million). These results were mostly attributable to the increase in sales volume through capacity expansion and tight control on costs.

Raw material price continues to be a major challenge to Tycon. Nevertheless, the management is confident that this issue could be overcome through more stringent cost control & improved operational efficiency. The Group expects that this stainless steel casting business will have a reasonable growth in the coming year.

Machine component

Open type impeller

Diffuser

MANAGEMENT DISCUSSION AND ANALYSIS

JOINTLY CONTROLLED ENTITY

Monforts Fong's Textile Machinery Co. Limited ("Monforts Fong's")

Monforts Fong's Manufacturing Plant

During the year under review, Monforts Fong's achieved satisfactory results. The revenue was approximately HK$469 million (2005: HK$434 million), representing an increase of 8% over that of last year and the Group's share of profit after tax increased to approximately HK$47 million (2005: HK$32 million), representing an increase of 47%.

The substantial increase in profitability compared to the revenue was mainly attributed to the extra contribution derived from the increased sales volume, effective cost control on both manufacturing and overhead costs as well as a more profitable product mix.

Since the start of the joint venture in the end of 1999, over 500 stenters have been installed in the China market. The Monforts Fong's stenter has now successfully established itself as the market leader in China and the stenter equipment of choice by virtually all leading textile customers in the China market. It is expected that this success will continue as the joint venture's market position further takes root and the growth in the China textile industry will continue also.

Monfongs 328/329 TwinAir Stenter Frame Range

ASSOCIATES

Foshan East Asia Company Limited (a 30% owned associate)

During the year under review, the sales revenue of woven color fabrics conducted by Foshan East Asia Company Limited increased 18% to approximately HK$226 million (2005: HK$192 million) and the Group's share of profit after tax was approximately HK$8.9 million (2005: HK$2.1 million), representing an increase of 333% over last year.

It is anticipated that this associate company will continue to maintain its profit contribution to the Group.

MANAGEMENT DISCUSSION AND ANALYSIS

HUMAN RESOURCES

As at December 31, 2006, the Group had a total of approximately 4,500 employees (2005: 3,300) spreading among China, Hong Kong, Macau, Germany, Switzerland, Thailand, India, Turkey, and Central – South America. For the year under review, staff costs, including directors' remuneration were approximately HK$197 million (2005: HK$174 million).

Employees are remunerated based on their performances, experience and prevailing industry practice. The Group's remuneration policies and packages were reviewed by its management on a regular basis. Bonus and rewards may also be awarded to employees based on performance evaluation, with an aim to encourage and reward staff to achieve better performance. Other employee benefits available for eligible employees include retirement benefits schemes and share option scheme.

To equip with the workforces to face the challenges ahead, the Group will continue to offer training programmes to staff in different levels and positions on an ongoing basis. The aim of these programmes is to cultivate a dynamic corporate culture and develop effective communication and customer service skills among staff members. Moreover, system controls will also be reinforced to ensure high operational efficiency and performance.

LIQUIDITY AND CAPITAL RESOURCES

On May 10, 2006, the Company issued HK$800 million zero coupon convertible bonds due 2011. The convertible bonds will carry rights to convert into new shares of the Company at the conversion price of HK$8.37 per share, subject to adjustments. (As at December 31, 2006, the adjusted conversion price is HK$8.02 per share.)

The net proceeds after deducting the relevant expenses amounted to approximately HK$773 million. The Group will utilize the above said proceeds for the establishment of new production facilities within the nearby Guangdong region, possible future acquisitions of business or potential joint ventures relating to its core business and to finance the Group's general working capital. As at December 31, 2006, the balances of the proceeds, which have not yet been utilized, were being placed in banks as short-term deposits. The directors may review and vary the purpose for which the proceeds are used in light of what they consider to be the optimal use of the proceeds from time to time.

Following the issue of the convertible bonds, the financial position of the Group has further been strengthened and improved. As at December 31, 2006, there was a gearing ratio of 38% and the current ratio was 4.5.

As at December 31, 2006, bank and other borrowings amounted to approximately HK$177 million. 95% of the bank borrowings were sourced from Hong Kong and remaining were sourced from Germany. 95% of the borrowings were denominated in Hong Kong dollars and the remaining was denominated in Euro. The bank borrowings of the Group are predominantly subject to floating interest rates.

At as December 31, 2006, the cash and bank balance amounted to approximately HK$580 million of which 54% were denominated in Hong Kong dollars, 18% in Renminbi, 14% in US dollars, 12% in Euro and 2% in Japanese Yen.

Several subsidiaries of the Group have foreign currency sales and purchases, which expose the Group to foreign exchange risks. Certain trade receivables and trade payables of the Group are denominated in foreign currencies. The exposure to foreign exchange risks of the Group during the year under review was not significant. Currently, the Group does not have a foreign currency hedging policy. However, the directors will monitor the Group's overall foreign exchange exposures and consider hedging significant foreign currency exposure should the need arises.

CORPORATE GOVERNANCE REPORT

CODE ON CORPORATE GOVERNANCE

The Code on Corporate Governance Practices (the "Code") was introduced to Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") which was in force for accounting periods commencing on or after January 1, 2005.

The Company is committed to maintaining a high standard of corporate governance within a sensible framework with an emphasis on the principles of transparency, accountability and independence. The Board of Directors of the Company (the "Board") believes that good corporate governance is essential to the success of the Company and the enhancement of shareholders' value.

In the opinion of the Board, the Company has complied with the code provisions in the Code during the year ended December 31, 2006.

CODES FOR SECURITIES TRANSACTIONS BY DIRECTORS AND RELEVANT EMPLOYEES

The Company has adopted in December, 2005 a code of conduct regarding securities transactions by the Directors on terms no less exacting than the required standard set out in the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 of the Listing Rules. All the Directors have confirmed, following a specific enquiry by the Company, that they have complied with the required standard as set out in the code of conduct regarding securities transactions by the Directors adopted by the Company during the year.

To comply with the code provision A. 5.4 of the Code, the Company has also adopted in December, 2005 a code of conduct regarding securities transactions by relevant employees on no less exacting terms than the Model Code, to regulate dealings in the securities of the Company by certain employees of the Company or directors or employees of the Company's subsidiaries who are considered to be likely in possession of unpublished price sensitive information in relation to the Company or its securities. No incident of non-compliance was noted by the Company in 2006.

CORPORATE GOVERNANCE REPORT

BOARD OF DIRECTORS

The Board is responsible for the management of the Company with acting in the interest of the Company and its shareholders as its principle and is accountable to the shareholders for the assets and resources entrusted to them by the shareholders. The key responsibilities of the Board include the formulation of the Company's long-term development strategies and operating direction, setting of the management targets and supervising members of the management in implementing matters resolved by the Board and performing the duties.

The Board is led by the Chairman and currently comprises eight Executive Directors and three Independent Non-executive Directors. The Directors of the Company during the year and up to the date of this Annual Report were:

Executive Directors

Mr. Fong Sou Lam *(Chairman)*	
Mr. Wan Wai Yung *(Managing Director)*	
Mr. Fong Kwok Leung, Kevin	
Mr. Fong Kwok Chung, Bill	
Mr. Tsui Wai Keung	
Dr. Tsui Tak Ming, William	
Ms. Poon Hang Sim, Blanche	
Mr. Tou Kit Vai	*(appointed on January 15, 2007)*
Mr. Peter Rainer Philipp	*(resigned on April 12, 2006)*

Independent Non-executive Directors

Mr. Cheung Chiu Fan	
Dr. Yuen Ming Fai	
Dr. Keung Wing Ching	*(appointed on June 1, 2006)*
Mr. Lui Chi Lung, Louis	*(service contract expired on September 8, 2006)*

The biographical details of the existing Directors are listed in the section of "Directors and Senior Management Profile" in this Annual Report.

Save as Mr. Fong Kwok Leung, Kevin and Mr. Fong Kwok Chung, Bill are the sons of Mr. Fong Sou Lam, there is no relationship (including financial, business, family or other material or relevant relationship) among members of the Board and in particular, between the Chairman and the Managing Director. The Company considers that the Board has the necessary skills and experience appropriate for discharging their duties as directors in the best interest of the Company and that the current board size as adequate for its present operations. Executive Directors are in charge of different businesses or functional divisions in accordance with their respective areas of expertise.

CORPORATE GOVERNANCE REPORT

CHAIRMAN AND CHIEF EXECUTIVE OFFICER

The Company does not at present have any officer with the title of "chief executive officer" ("CEO") but instead the duties of a CEO are performed by the Managing Director. In order to have a clear division between the management of the Board and the day-to-day management of the business operation of the Company, the role of the Chairman is separate from that of the Managing Director. The Chairman focuses on overall corporate development and strategic direction of the Group and provides leadership for the Board and oversees the efficient functioning of the Board. The Managing Director is responsible for all day-to-day corporate management matters as well as assisting the Chairman in planning and developing the Group's strategies. Such division of responsibilities helps to reinforce their independence and to ensure a balance of power and authority.

INDEPENDENT NON-EXECUTIVE DIRECTORS

In compliance with Rule 3.10(2) of the Listing Rules, Mr. Cheung Chiu Fan, one of the Independent Non-executive Directors, is a public auditor and has appropriate qualifications and accounting and related financial management expertise.

The Company has received from each of the Independent Non-executive Directors an annual confirmation of his independence. The Board considers that each Independent Non-executive Director is independent in character and judgement and that they all meet the specific independence criteria as required under Rule 3.13 of the Listing Rules. Moreover, all Independent Non-executive Directors are engaged on service contracts for a term of two years, subject to retirement by rotation and re-election in accordance with the provisions of the Bye-Laws of the Company.

The Independent Non-executive Directors are expressly identified in all of the Company's publications such as circular, announcement or relevant corporate communications in which the names of Directors of the Company are disclosed.

BOARD MEETING

The Board conducts meetings on a regular basis and on an ad hoc basis, as required by business needs. The Bye-Laws of the Company allows board meetings to be conducted by way of telephone or videoconference and any resolutions to be passed by way of written resolutions circulated to and signed by all Directors from time to time when necessary unless any matters in which a substantial shareholder or a Director or their respective associates has a conflict of interest. The Board held a total of five regular Board Meetings during the year under review. The attendance record of each Director at the Board Meetings is disclosed below in this report.

In the said Board Meetings, sufficient fourteen-day notices for regular board meetings and notice in reasonable days for non-regular board meetings were given to all Directors so as to ensure that each of them had an opportunity to attend the meetings, and agendas and accompanying board papers were given to all Directors in a timely manner before the appointed date of the board meetings and at least three days before the regular board meetings. Sufficient information was also supplied by the management to the Board to enable it to make decisions, which are made in the best interests of the Company. All minutes are kept by the Company Secretary and are open for inspection at any reasonable time on reasonable notice by any Director.

CORPORATE GOVERNANCE REPORT

NOMINATION OF DIRECTORS

The Board is responsible for considering the suitability of a candidate to act as a Director, and approving and terminating the appointment of a Director. The Company has not set up a nomination committee for the time being.

The Chairman is mainly responsible for identifying suitable candidates for members of the Board when there is a vacancy or an additional Director is considered necessary. The Chairman will propose the appointment of such candidates to each member of the Board for consideration and each member of the Board will review the qualifications of the relevant candidates for determining the suitability to the Group on the basis of his qualifications, experience and background. The decision of appointing a Director must be approved by the Board.

APPOINTMENT AND RE-ELECTION OF DIRECTORS

The Board is empowered under the Company's Bye-Laws to appoint any person as a Director either to fill a casual vacancy on or as an additional member of the Board. A newly appointed Director must retire and be-elected at the first annual general meeting after his/her appointment. According to the Bye-Laws of the Company, at each annual general meeting of the Company, one-third of the Directors for the time being (or, if their number is not a multiple of three, the number nearest to one-third) should retire from office by rotation, provided that the Chairman and Managing Director of the Company should not be subject to retirement by rotation or be taken into account in determining the number of directors to retire each year.

During the year of 2006, a Board Meeting was held to approve the appointment of Dr. Keung Wing Ching as an Independent Non-executive Director of the Company with effect from June 1, 2006. In addition, Mr. Tou Kit Vai was appointed as an additional Executive Director of the Company with effect from January 15, 2007.

In the spirit of good corporate governance practices, Mr. Fong Sou Lam who is the Chairman of the Board of the Company and Mr. Wan Wai Yung who is the Managing Director of the Company, will voluntarily retire from their office by rotation at the relevant annual general meetings of the Company notwithstanding that they are not required by the Bye-Laws to do so.

Mr. Wan Wai Yung, Mr. Fong Kwok Leung, Kevin, Dr. Tsui Tak Ming, William, Mr. Tou Kit Vai and Dr. Keung Wing Ching will retire from office by rotation under the Bye-Laws of the Company at the forthcoming annual general meeting, but all of them will be offering themselves for re-election at the same meeting.

CORPORATE GOVERNANCE REPORT

REMUNERATION COMMITTEE

In order to comply with the code provision B.1.1. of the Code, the Board has established a Remuneration Committee in December, 2005 with specific terms of reference which deal clearly with its authority and duties. The terms of reference have been posted on the Company's website (www.fongs.com).

The Remuneration Committee comprises the following five members, the majority of which are the Independent Non-executive Directors:

Mr. Fong Sou Lam *(Committee Chairman)*
Mr. Wan Wai Yung
Mr. Cheung Chiu Fan
Dr. Yuen Ming Fai
Dr. Keung Wing Ching

The Remuneration Committee's role is to make recommendations to the Board on the remuneration policy and structures for Directors of the Company and senior management of the Group and to ensure that they are fairly rewarded for their individual contribution to the Group's overall performance, having regard to the interests of the shareholders. The overriding objective of the remuneration policy is to ensure that the Company is able to attract, retain and motivate a high-calibre team which is essential to the success of the Company. The principal duties of the Remuneration Committee include determining the specific remuneration packages of all Executive Directors and senior management as well as reviewing and approving performance-based remuneration by reference to corporate goals and objectives resolved by the Board from time to time. In particular, the Remuneration Committee is delegated with the specific task of ensuring that no Director is involved in deciding his own remuneration.

The Remuneration Committee shall meet as and when required to consider remuneration-related matters. In 2006, the Remuneration Committee convened one meeting, where it approved the performance related incentive bonus payable to the Executive Directors of the Company in respect of the financial year ended December 31, 2005. The attendance record of the members of the Remuneration Committee is disclosed below in this report.

Prior to the establishment of the Remuneration Committee, consistent with the principles applied in the past, the remunerations of the Directors and senior management were determined with reference to the performance and profitability of the Group as well as remuneration benchmarks from other local and international companies and the prevailing market conditions.

CORPORATE GOVERNANCE REPORT

AUDIT COMMITTEE

The Company established its Audit Committee in December, 1998 with reference to "A Guide for the Formation of an Audit Committee" issued by the Hong Kong Institute of Certified Public Accountants (formerly known as Hong Kong Society of Accountants). In accordance with the requirements of the Code, the terms of reference of the Audit Committee were revised in December, 2005 in terms substantially the same as the provisions set out in the Code. The revised terms of reference of the Audit Committee are available on the Company's website (www.fongs.com).

The principal duties of the Audit Committee include the review and supervision of the Group's financial reporting system and internal control procedures, review of the Group's financial information and review of the relationship with the external auditors of the Company. Regular meetings have been held by the Audit Committee since its establishment. The Audit Committee also reviews the Company's internal audit plan, and submits relevant reports and recommendations to the Board on a regular basis.

The Audit Committee comprises three Independent Non-executive Directors, namely Mr. Cheung Chiu Fan (Chairman of the Audit Committee), Dr. Yuen Ming Fai and Dr. Keung Wing Ching. The Audit Committee meets formally at least three times a year. The external auditors and the Executive Directors and senior management are invited to attend the meetings whenever it is considered appropriate or necessary. The Audit Committee held three meetings in 2006 and the individual attendance of members are set out below in this report.

In discharging its responsibilities, the Audit Committee had performed the following works during the year of 2006:

(i) reviewed the interim and annual financial statements and the related results announcements;

(ii) reviewed the change in accounting standards and assessment on potential impacts on the Group's financial statements;

(iii) reviewed the continuing connected transactions and commented on the fairness and reasonableness of the transactions;

(iv) reviewed the Group's internal control system and discussed the relevant issues including financial, operational and compliance controls and risk management functions; and

(v) made recommendation on the appointment or re-appointment on the external auditors and approved their terms of engagement.

The Audit Committee recommended to the Board that, subject to shareholders' approval at the forthcoming annual general meeting, Messrs. Deloitte Touche Tohmatsu be re-appointed as the Company's external auditors for 2007.

CORPORATE GOVERNANCE REPORT

ATTENDANCE RECORD OF INDIVIDUAL DIRECTORS AT MEETINGS IN 2006

	Number of meetings attended/held		
	Board Meeting	**Audit Committee Meeting**	**Remuneration Committee Meeting**
Executive Directors			
Mr. Fong Sou Lam	5/5	2/3	1/1
Mr. Wan Wai Yung	4/5		1/1
Mr. Fong Kwok Leung, Kevin	5/5	1/3	
Mr. Fong Kwok Chung, Bill	4/5		
Mr. Tsui Wai Keung	2/5		
Dr. Tsui Tak Ming, William	5/5	2/3	
Ms. Poon Hang Sim, Blanche	5/5	3/3	
Independent Non-executive Directors			
Mr. Cheung Chiu Fan	3/5	3/3	1/1
Dr. Yuen Ming Fai	3/5	3/3	0/1
Dr. Keung Wing Ching	1/1	3/3	1/1

In each of the above meetings, certain Directors were unable to attend the meeting(s) due to business trip or other commitment.

AUDITORS' REMUNERATION

During the year, Messrs. Deloitte Touche Tohmatsu, auditors of the Company (which for the purpose includes any entity under common control, ownership or management with the auditors or any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as part of the audit firm nationally or internationally) provided the following audit and non-audit services to the Group:

(i) Audit services;

(ii) Non-audit service- agreed-upon procedures for continuing connected transactions and results announcements; and

(iii) Non-audit service- tax advisory services

Remuneration paid to other auditors for audit services rendered to overseas subsidiaries was approximately HK$123,630.

RESPONSIBILITY FOR PREPARATION AND REPORTING OF ACCOUNTS

The consolidated financial statements of the Company for the year ended December 31, 2006 have been reviewed by the Audit Committee and audited by the external auditors, Messrs. Deloitte Touche Tohmatsu. The Directors acknowledged their responsibility for preparing the financial statements of the Group which were prepared in accordance with statutory requirements and applicable accounting standards. A statement by the auditors about their reporting responsibilities is set out in the Independent Auditor's Report of this Annual Report.

INTERNAL CONTROLS

The Board has overall responsibilities for maintaining sound and effective internal control systems of the Group. The Board has delegated to the management the implementation of such systems of internal controls as well as the review of relevant financial, operational and compliance controls and risk management procedures of the Group. The management throughout the Group maintains and monitors the internal control systems on an ongoing basis.

There is currently no internal audit function within the Group that is separate and independent from the Group's finance team. The finance team assumes also responsibility for conducting regular review of internal control procedures, including accounting system and procedures. Although this arrangement can be improved, management is not concerned with the lack of segregation of duties having assumed the current organizational structure, lines of responsibility and authority of the management team and the risks associated with the operations of the Group.

INVESTOR RELATIONS

During the year under review, the Company has proactively enhanced its corporate transparency and communications with its shareholders and the investment community through its mandatory interim and annual report as well as voluntary press releases. Through the timely distribution of press releases, the Company has also kept the public abreast of its latest developments. Regular meetings and plant visits have been organized to enhance the investors' understanding of the Group's businesses and production operations.

The Company has set up a corporate website (www.fongs.com) at which relevant information including the latest development of the Group will be announced. The website offers the latest information regarding various aspects of the Group to investors and the public. The Company will improve the website in the future, making it an interactive communication platform between the Company and its investors.

For and on behalf of the Board
Fong Sou Lam
Chairman

Hong Kong, April 16, 2007

DIRECTORS' REPORT

The Directors present their annual report and the audited consolidated financial statements for the year ended December 31, 2006.

PRINCIPAL ACTIVITIES

The Company acts as an investment holding company.

The subsidiaries of the Company are principally engaged in the manufacture and sale of dyeing and finishing machines, trading of stainless steel supplies and the manufacture and sale of stainless steel casting products. The activities of its principal subsidiaries are set out in note 39 to the consolidated financial statements.

RESULTS AND APPROPRIATIONS

The results of the Group for the year ended December 31, 2006 are set out in the consolidated income statement on page 37.

An interim dividend of 8 HK cents per share plus an interim special dividend of 3 HK cents per share, amounting to a total of approximately HK$61 million, were paid to the shareholders during the year. The Directors now recommend the payment of a final dividend of 8 HK cents per share plus a final special dividend of 7 HK cents per share to the shareholders on the register of members on May 25, 2007, amounting to approximately HK$84 million, and the retention of the remaining profit for the year of approximately HK$115 million.

Subject to the approval of the shareholders at the forthcoming annual general meeting, dividend is expected to be despatched to the shareholders on or before June 6, 2007.

PROPERTY, PLANT AND EQUIPMENT

Details of movements in property, plant and equipment of the Group during the year are set out in note 13 to the consolidated financial statements.

MAJOR CUSTOMERS AND SUPPLIERS

For the year ended December 31, 2006, the aggregate amount of revenue attributable to the Group's five largest customers represented less than 8% of the Group's total revenue.

The aggregate amount of purchases attributable to the Group's five largest suppliers accounted for approximately 40% of the Group's total purchases and the amount of purchases attributable to the Group's largest supplier was approximately 24% of the total purchases.

None of the Directors, their associates, or any shareholder, which to the knowledge of the Directors owns more than 5% of the Company's share capital, has any interest in the Group's five largest suppliers or customers.

DIRECTORS' REPORT

DISTRIBUTABLE RESERVES OF THE COMPANY

The Company's reserves available for distribution to shareholders as at December 31, 2006 were as follows:

	HK$'000
Contributed surplus	23,033
Retained profits	44,692
Dividend reserve	83,747
	151,472

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

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

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

DIRECTORS AND SERVICE CONTRACTS

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

Executive Directors:

Mr. Fong Sou Lam *(Chairman)*
Mr. Wan Wai Yung *(Managing Director)*
Mr. Fong Kwok Leung, Kevin
Mr. Fong Kwok Chung, Bill
Mr. Tsui Wai Keung
Dr. Tsui Tak Ming, William
Ms. Poon Hang Sim, Blanche
Mr. Tou Kit Vai *(appointed on January 15, 2007)*
Mr. Peter Rainer Philipp *(resigned on April 12, 2006)*

Independent Non-executive Directors:

Mr. Cheung Chiu Fan
Dr. Yuen Ming Fai
Dr. Keung Wing Ching *(appointed on June 1, 2006)*
Mr. Lui Chi Lung, Louis *(service contract expired on September 8, 2006)*

DIRECTORS' REPORT

Mr. Cheung Chiu Fan was appointed under a contract for a term of 2 years commencing on January 1, 2005 and expiring on December 31, 2006. Upon expiry, his term of office has been extended to December 31, 2008.

Mr. Lui Chi Lung, Louis was appointed under a contract for a term of 2 years commencing on September 9, 2004 and expiring on September 8, 2006. Upon expiry, the contract was not renewed.

Dr. Yuen Ming Fai was appointed under a contract for a term of 2 years commencing on September 1, 2004 and expiring on August 31, 2006. Upon expiry, his term of office has been extended to August 31, 2008.

Dr. Keung Wing Ching was appointed under a contract for a term of 2 years commencing on June 1, 2006 and expiring on May 31, 2008.

The Company has received confirmations of independence from all Independent Non-executive Directors and considers them to be independent.

In accordance with Clauses 99 and 102 of the Company's Bye-Laws, the following Directors, namely Mr. Wan Wai Yung, Mr. Fong Kwok Leung, Kevin, Dr. Tsui Tak Ming, William, Mr. Tou Kit Vai and Dr. Keung Wing Ching, will retire from office at the forthcoming annual general meeting and, being eligible, offer themselves for re-election.

Other than as disclosed above, no Director proposed for re-election at the forthcoming annual general meeting has a 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 THE SHARES OF THE COMPANY

As at December 31, 2006, the interests of the Directors and their associates in the shares of the Company and its associated corporations as recorded in the register maintained by the Company pursuant to Section 352 of the Securities and Futures Ordinance ("SFO"), or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers, were as follows:

Long position in 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
Mr. Fong Sou Lam	Beneficial owner	22,622,000	4.05%
Mr. Fong Kwok Leung, Kevin	Beneficial owner	1,550,000	0.27%
	Held by spouse	200,000	0.04%
	Held by discretionary trusts *(note)*	304,875,601	54.60%
		306,625,601	54.91%
Mr. Fong Kwok Chung, Bill	Beneficial owner	7,442,000	1.33%
	Held by discretionary trusts *(note)*	304,875,601	54.60%
		312,317,601	55.93%
Mr. Wan Wai Yung	Beneficial owner	1,743,500	0.31%
Ms. Poon Hang Sim, Blanche	Beneficial owner	120,000	0.02%

Note: The 304,875,601 shares are owned by two discretionary trusts, the beneficiaries of which include Mr. Fong Kwok Leung, Kevin, Mr. Fong Kwok Chung, Bill and other Fong's family members. These shares represented an interest duplicated amongst those two Directors.

Save as disclosed above and other than certain nominee shares in subsidiaries held by the Directors in trust for the Company or its subsidiaries, none of the Directors, chief executive nor their associates had any interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations as at December 31, 2006.

DIRECTORS' REPORT

SHARE CAPITAL

Details of movements in the Company's share capital during the year are set out in note 29 to the consolidated financial statements.

SHARE OPTIONS

Particulars of the Company's share option scheme are set out in note 31 to the consolidated financial statements.

No share option has been granted by the Company under the share option scheme since its adoption.

ARRANGEMENTS TO PURCHASE SHARES OR DEBT SECURITIES

Other than the share option scheme disclosed above, at no time during the year was the Company or its subsidiaries a party to any arrangements to enable the Directors of the Company (including their spouse and children under 18 years of age) to acquire benefits by means of the acquisition of shares in, or debt securities including debentures of, the Company or any other body corporate.

CONTINUING CONNECTED TRANSACTIONS

During the year ended December 31, 2006, the Group entered into the following transactions which are defined in Chapter 14A of the Listing Rules as "continuing connected transactions" and are exempted from the independent shareholders' approval requirements. These continuing connected transactions are subject to the reporting and announcement requirements set out in Chapter 14A of the Listing Rules.

(1) The Group entered into an operating lease agreement with Sou Lam Company Limited ("Sou Lam") in which Messrs. Fong Kwok Leung, Kevin and Fong Kwok Chung, Bill have beneficial interests.

On December 30, 2004, Fong's National Engineering Co., Ltd. ("FNECL"), a wholly-owned subsidiary of the Company, entered into an operating lease agreement with Sou Lam for the use of a portion of a factory building by the Group as general office as well as for industrial or godown purposes for a term of three years from January 1, 2005 to December 31, 2007. The total rentals paid by the Group to Sou Lam for the year amounted to HK$5,418,000. Details of the transaction were set out in the press announcement of the Company dated December 30, 2004.

(2) *The Group, through its three subsidiaries, entered into five agreements with PSP Marketing Inc. ("PSP Marketing") in relation to agency and marketing activities for the sales of the products of these subsidiaries. PSP Marketing is beneficially owned as to 51% by Mr. Peter Rainer Philipp who is currently a director of certain operating subsidiaries of the Group.*

(i) On May 1, 2003, a regional sales coordination agreement was entered into between PSP Marketing and FNECL whereby PSP Marketing was appointed as the exclusive sales coordinator to carry out sales and marketing activities in respect the **FONG'S** branded products of the Group in Central and South America for an initial term of three years commencing from May 1, 2003.

(ii) On October 4, 2003, a sales agency agreement was entered into between PSP Marketing and FNECL whereby PSP Marketing was appointed as the exclusive sales agent for the sales of the **FONG'S** branded products of the Group in Canada and the United States of America (the "USA") with effect from October 4, 2003.

(iii) On May 14, 2003, a technical, sales and marketing support agreement entered into between PSP Marketing and Xorella AG, a wholly owned subsidiary of the Company whereby PSP Marketing was engaged to provide technical, sales and marketing supports in respect of the products of Xorella AG in Central and South America with effect from May 2, 2003.

(iv) On July 22, 2003, a sales agency agreement entered into between PSP Marketing and Xorella AG whereby PSP Marketing was appointed as the exclusive sales agent for the sales of the products of Xorella AG in Canada and the USA with effect from July 22, 2003.

(v) On November 4, 2004, a sales agency agreement was entered into between PSP Marketing and THEN Maschinen GmbH, a wholly-owned subsidiary of the Company, whereby PSP Marketing was appointed as the exclusive sales agent for the sales of the **THEN** branded products of the Group in the USA with effect from November 1, 2004.

By a subsequent mutual agreement between PSP Marketing and the Group, the parties have agreed that with effect from April 10, 2005, notwithstanding any provisions set out in the above-mentioned agreements and unless otherwise being earlier terminated by either parties, each of the above-mentioned agreements shall not be renewable beyond December 31, 2007 and all the agreements shall expire on December 31, 2007.

Details of these transactions were set out in the press announcement of the Company dated April 20, 2005.

The aggregate amount paid and payable to PSP Marketing under the above-mentioned agreements for the year was HK$7,866,000, which has not exceeded the cap amount under Rule 14A. 34 of the Listing Rules.

Pursuant to Rule 14A.38 of the Listing Rules, the Board of Directors engaged the auditors of the Company to perform certain agreed upon procedures in respect of the continuing connected transactions of the Group. The auditors have reported their factual findings on these procedures to the Board of Directors. The Independent Non-executive Directors have reviewed the continuing connected transactions and the report of the auditors and have confirmed that the transactions have been entered into by the Group in the ordinary course of its businesses, on normal commercial terms and in accordance with the terms of the agreements governing such transactions that are fair and reasonable and in the interest of the shareholders of the Company as a whole.

CONTRACTS OF SIGNIFICANCE

Other than the continuing connected transactions as disclosed above, no other contracts of significance to which the Company or 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.

DISCLOSABLE INTERESTS AND SHORT POSITIONS OF SHAREHOLDERS UNDER THE SFO

As at December 31, 2006, the register maintained by the Company pursuant to Section 336 of the SFO shows that, other than the interests disclosed above in respect of certain Directors, the following shareholders had notified the Company of relevant interests in the issued share capital of the Company.

Long position in shares of HK$0.10 each of the Company

Name of shareholder	Capacity	Number of issued ordinary shares	Percentage of the issued share capital in the Company
Capital Research and Management Company	Beneficial owner	36,590,000	6.55%
Aberdeen Asset Management Plc.	Beneficial owner	33,626,000	6.02%

Save as disclosed above, as at December 31, 2006, the Company had not been notified of any person who had an interest or short position in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO.

DONATIONS

During the year, the Group made charitable and other donations amounting to HK$15,576,000.

EMOLUMENT POLICY

The Group's emolument policy, including salaries and bonuses, is in line with the local practices where the Company and its subsidiaries operate. The emolument policy of the Group is reviewed by the Remuneration Committee of the Company regularly, making reference to legal framework, market conditions and performance of the Group and individual employee.

The emolument packages of the Directors of the Company will be reviewed by the Remuneration Committee of the Company regularly. A share option scheme was established by the Company on May 26, 2003 to grant options to eligible participants for the purpose of providing incentives and rewards to those who contribute to the success of the Group's operations. Details of the share option scheme are set out in note 31 to the consolidated financial statements. No option has been granted by the Company under the share option scheme since its adoption.

PRE-EMPTIVE RIGHTS

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

POST BALANCE SHEET EVENT

Details of a continuing connected transaction occurring after the balance sheet date are set out in note 36 to the consolidated financial statements.

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

During the year, the Company repurchased certain of its own shares through the Stock Exchange, details of which are set out in note 29 to the consolidated financial statements. The Directors considered that the repurchases would increase the net asset value per share and earnings per share of the Company.

PUBLIC FLOAT

Based on the information that is publicly available to the Company and within the knowledge of the Directors, as at the date of this report, there is sufficient public float of not less than 25% of the Company's issued shares as required under the Listing Rules.

AUDITORS

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

On behalf of the Board

Fong Sou Lam
DIRECTOR
Hong Kong, April 16, 2007

INDEPENDENT AUDITOR'S REPORT

Deloitte.
德勤

TO THE SHAREHOLDERS OF FONG'S INDUSTRIES COMPANY LIMITED
立信工業有限公司
(Incorporated in Bermuda with limited liability)

We have audited the consolidated financial statements of Fong's Industries Company Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") set out on pages 37 to 91, which comprise the consolidated balance sheet as at December 31, 2006, the consolidated income statement, the consolidated statement of recognised income and expense and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

DIRECTORS' RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

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

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with Section 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. We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the consolidated financial statements are free from material misstatement.

INDEPENDENT AUDITOR'S REPORT

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Directors, as well as evaluating the overall presentation of the consolidated financial statements.

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

OPINION

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

Deloitte Touche Tohmatsu
Certified Public Accountants
Hong Kong

April 16, 2007

CONSOLIDATED INCOME STATEMENT

(For the year ended December 31, 2006)

	NOTES	2006 HK$'000	2005 HK$'000
Revenue	6	**2,380,036**	2,012,252
Cost of sales		**(1,697,437)**	(1,450,290)
Gross profit		**682,599**	561,962
Interest income		**18,489**	2,576
Other income		**52,291**	39,108
Gain on fair value change of the derivative component of convertible loan notes		**11,001**	–
Selling and distribution costs		**(92,871)**	(90,121)
General and administrative expenses		**(305,236)**	(239,668)
Other expenses		**(60,623)**	(50,216)
Loss on fair value change of financial instruments		**(2,527)**	–
Finance costs	7	**(49,817)**	(17,242)
Share of results of an associate		**8,893**	2,054
Share of results of jointly controlled entities		**46,740**	32,253
Profit before tax	8	**308,939**	240,706
Income tax expense	10	**(48,906)**	(22,510)
Profit for the year		**260,033**	218,196
Attributable to:			
Equity holders of the parent		**260,033**	218,653
Minority interests		**–**	(457)
		260,033	218,196
Earnings per share	12		
Basic		**46.5 HK cents**	39.0 HK cents
Diluted		**44.8 HK cents**	N/A

CONSOLIDATED BALANCE SHEET

(At December 31, 2006)

	NOTES	2006 HK$'000	2005 HK$'000
Non-current assets			
Property, plant and equipment	13	**288,002**	255,889
Prepaid lease payments	14	**11,639**	11,665
Intellectual property rights	15	**21,934**	24,826
Interests in an associate	16	**42,431**	33,142
Interests in jointly controlled entities	17	**81,312**	60,751
Deposits for acquisition of property, plant and equipment		**9,958**	–
Deferred tax assets	28	**5,525**	4,268
		460,801	390,541
Current assets			
Inventories	18	**778,372**	367,973
Trade and other receivables	19	**404,475**	226,685
Dividend receivable from a jointly controlled entity		**–**	7,500
Prepaid lease payments	14	**341**	332
Amount due from a jointly controlled entity	20	**2,475**	8,703
Derivative financial instrument	21	**27**	–
Tax recoverable		**691**	7,725
Structured deposits	22	**127,890**	–
Bank balances, deposits and cash	23	**580,464**	312,704
		1,894,735	931,622
Current liabilities			
Trade and other payables	24	**329,464**	221,165
Amount due to a jointly controlled entity	20	**1,701**	–
Warranty provision	25	**13,264**	12,299
Derivative financial instrument	21	**244**	–
Tax liabilities		**23,339**	6,012
Borrowings – due within one year	27	**54,613**	87,015
		422,625	326,491
Net current assets		**1,472,110**	605,131
		1,932,911	995,672

CONSOLIDATED BALANCE SHEET

(At December 31, 2006)

	NOTES	2006 HK$'000	2005 HK$'000
Capital and reserves			
Share capital	29	**55,842**	56,038
Reserves	30	**959,244**	817,229
Equity attributable to equity holders of the parent		**1,015,086**	873,267
Minority interests	30	**1,290**	1,290
Total equity		**1,016,376**	874,557
Non-current liabilities			
Borrowings – due after one year	27	**122,500**	120,000
Deferred tax liabilities	28	**1,190**	1,115
Embedded derivative component of convertible loan notes	26	**25,798**	–
Convertible loan notes	26	**767,047**	–
		916,535	121,115
		1,932,911	995,672

The financial statements on pages 37 to 91 were approved and authorised for issue by the Board of Directors on April 16, 2007 and are signed on its behalf by:

Fong Kwok Chung, Bill
DIRECTOR

Fong Sou Lam
DIRECTOR

CONSOLIDATED STATEMENT OF RECOGNISED INCOME AND EXPENSE

(For the year ended December 31, 2006)

	2006 HK'000	2005 HK$'000
Net exchange difference arising on translation of overseas subsidiaries recognised directly in equity	**16,294**	35
Share of changes in exchange reserves of an associate and a jointly controlled entity	**3,722**	1,911
Net income recognised directly in equity	**20,016**	1,946
Translation reserve realised on disposal of a subsidiary	**–**	1,863
Profit for the year	**260,033**	218,196
Total recognised income and expense for the year	**280,049**	222,005
Attributable to:		
Equity holders of the parent	**280,049**	222,462
Minority interests	**–**	(457)
	280,049	222,005

CONSOLIDATED CASH FLOW STATEMENT

(For the year ended December 31, 2006)

	2006 HK$'000	2005 HK$'000
OPERATING ACTIVITIES		
Profit before tax	**308,939**	240,706
Adjustments for:		
Finance costs	**43,177**	13,191
Interest income	**(18,489)**	(2,576)
Share of results of an associate	**(8,893)**	(2,054)
Share of results of jointly controlled entities	**(46,740)**	(32,253)
Depreciation and amortisation	**34,525**	32,261
(Reversal of) allowance for doubtful debts	**(870)**	2,159
Allowance for inventories	**1,654**	985
Loss on fair value change on financial instruments	**2,527**	–
Gain on fair value change of derivative components of convertible loan notes	**(11,001)**	–
Loss (gain) on disposal of property, plant and equipment	**1,044**	(67)
Gain on disposal of prepaid lease payments	**–**	(10,741)
Loss on disposal of a subsidiary	**–**	1,658
Increase in warranty provision	**13,200**	12,239
Operating cash flows before movements in working capital	**319,073**	255,508
(Increase) decrease in inventories	**(396,781)**	24,481
Increase in trade and other receivables	**(179,768)**	(35,688)
Decrease (increase) in amount due from a jointly controlled entity	**6,335**	(8,703)
Increase (decrease) in trade and other payables	**101,155**	(24,780)
Increase (decrease) in amount due to a jointly controlled entity	**1,701**	(2,420)
Utilisation of warranty provision	**(12,235)**	(11,005)
Cash (used in) generated from operations	**(160,520)**	197,393
Hong Kong profits tax paid	**(20,036)**	(27,213)
Overseas income tax paid	**(6,642)**	(12,175)
Hong Kong profits tax refunded	**1**	–
Overseas income tax refunded	**–**	8,489
NET CASH (USED IN) GENERATED FROM OPERATING ACTIVITIES	**(187,197)**	166,494

CONSOLIDATED CASH FLOW STATEMENT

(For the year ended December 31, 2006)

	NOTE	2006 HK$'000	2005 HK$'000
INVESTING ACTIVITIES			
Increase in structured deposits		**(130,200)**	–
Purchases of property, plant and equipment		**(53,652)**	(23,800)
Deposits paid for acquisition of property, plant and equipment		**(9,958)**	–
Investment in jointly controlled entities		**(1,579)**	–
Dividends received from jointly controlled entities		**37,500**	22,500
Interest received		**18,489**	2,576
Dividend received from an associate		**1,084**	–
Proceeds from disposal of property, plant and equipment		**287**	762
Proceeds from disposal of prepaid lease payments		**–**	23,371
Proceeds from disposal of a subsidiary	32	**–**	1,818
Purchases of prepaid lease payments		**–**	(394)
NET CASH (USED IN) GENERATED FROM INVESTING ACTIVITIES		**(138,029)**	26,833
FINANCING ACTIVITIES			
Proceed on issue of convertible loan notes		**800,000**	–
New bank loan raised		**59,558**	200,000
Dividends paid		**(128,691)**	(140,094)
Repayment of bank loans		**(96,515)**	(70,000)
Issue cost of convertible loan notes		**(26,460)**	–
Interest paid on bank loans		**(12,178)**	(11,930)
Repurchase of shares		**(9,539)**	–
Factoring charges		**(693)**	(1,232)
Net decrease in trust receipt loans		**–**	(110,851)
Repayment of obligations under finance leases		**–**	(1,518)
Interest paid on finance leases		**–**	(29)
Other borrowings raised		**5,055**	3,978
NET CASH GENERATED FROM (USED IN) FINANCING ACTIVITIES		**590,537**	(131,676)
NET INCREASE IN CASH AND CASH EQUIVALENTS		**265,311**	61,651
CASH AND CASH EQUIVALENTS AT BEGINNING OF THE YEAR		**312,704**	254,176
Effect of foreign exchange rate changes		**2,449**	(3,123)
CASH AND CASH EQUIVALENTS AT END OF THE YEAR, representing bank balances, deposits and cash		**580,464**	312,704

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(For the year ended December 31, 2006)

1. GENERAL

The Company is incorporated in Bermuda as an exempted company with limited liability and its securities are listed on the Stock Exchange. The address of the registered office and principal place of business of the Company is disclosed in the section of "Corporate Information" in the Annual Report.

The consolidated financial statements are presented in Hong Kong dollars, which is the same as the functional currency of the Company.

The Company acts as an investment holding company. Its subsidiaries are principally engaged in the manufacture and sale of dyeing and finishing machines, trading of stainless steel supplies and the manufacture and sale of stainless steel casting products.

2. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS

In the current year, the Group has applied, for the first time, a number of new standard, amendments and interpretations (hereinafter collectively referred to as "new HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA") which are either effective for accounting periods beginning on or after December 1, 2005 or January 1, 2006. The adoption of the new HKFRSs had no material effect on how the results and financial position for the current or prior accounting periods have been prepared and presented. Accordingly, no prior period adjustment has been required.

The Group has not early applied the following new standard, amendments and interpretations that have been issued but are not yet effective. The Directors of the Company anticipate that the application of these standard, amendments and interpretations will have no material impact on the results and the financial position of the Group.

HKAS 1 (Amendment)	Capital disclosures[1]
HKFRS 7	Financial instruments: Disclosures[1]
HKFRS 8	Operating Segments[2]
HK(IFRIC) – Int 7	Applying the restatement approach under HKAS29 Financial Reporting in Hyperinflationary Economies[3]
HK(IFRIC) – Int 8	Scope of HKFRS 2[4]
HK(IFRIC) – Int 9	Reassessment of embedded derivatives[5]
HK(IFRIC) – Int 10	Interim financial reporting and impairment[6]
HK(IFRIC) – Int 11	HKFRS 2 – Group and Treasury Share Transactions[7]
HK(IFRIC) – Int 12	Service Concession Arrangements[8]

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

[1] Effective for annual periods beginning on or after January 1, 2007

[2] Effective for annual periods beginning on or after January 1, 2009

[3] Effective for annual periods beginning on or after March 1, 2006

[4] Effective for annual periods beginning on or after May 1, 2006

[5] Effective for annual periods beginning on or after June 1, 2006

[6] Effective for annual periods beginning on or after November 1, 2006

[7] Effective for annual periods beginning on or after March 1, 2007

[8] Effective for annual periods beginning on or after January 1, 2008

3. SIGNIFICANT ACCOUNTING POLICIES

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

The consolidated financial statements have been prepared in accordance with the Hong Kong Financial Reporting Standards issued by the HKICPA. In addition, the consolidated financial statements include applicable disclosures required by the Listing Rules and by the Hong Kong Companies Ordinance.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

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.

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Interests in associates

An associate is an entity over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture.

The results and assets and liabilities of associates are incorporated in these 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 profit and loss and 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, 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 relevant 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.

Interests in jointly 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, 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.

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Intellectual property rights

On initial recognition, intellectual property rights acquired separately are recognised at cost. After initial recognition, intellectual property rights with finite useful lives are carried at cost less accumulated amortisation and any accumulated impairment losses. Amortisation for intellectual property rights with finite useful lives is provided on a straight-line basis over their estimated useful lives.

Intellectual property rights with finite useful lives are tested for impairment when there is an indication that an asset may be impaired (see the accounting policy in respect of impairment losses below).

Revenue recognition

Revenue is measured at 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 discount and sales related taxes.

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

Service income is recognised when services are provided.

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.

Service income

Service income represents the income from providing management services to jointly controlled entities.

Property, plant and equipment

Property, plant and equipment, other than construction in progress and freehold land, are stated at cost less subsequent accumulated depreciation and accumulated impairment losses.

Depreciation is provided to write off the cost of items of property, plant and equipment, other than construction in progress and freehold land, over their estimated useful lives and after taking into account their estimated residual values, using the straight-line method, at the following rates per annum:

Buildings	Over the terms of the leases or 5%
Leasehold improvements	10%
Plant and machinery	10% – 20%
Furniture and equipment	20%
Motor vehicles	20%
Moulds and tools	20%

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Property, plant and equipment *(Continued)*

Freehold land and construction in progress are carried at cost less any identified impairment losses. Depreciation of construction in progress 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).

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 consolidated income statement in the year in which the item is derecognised.

Impairment losses

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible 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.

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.

Leasing

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

Rentals payable under operating leases are charged to consolidated income statement on a straight-line basis over the term of the relevant leases. 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.

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 the respective 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 that are measured in terms of historical cost in a foreign currency are not retranslated.

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Foreign currencies *(Continued)*

Exchange differences arising on the settlement of monetary items, and on the translation of monetary items, are recognised in profit or loss in the year in which they arise, except for exchange differences arising on a monetary item that forms part of the Group's net investment in a foreign operation, in which case, such exchange differences are recognised in equity in the consolidated financial statements.

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. Hong Kong 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 year, 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 differences are recognised in the consolidated income statement in the year in which the foreign operation is disposed of.

Borrowing costs

All borrowing costs are recognised as and included in finance costs in the consolidated income statement in the year in which they are incurred.

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 profit as reported in the consolidated income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes 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 recognised on differences between the carrying amount of assets and liabilities in the consolidated 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 (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Taxation *(Continued)*

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries, 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 profit 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 year when the liability is settled or the asset is realised. Deferred tax is charged or credited to profit or loss, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using the weighted average method.

Retirement benefits costs

Payments to defined contribution retirement benefits plans, state-managed retirement benefit schemes and the Mandatory Provident Fund Scheme are charged as an expense when employees have rendered service entitling them to the contributions.

Research and development expenditure

Expenditure on research activities is recognised as an expense in the period in which it is incurred.

An internally-generally intangible asset arising from development expenditure is recognised only if it is anticipated that the development costs incurred on a clearly-defined project will be recovered through future commercial activity. The resultant asset is amortised on a straight-line basis over its useful life, and carried at cost less subsequent accumulated amortisation and any accumulated impairment losses.

Where no internally-generated intangible asset can be recognised, development expenditure is recognised as an expense in the year in which it is incurred.

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Financial instruments

Financial assets and financial liabilities are recognised on the balance sheet when the Group 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

The Group's financial assets are classified into financial assets at fair value through profit and loss and loans and receivables. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace. The accounting policies adopted in respect of each category of financial assets are set out below.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets designated at fair value through profit or loss on initial recognition (including structured deposits).

A financial asset may be designated as at fair value through profit or loss upon initial recognition if it forms part of a contract containing one or more embedded derivatives, and HKAS 39 permits the entire combined contract (asset or liability) to be designated as at fair value through profit or loss.

At each balance sheet date subsequent to initial recognition, financial assets 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 year in which they arise.

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, amount due from a jointly controlled entity and bank balances and deposits) 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 years 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.

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Financial instruments *(Continued)*

Financial liabilities and equity

Financial liabilities and equity instruments issued by the Group 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 after deducting all of its liabilities. The Group's financial liabilities are generally classified into other financial liabilities. The accounting policies adopted in respect of financial liabilities and equity instruments are set out below.

Other financial liabilities

Other financial liabilities including trade and other payables, amount due to a jointly controlled entity and borrowings are subsequently measured at amortised cost, using the effective interest rate method after initial recognition.

Convertible loan notes contain liability, conversion option derivative and early redemption option derivative components

Convertible loan notes issued by the Company that contain liability, conversion option derivative and early redemption option derivative components are classified separately into respective items on initial recognition. Conversion option will be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the Company's own equity instruments is a conversion option derivative. At the date of issue, the liability, conversion option derivative and early redemption option derivative components are recognised at fair value.

In subsequent periods, the liability component of the convertible loan notes is carried at amortised cost using the effective interest method. The conversion option derivative and the early redemption option derivative are measured at fair value with change in fair values recognised in profit or loss.

Transaction costs that relate to the issue of the convertible loan notes are allocated to the liability conversion option derivative and early redemption option derivative components in proportion to the allocation of the proceeds. Transaction costs relating to the conversion option derivative and early redemption option derivative are charged to profit or loss immediately. Transaction costs relating to the liability component are included in the carrying amount of the liability portion and amortised over the period of the convertible loan notes using the effective interest method.

Equity instruments

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

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Financial instruments *(Continued)*

Financial liabilities and equity (Continued)

Derivative financial instruments and hedging

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

Derivatives of the Group do not qualify for hedge accounting thus they 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.

Embedded derivatives

Derivatives embedded in non-derivative host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not measured at fair value with changes in fair value recognised 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 receivable and the cumulative gain or loss that had been recognised directly in equity is recognised in profit or loss.

Financial liabilities are derecognised 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 paid and payable is recognised in profit or loss.

Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, and it is probable that the Group will be required to settle that obligation. Provisions are measured at the directors' best estimate of the expenditure required to settle the obligation at the balance sheet date, and are discounted to present value where the effect is material.

4. KEY SOURCES OF ESTIMATION UNCERTAINTY

The key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are also discussed below.

Income taxes

No deferred tax asset has been recognised in respect of tax losses of approximately HK$156,000,000 due to the unpredictability of future profit streams. In cases where the actual future profits generated are more than expected, a material deferred tax asset may be recognised.

Valuation of the embedded derivatives in convertible loan notes

The fair values for the embedded derivatives in convertible loan notes are established by using valuation techniques. The Group has established a process to ensure that valuation techniques are developed by qualified personnel and are validated and reviewed by personnel independent of the area that developed the valuation techniques. Valuation techniques are certified before being implemented for valuation and are calibrated to ensure that outputs reflect actual market conditions. However, it should be noted that some inputs, such as credit and counterparty risk and risk correlations, volatility of share price and dividend yield of the Company, require management estimates. Management estimates and assumptions are reviewed periodically and are adjusted if necessary. Should any of the estimates and assumptions changed, it may lead to a change in the fair value of the embedded derivatives in convertible loan notes.

5. FINANCIAL INSTRUMENTS

a. Financial risk management objectives and policies

The Group's major financial instruments include trade and other receivables, bank balances and deposits, trade and other payables, amount due from (and to) jointly controlled entities, convertible loan notes and borrowings. 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

Several subsidiaries of the Company have foreign currency sales and purchases in United States Dollars ("USD"), Euro ("EUR"), Swiss Franc ("CHF") and Renminbi ("RMB"), which expose the Group to foreign currency risk. Certain trade receivables and trade payables 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 consider hedging significant foreign currency exposure should the need arise.

5. FINANCIAL INSTRUMENTS *(Continued)*

a. Financial risk management objectives and policies *(Continued)*

Interest rate risk

The Group's fair value interest rate risk and cash flow interest rate risk relates to the Group's zero coupon convertible loan notes and borrowings with fixed interest rates and floating interest rates. The Group is exposed to interest rate risk through the impact of rate changes on interest bearing borrowings and convertible loan notes. The interest rates and terms of repayment of convertible loan notes and borrowings of the Group are disclosed in notes 26 and 27, respectively.

The Group currently does not have an interest rate hedging policy. However, the management monitors interest rate change exposure and will consider hedging significant interest rate change exposure should the need arise.

Credit risk

The Group's maximum exposure to credit risk in the event of the counterparties' failure to perform their obligations as at December 31, 2006 in relation to each class of recognised financial assets is the carrying amount of those assets as stated in the consolidated balance sheet. 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 debt 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.

Although the bank balances and deposits are concentrated on certain counterparties, the credit risk on liquid funds is limited because the counterparties are banks with high crediting ratings assigned by international credit rating agencies.

The Group has no significant concentration of credit risk, with exposure spread over a number of counterparties and customers.

Price risk

The Group is exposed to security price risk in respect of the conversion option and early redemption option embedded in the convertible loan notes which allows the notes holders to convert to the Company's ordinary shares.

5. FINANCIAL INSTRUMENTS *(Continued)*

b. Fair value of financial instruments

The fair value of financial assets and financial liabilities are determined as follows:

- the fair value of other financial assets and financial liabilities (excluding derivative instruments) are determined in accordance with generally accepted pricing models based on discounted cash flow analysis or using prices from observable current market transaction and

- the fair value of a non-option derivative is estimated using discounted cash flow analysis and the applicable yield curve. For an option-based derivative, the fair value is estimated using option pricing models (for example, the binomial model).

The Directors consider that the carrying amounts of financial assets and financial liabilities recorded at amortised cost in the financial statements approximate their fair values.

6. REVENUE AND BUSINESS AND GEOGRAPHICAL SEGMENTS

Business segments

Revenue is measured at fair value of the consideration received and receivable and represents amounts receivable for goods sold to outside customers, less returns and allowances.

For management purposes, the Group is currently organised into three operating divisions – manufacture and sale of dyeing and finishing machines, trading of stainless steel supplies and manufacture and sale of stainless steel casting products. These divisions are the basis on which the Group reports its primary segment information.

The unallocated corporate assets include mainly bank balances, deposits and cash and the unallocated corporate liabilities include mainly borrowings and convertible loan notes.

6. REVENUE AND BUSINESS AND GEOGRAPHICAL SEGMENTS *(Continued)*

Business segments *(Continued)*

Segment information about these businesses is presented below:

2006

	Manufacture and sale of dyeing and finishing machines HK$'000	Trading of stainless steel supplies HK$'000	Manufacture and sale of stainless steel casting products HK$'000	Eliminations HK$'000	Consolidated HK$'000
REVENUE					
External sales	1,312,912	809,195	257,929	–	2,380,036
Inter-segment sales	58,116	383,171	31,792	(473,079)	–
Total	1,371,028	1,192,366	289,721	(473,079)	2,380,036
RESULTS					
Segment results	95,663	145,275	35,222	–	276,160
Interest income					18,489
Gain on fair value change of the derivative components of convertible loan notes					11,001
Loss on fair value change of financial instruments					(2,527)
Finance costs					(49,817)
Share of results of an associate					8,893
Share of results of jointly controlled entities	46,740				46,740
Profit before tax					308,939
Income tax expense					(48,906)
Profit for the year					260,033

Inter-segment sales are charged at terms agreed between relevant parties.

6. REVENUE AND BUSINESS AND GEOGRAPHICAL SEGMENTS *(Continued)*

Business segments *(Continued)*

2006 *(Continued)*

CONSOLIDATED BALANCE SHEET

	Manufacture and sale of dyeing and finishing machines HK$'000	Trading of stainless steel supplies HK$'000	Manufacture and sale of stainless steel casting products HK$'000	Consolidated HK$'000
ASSETS				
Segment assets	879,556	372,363	265,277	1,517,196
Interests in an associate				42,431
Interests in jointly controlled entities	81,312			81,312
Unallocated corporate assets				714,597
Consolidated total assets				2,355,536
LIABILITIES				
Segment liabilities	261,252	22,973	60,204	344,429
Unallocated corporate liabilities				994,731
Consolidated total liabilities				1,339,160

OTHER INFORMATION

	Manufacture and sale of dyeing and finishing machines HK$'000	Trading of stainless steel supplies HK$'000	Manufacture and sale of stainless steel casting products HK$'000	Consolidated HK$'000
Capital additions	39,518	1,901	12,233	53,652
Depreciation and amortisation	30,666	879	2,980	34,525
(Gain) loss on disposal of property, plant and equipment	(36)	–	1,080	1,044
(Reversal of) allowance for inventories	(452)	–	2,106	1,654
Allowance for (reversal of) doubtful debts	523	(74)	(1,319)	(870)
Increase in warranty provision	13,200	–	–	13,200

6. REVENUE AND BUSINESS AND GEOGRAPHICAL SEGMENTS

(Continued)

Business segments *(Continued)*

2005

	Manufacture and sale of dyeing and finishing machines HK$'000	Trading of stainless steel supplies HK$'000	Manufacture and sale of stainless steel casting products HK$'000	Eliminations HK$'000	Consolidated HK$'000
REVENUE					
External sales	1,162,714	646,466	203,072	–	2,012,252
Inter-segment sales	64,297	265,978	22,827	(353,102)	–
Total	1,227,011	912,444	225,899	(353,102)	2,012,252
RESULTS					
Segment results	129,295	64,192	27,578	–	221,065
Interest income					2,576
Finance costs					(17,242)
Share of results of an associate					2,054
Share of results of a jointly controlled entity	32,253				32,253
Profit before tax					240,706
Income tax expense					(22,510)
Profit for the year					218,196

Inter-segment sales are charged at terms agreed between relevant parties.

6. REVENUE AND BUSINESS AND GEOGRAPHICAL SEGMENTS *(Continued)*

Business segments *(Continued)*

2005 *(Continued)*

CONSOLIDATED BALANCE SHEET

	Manufacture and sale of dyeing and finishing machines HK$'000	Trading of stainless steel supplies HK$'000	Manufacture and sale of stainless steel casting products HK$'000	Consolidated HK$'000
ASSETS				
Segment assets	632,450	150,894	120,229	903,573
Interests in an associate				33,142
Interests in a jointly controlled entity	60,751			60,751
Unallocated corporate assets				324,697
Consolidated total assets				1,322,163
LIABILITIES				
Segment liabilities	176,884	23,792	32,788	233,464
Unallocated corporate liabilities				214,142
Consolidated total liabilities				447,606

OTHER INFORMATION

	Manufacture and sale of dyeing and finishing machines HK$'000	Trading of stainless steel supplies HK$'000	Manufacture and sale of stainless steel casting products HK$'000	Consolidated HK$'000
Capital additions	20,536	156	3,108	23,800
Increase in prepaid lease payments	394	–	–	394
Depreciation and amortisation	27,525	961	3,775	32,261
(Gain) loss on disposal of property, plant and equipment and prepaid lease payments	(10,836)	2	26	(10,808)
Allowance for inventories	–	–	985	985
(Reversal of) allowance for doubtful debts	(173)	(484)	2,816	2,159
Increase in warranty provision	12,239	–	–	12,239

6. REVENUE AND BUSINESS AND GEOGRAPHICAL SEGMENTS

(Continued)

Geographical segments

The Group's operations are located mainly in Hong Kong, the People's Republic of China (the "PRC"), Germany and Switzerland.

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

	Revenue by geographical market	
	2006	2005
	HK$'000	HK$'000
The PRC	**875,647**	780,340
Hong Kong	**590,674**	581,100
Asia Pacific (other than the PRC and Hong Kong)	**484,353**	273,608
Europe	**222,063**	207,148
North and South America	**154,350**	149,616
Others	**52,949**	20,440
	2,380,036	2,012,252

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

	Carrying amount of segment assets		Additions to property, plant and equipment	
	2006	2005	**2006**	2005
	HK$'000	HK$'000	**HK$'000**	HK$'000
The PRC	**651,456**	433,103	**42,445**	15,803
Hong Kong	**619,096**	335,159	**6,646**	4,302
Europe	**241,257**	135,311	**4,340**	3,695
Asia Pacific (other than the PRC and Hong Kong)	**5,387**	–	**221**	–
	1,517,196	903,573	**53,652**	23,800

7. FINANCE COSTS

	2006 HK$'000	2005 HK$'000
Interest on:		
Bank borrowings wholly repayable within five years	**12,178**	11,930
Obligations under finance leases	**–**	29
Effective interest expense on convertible loan notes	**29,089**	–
Bank charges	**6,640**	4,051
Issue cost of convertible loan notes in respect of the embedded derivative components	**1,217**	–
Factoring charges	**693**	1,232
	49,817	17,242

8. PROFIT BEFORE TAX

	2006 HK$'000	2005 HK$'000
Profit before tax has been arrived at after charging (crediting):		
Amortisation of intellectual property rights	**2,892**	2,892
Amortisation of prepaid lease payments	**341**	370
Depreciation of property, plant and equipment	**31,292**	28,999
Total depreciation and amortisation	**34,525**	32,261
Allowance for inventories	**1,654**	985
(Reversal of) allowance for doubtful debts	**(870)**	2,159
Auditor's remuneration	**2,437**	1,417
Cost of inventories recognised as an expense	**1,695,783**	1,449,305
Loss (gain) on disposal of property, plant and equipment	**1,044**	(67)
Gain on disposal of prepaid lease payments	**–**	(10,741)
Loss on disposal of a subsidiary	**–**	1,658
Net foreign exchange (gain) loss	**(23,214)**	820
Research and development costs	**687**	1,330
Staff costs, including directors' emoluments		
Salaries, wages and other benefits	**180,094**	159,470
Retirement benefits scheme contributions	**16,840**	14,303
	196,934	173,773
Share of tax of an associate (included in share of results of an associate)	**3,428**	339
Share of tax of jointly controlled entities (included in share of results of jointly controlled entities)	**2,801**	4,944

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(For the year ended December 31, 2006)

9. DIRECTORS' AND EMPLOYEES' EMOLUMENTS

(a) Directors' emoluments

The emoluments paid or payable to each of the twelve (2005: fourteen) Directors were as follows:

	Executive directors								Independent non-executive directors				
	Wan Wai Yung HK$'000	Fong Sou Lam HK$'000	Fong Kwok Chung, Bill HK$'000	Fong Kwok Leung, Kevin HK$'000	Tsui Wai Keung HK$'000	Tsui Tak Ming, William HK$'000	Poon Hang Sim, Blanche HK$'000	Peter Rainer Philipp HK$'000	Yuen Ming Fai HK$'000	Cheung Chiu Fan HK$'000	Lui Chi Lung, Louis HK$'000	Keung Wing Ching HK$'000	Total HK$'000
2006													
Fees	–	–	–	–	–	–	–	–	64	64	42	44	214
Other emoluments:													
Salaries and other benefits	4,008	3,250	2,103	1,780	1,300	1,300	1,068	562	–	–	–	–	15,371
Performance related incentive payments	–	–	700	400	700	400	315	–	–	–	–	–	2,515
Retirement benefits scheme contributions	243	240	141	96	96	83	76	–	–	–	–	–	975
Total emoluments	4,251	3,490	2,944	2,276	2,096	1,783	1,459	562	64	64	42	44	19,075

	Executive directors											Independent non-executive directors			
	Wan Wai Yung HK$'000	Lee Che Chiu HK$'000	Fong Sou Lam HK$'000	Fong Kwok Chung, Bill HK$'000	Fong Kwok Leung, Kevin HK$'000	Tsui Tak Ming, William HK$'000	Poon Hang Sim, Blanche HK$'000	Tsui Wai Keung HK$'000	Peter Rainer Philipp HK$'000	Mo Yiu Leung, Jerry HK$'000	Cheuk Hon Kin, Kelvin HK$'000	Yuen Ming Fai HK$'000	Cheung Chiu Fan HK$'000	Lui Chi Lung, Louis HK$'000	Total HK$'000
2005															
Fees	–	–	–	–	–	–	–	–	–	–	–	50	50	50	150
Other emoluments:															
Salaries and other benefits	3,340	2,614	3,250	2,103	1,775	1,299	1,010	1,298	1,346	1,659	1,198	–	–	–	20,892
Performance related incentive payments	668	871	–	248	380	393	260	737	–	560	394	–	–	–	4,511
Retirement benefits scheme contributions	195	12	240	136	96	79	64	96	–	10	88	–	–	–	1,016
Total emoluments	4,203	3,497	3,490	2,487	2,251	1,771	1,334	2,131	1,346	2,229	1,680	50	50	50	26,569

Note: The performance related incentive payments are determined as a percentage of the profit of the Group for the years ended December 31, 2006 and 2005.

No Director waived any emoluments in the years ended December 31, 2006 and 2005.

9. DIRECTORS' AND EMPLOYEES' EMOLUMENTS *(Continued)*

(b) Employees' emoluments

The five highest paid individuals in the Group in 2006 and 2005 were all Directors of the Company and details of their emoluments are included above.

10. INCOME TAX EXPENSE

	2006	2005
	HK$'000	HK$'000
Hong Kong Profits Tax calculated at 17.5% of the estimated assessable profits:		
Current year	**41,875**	21,621
Under(over)provision in prior years	**211**	(404)
Overseas income tax:		
Current year	**7,627**	10,283
Under(over)provision in prior years	**375**	(8,537)
	50,088	22,963
Deferred tax *(note 28)*	**(1,182)**	(453)
	48,906	22,510

Overseas income tax is calculated at rates prevailing in the respective jurisdictions.

The Group's subsidiaries operating in the PRC are eligible for certain tax concessions and part of the income tax was exempted from PRC income tax.

In 2005, a subsidiary obtained approval from the PRC tax authority for granting a concessionary tax rate on taxable profits in 2002 and 2003. An overprovision of overseas income tax in prior years of approximately HK$8,500,000 was thus reversed in last year.

10. INCOME TAX EXPENSE *(Continued)*

The income tax expense for the year can be reconciled to the profit per the income statement as follows:

	2006 HK$'000	2005 HK$'000
Profit before tax	**308,939**	240,706
Tax at the Hong Kong Profits Tax rate of 17.5%	**54,064**	42,123
Tax effect of:		
– expenses that are not deductible for tax purpose	**7,779**	935
– income that are not taxable for tax purpose	**(14,151)**	(5,741)
– tax losses not recognised	**16,300**	6,399
– share of results of an associate	**(1,556)**	(359)
– share of results of jointly controlled entities	**(8,180)**	(5,644)
Income tax on concessionary rate	**(1,917)**	(2,492)
Effect of different tax rates of subsidiaries operating in other jurisdictions	**(3,910)**	(3,711)
Under(over)provision in prior years	**586**	(8,941)
Others	**(109)**	(59)
Income tax expense for the year	**48,906**	22,510

11. DIVIDENDS/SPECIAL DIVIDEND

	2006 HK$'000	2005 HK$'000
Dividends recognised as distribution during the year:		
Interim dividend of 8 HK cents (2005: 8 HK cents) per share	**44,688**	44,830
Final dividend of 5 HK cents (2005: 7 HK cents) per share	**28,019**	39,227
	72,707	84,057
Interim special dividend of 3 HK cents (2005: 3 HK cents) per share	**16,758**	16,811
Final special dividend of 7 HK cents (2005: 7 HK cents) per share	**39,226**	39,226
	55,984	56,037

11. DIVIDENDS/SPECIAL DIVIDEND *(Continued)*

The final dividend and final special dividend of 8 HK cents and 7 HK cents, respectively, per share have been proposed by the Directors and is subject to approval by the shareholders at the forthcoming annual general meeting.

12. EARNINGS PER SHARE

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

	2006	2005
	HK$'000	HK$'000
Earnings		
Profit for the year attributable to equity holders of the parent	**260,033**	218,653
Effect of dilutive potential ordinary shares:		
Interest on convertible loan notes	**29,089**	–
Gain on fair value change on convertible loan notes	**(11,001)**	–
Earnings for the purposes of diluted earnings per share	**278,121**	218,653

	2006	2005
	'000	'000
Number of shares		
Weighted average number of ordinary shares for the purposes of basic earnings per share	**559,525**	560,378
Effect of dilutive potential ordinary shares:		
Convertible loan notes	**61,799**	
Weighted average number of ordinary shares for the purposes of diluted earnings per share	**621,324**	

13. PROPERTY, PLANT AND EQUIPMENT

	Freehold land	Buildings	Leasehold improvements	Plant and machinery	Furniture and equipment	Motor vehicles	Moulds and tools	Construction in progress	Total
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
COST									
At January 1, 2005	9,563	200,244	5,040	133,931	52,926	17,107	6,052	19,299	444,162
Currency realignment	–	3,651	56	2,079	(381)	11	75	371	5,862
Additions	–	809	1,761	10,924	6,671	1,842	381	1,412	23,800
Disposals	–	(413)	–	(206)	(537)	(1,580)	–	–	(2,736)
At December 31, 2005 and January 1, 2006	9,563	204,291	6,857	146,728	58,679	17,380	6,508	21,082	471,088
Currency realignment	–	9,271	119	6,425	1,685	227	190	844	18,761
Transfer	–	24,588	–	574	–	–	–	(25,162)	–
Additions	–	–	1,807	26,888	10,321	3,451	151	11,034	53,652
Disposals	–	–	–	(9,819)	(6,440)	(880)	–	–	(17,139)
At December 31, 2006	**9,563**	**238,150**	**8,783**	**170,796**	**64,245**	**20,178**	**6,849**	**7,798**	**526,362**
DEPRECIATION AND AMORTISATION									
At January 1, 2005	–	72,922	2,003	58,061	36,621	11,437	4,546	–	185,590
Currency realignment	–	1,398	12	1,041	87	37	76	–	2,651
Provided for the year	–	9,155	734	11,279	5,295	2,278	258	–	28,999
Eliminated on disposals	–	(91)	–	(179)	(469)	(1,302)	–	–	(2,041)
At December 31, 2005 and January 1, 2006	–	83,384	2,749	70,202	41,534	12,450	4,880	–	215,199
Currency realignment	–	3,347	49	2,987	969	154	171	–	7,677
Provided for the year	–	10,165	962	11,258	6,742	1,911	254	–	31,292
Eliminated on disposals	–	–	–	(8,818)	(6,303)	(687)	–	–	(15,808)
At December 31, 2006	**–**	**96,896**	**3,760**	**75,629**	**42,942**	**13,828**	**5,305**	**–**	**238,360**
NET BOOK VALUES									
At December 31, 2006	**9,563**	**141,254**	**5,023**	**95,167**	**21,303**	**6,350**	**1,544**	**7,798**	**288,002**
At December 31, 2005	9,563	120,907	4,108	76,526	17,145	4,930	1,628	21,082	255,889

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

An analysis of the Group's freehold land and buildings is as follows:

	2006 HK$'000	2005 HK$'000
Buildings on long leases located in the PRC	**90**	91
Buildings on medium-term leases located in the PRC	**128,685**	109,295
Buildings on medium-term leases located in Hong Kong	**67**	69
Freehold land and buildings in Europe	**21,975**	21,015
	150,817	130,470

At December 31, 2005, the Group pledged the buildings on medium-term leases located in Hong Kong to secure banking facilities granted to the Group. The pledge was released in 2006.

14. PREPAID LEASE PAYMENTS

	2006 HK$'000	2005 HK$'000
The Group's prepaid lease payments comprise:		
Leasehold land in Hong Kong:		
Medium-term leases	**410**	422
Leasehold land in the PRC:		
Long leases	**381**	388
Medium-term leases	**11,189**	11,187
	11,980	11,997
Analysed for reporting purposes as:		
Current asset	**341**	332
Non-current asset	**11,639**	11,665
	11,980	11,997

At December 31, 2005, the Group pledged the prepaid lease payments relating to the medium-term leasehold land in Hong Kong to secure banking facilities granted to the Group. The pledge was released in 2006.

15. INTELLECTUAL PROPERTY RIGHTS

	HK$'000
COST	
At January 1, 2005, December 31, 2005, January 1, 2006 and December 31, 2006	28,923
AMORTISATION	
At January 1, 2005	1,205
Provided for the year	2,892
At December 31, 2005 and January 1, 2006	4,097
Provided for the year	2,892
At December 31, 2006	**6,989**
CARRYING AMOUNT	
At December 31, 2006	**21,934**
At December 31, 2005	24,826

Intellectual property rights represent technical know-how skills for manufacturing of machines and are amortised on a straight-line basis over ten years.

16. INTERESTS IN AN ASSOCIATE

	2006 HK$'000	2005 HK$'000
Cost of unlisted investment in an associate	**46,469**	46,469
Share of post-acquisition results, net of dividends received	**(4,038)**	(13,327)
Share of net assets	**42,431**	33,142

At the balance sheet date, the principal associate of the Group represented a 30% interest in Foshan East Asia Company Limited ("Foshan East Asia"), a sino-foreign equity enterprise registered and operated in the PRC. It acts as a holding company and its subsidiaries are engaged in the manufacture of colour woven fabrics.

16. INTERESTS IN AN ASSOCIATE *(Continued)*

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

	2006 HK$'000	2005 HK$'000
Revenue	226,474	192,144
Profit for the year	29,643	6,846
Profit attributable to the Group	8,893	2,054
Financial position:		
Total non-current assets	108,491	116,088
Total current assets	228,555	206,657
Total non-current liabilities	(65,952)	(89,828)
Total current liabilities	(122,659)	(116,025)
Minority interests	(6,999)	(6,419)
	141,436	110,473
Shareholders' funds attributable to the Group	42,431	33,142

17. INTERESTS IN JOINTLY CONTROLLED ENTITIES

	2006 HK$'000	2005 HK$'000
Cost of unlisted investment in jointly controlled entities	10,779	9,200
Share of post-acquisition profits, net of dividends received	70,533	51,551
Share of net assets	81,312	60,751

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

As at December 31, 2006, the Group had interests in the following significantly jointly controlled entities:

Name of entity	Place of incorporation or registration/ operations	Nominal value of issued capital/ registered capital	Proportion of share capital/ registered capital/ attributable to the Group	Principal activities
Monforts Fong's Textile Machinery Co., Ltd.	Hong Kong/ The PRC	HK$9,200,000	50%	Manufacture and trading of textile machinery
Monforts Fong's Textile Machinery (Macao Commercial Offshore) Co., Ltd.	Macau	MOP50,000	50%	Trading of textile machinery
Plexxor Co., Ltd.	Hong Kong	HK$3,000,000	51%	Trading of textile machinery

The Group holds 51% of the share capital of Plexxor Co., Limited and controls 51% of the voting power at general meetings. However under a shareholders' agreement. Plexxor Co., Limited is jointly controlled by the Group and the other significant shareholder. Therefore, Plexxor Co., Limited is classified as a jointly controlled entity of the Group.

The summarised financial information in respect of the Group's jointly controlled entities which are accounted for using the equity method is set out below:

	2006 HK$'000	2005 HK$'000
Income	**314,350**	217,178
Expense	**267,610**	184,925
Profit attributable to the Group	**46,740**	32,253
Financial position:		
Total non-current assets	**26,783**	21,236
Total current assets	**114,081**	87,745
Total non-current liabilities	**(32)**	(36)
Total current liabilities	**(59,520)**	(48,194)
	81,312	60,751

18. INVENTORIES

	2006 HK$'000	2005 HK$'000
Raw materials	**519,055**	207,951
Work in progress	**158,562**	85,921
Finished goods	**100,755**	74,101
	778,372	367,973

19. TRADE AND OTHER RECEIVABLES

	2006 HK$'000	2005 HK$'000
Trade receivables	**267,742**	159,064
Less: Allowance for doubtful debts	**(17,339)**	(19,058)
	250,403	140,006
Bills receivables	**100,050**	59,692
	350,453	199,698
Other receivables	**54,022**	26,987
Total trade and other receivables	**404,475**	226,685

The Group allows an average credit period of 60 days (2005: 60 days) to its trade customers.

The following is an aged analysis of trade receivables net of allowance for doubtful debts and bills receivables at the balance sheet date:

	2006 HK$'000	2005 HK$'000
0-30 days	**324,846**	191,535
31-60 days	**14,990**	4,975
Over 60 days	**10,617**	3,188
	350,453	199,698

At December 31, 2005, the Group pledged trade receivables at a carrying value of HK$10,206,000 to secure credit facilities granted to the Group. The pledge was released in 2006.

19. TRADE AND OTHER RECEIVABLES *(Continued)*

The Group's trade receivables denominated in currencies other than the functional currencies of the relevant group entities are set out below:

	USD'000	*EUR'000*	*CHF'000*	*RMB'000*
As at December 31, 2006	19,876	4,252	1,124	21,623
As at December 31, 2005	13,093	1,523	1,112	9,575

20. AMOUNT DUE FROM (AND TO) JOINTLY CONTROLLED ENTITIES

The amount, which is aged within 60 days, is unsecured, interest-free and repayable on demand.

21. DERIVATIVE FINANCIAL INSTRUMENTS

	2006		2005	
	Assets HK$'000	**Liabilities HK$'000**	Assets HK$'000	Liabilities HK$'000
Foreign currency forward contract	**27**	**–**	–	–
Foreign currency forward contract	**–**	**244**	–	–
	27	**244**	–	–

At December 31, 2006, the Group had the following foreign currency forward contracts dominated in USD and EUR, the major terms of these contracts are as follows:

Notional amount	**Maturity**	**Exchange rate**
Buy USD500,000 (if market rate at the date of settlement is above USD1 to HK$7.738) or buy USD1,000,000 (if market rate at the date of settlement is equal to or below USD1 to HK$7.738)	February 9, 2007	USD1 to HK$7.738
Sell EUR1,000,000 (if market rate at the date of settlement is greater than USD1 to EUR1.157 and equal to or less than USD1 to EUR1.247) or sell EUR2,000,000 (if market rate is greater than USD1 to EUR1.247)	March 15, 2007	USD1 to EUR1.247

The fair values of other financial assets/liabilities have been determined based on the quoted market price provided by the bank for equivalent instruments at the balance sheet date. All fair value adjustments are recognised in the consolidated income statement.

22. STRUCTURED DEPOSITS

Structured deposits are stated at fair value and represent deposits placed in a bank, which bear interest rates ranging from 7% to 8.5% per annum when the London Interbank Offered Rate ("LIBOR") fixing with a designated maturity of 12 months minus LIBOR fixing with a designated maturity of 3 months (the "Rate") is greater than or equals to 0.15% or 0.18%. No interest will be received if the Rate is lower than 0.15% or 0.18%. The structured deposits will mature in 2007. The Group designated the structured deposits as at fair value through profit or loss. The fair value of the structured deposits has been determined based on the present value of estimated future cash flows discounted at the effective interest rate of 3.5% per annum provided by the bank at the balance sheet date.

23. BANK BALANCES, DEPOSITS AND CASH

The amount includes short-term fixed deposits which carry fixed interest rate ranging from 2% to 4.85% per annum (2005: 0.25% to 3.9% per annum).

24. TRADE AND OTHER PAYABLES

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

	2006 **HK$'000**	2005 HK$'000
0-30 days	**64,174**	53,925
31-60 days	**10,893**	5,107
Over 60 days	**3,028**	2,969
	78,095	62,001

The Group's trade payables denominated in currencies other than the functional currencies of the relevant group entities are set out below:

	USD'000	EUR'000	CHF'000	RMB'000
As at December 31, 2006	1,023	1,294	982	20,611
As at December 31, 2005	1,417	1,266	706	12,649

25. WARRANTY PROVISION

	2006	2005
	HK$'000	HK$'000
At January 1	**12,299**	11,065
Additional provision in the year	**13,200**	12,239
Utilisation of provision	**(12,235)**	(11,005)
At December 31	**13,264**	12,299

The warranty provision represents the management's best estimate of the Group's liability under a 12-month warranty period granted on the sale of dyeing and finishing machines based on past experience.

26. CONVERTIBLE LOAN NOTES

The Company issued zero coupon convertible loan notes (the "Notes") in the aggregate principal amount of HK$800,000,000 at a par value of HK$10,000 each on May 10, 2006. Details of the Notes are set out in the Company's circular dated April 16, 2006. The features of the Notes are as follows:

(i) Conversion option:

– The Notes are denominated in Hong Kong dollars. The Notes entitle the holders to convert them into ordinary shares of the Company (the "Share") at any time from and including May 25, 2006 to April 25, 2011 at a conversion price of HK$8.37 per Share. If the arithmetic average of the closing price of the Share for each day during the 15 consecutive the Stock Exchange trading days ending 60 days before each anniversary of the closing date of the Notes is less than the conversion price then in effect, the conversion price may be adjusted downwards at the discretion and option of the Company, such that the adjusted conversion price in no event shall be less than 80% of the initial conversion price. If the Notes have not been converted, they will be redeemed at 124.01% of the principal amount on May 10, 2011 (the "maturity date").

(ii) Holder early redemption option:

– All or some of the Notes may be redeemed at the option of the holders at 111.36% of the principal amount on November 10, 2008.

26. CONVERTIBLE LOAN NOTES *(Continued)*

(iii) Issuer early redemption option:

– On or at any time after November 10, 2008, the Company may redeem all, but not some only, of the Notes at any time prior to the maturity date, at an amount (the "Early Redemption Amount") if (i) the closing price of the Share for each of the 30 consecutive trading days, the last which falls within five trading days prior to the date upon which notice of such redemption is given was at least 130% of the applicable Early Redemption Amount in effect on such trading day divided by the conversion ratio or (ii) at least 90% in principal amount of the Notes has already been converted, redeemed or purchased and cancelled.

– The Early Redemption Amount of the Notes, for each HK$10,000 principal amount of the Notes, is determined so that it represents for the holder a gross yield of 4.35% per annum, calculated on a semi-annual basis.

The convertible loan notes contain liability component, conversion option derivative and two early redemption option derivatives. The conversion option derivative is not closely related to the liability component and is classified as a derivative as the conversion will not result in the Company issuing a fixed number of shares in settlement of a fixed amount of the liability component. The issuer early redemption option derivative is not closely related to the host contract as the early redemption amount is not close to the amortised cost of the liability on the redemption date. Both the conversion option derivative and issuer early redemption option derivative are measured at fair value with change in fair value recognised in profit or loss. The holder early redemption option derivative is not separately recognised from the liability component as the early redemption amount approximates the amortised cost of the liability on the redemption date and it is considered as closely related to the economic characteristics and risks of the host contract.

The fair value of the convertible loan notes with embedded derivatives were determined by the Directors with reference to a valuation report carried out by Vigers Appraisal & Consulting Limited, independent and recognised international business valuers, on May 10, 2006 at HK$774,757,000. At December 31, 2006, the liability component of the convertible loan notes is HK$767,047,000 which is stated at amortised cost using the effective interest method and the fair value of the derivative component of the convertible loan notes is HK$25,798,000. The effective interest expense of convertible loan notes and change in fair value of the embedded derivatives amounting to HK$29,089,000 and HK$11,001,000, respectively, have been recognised in the consolidated income statement for the year ended December 31, 2006.

26. CONVERTIBLE LOAN NOTES *(Continued)*

The methods and assumptions applied for the valuation of the convertible loan notes are as follows:

(1) Valuation of liability component

At the date of issue, the liability component was recognised at fair value. The fair value of liability component was calculated based on the present value of the initial recognition contractually determined stream of future cash flows discounted at the required yield, which was determined with reference to the average yield of notes with similar credit rating and remaining time to maturity. In subsequent periods, the liability component is carried at amortised cost using the effective interest method. The effective interest rate of the liability component is 6.1%.

(2) Valuation of conversion option derivative

Bionomial model is used for valuation of conversion option derivative. The inputs into the model were as follows:

	May 10, 2006	December 31, 2006
Stock price	**HK$6.2**	HK$5.25
Exercise price	**HK$8.37**	HK$8.02
Volatility	**35%**	35%
Dividend yield	**4%**	4%
Option life	**5 years**	4.36 years
Risk free rate	**4.54%**	3.69%

(3) Valuation of issuer early redemption option derivative

Bionomial model is used for valuation of issuer early redemption option derivative. The inputs into the model were as follows:

	May 10, 2006	December 31, 2006
Stock price	**HK$6.2**	HK$5.25
Exercise price	**HK$10.881**	HK$10.426
Volatility	**35%**	35%
Dividend yield	**4%**	4%
Option life	**5 years**	4.36 years
Risk free rate	**4.54%**	3.69%

26. CONVERTIBLE LOAN NOTES *(Continued)*

The movement of the liability component, and the derivative component (including conversion option derivative and issuer redemption option derivative) of the convertible loan notes for the year ended December 31, 2006 is set out as follows:

	Liability component HK$'000	**Derivative component** HK$'000
Carrying amount at May 10, 2006	737,958	36,799
Changes in fair value	–	(11,001)
Effective interest expenses	29,089	–
Carrying amount at December 31, 2006	767,047	25,798

The fair value of derivative component comprises of conversion option derivative of HK$65,347,000 and issuer early redemption option derivative of HK$39,549,000 as at December 31, 2006, which are presented on a net basis as their terms are inter-related.

27. BORROWINGS

	2006 **HK$'000**	2005 HK$'000
Borrowings comprise the following:		
Bank loans	**172,058**	200,000
Other borrowings	**5,055**	7,015
	177,113	207,015
Secured	**–**	157,015
Unsecured	**177,113**	50,000
	177,113	207,015

27. BORROWINGS *(Continued)*

The above amounts are repayable as follows:

	2006	2005
	HK$'000	HK$'000
Within one year	**54,613**	87,015
In the second year	**40,000**	30,000
In the third to fifth years inclusive	**82,500**	90,000
	177,113	207,015
Less: Amount due within one year shown under current liabilities	**(54,613)**	(87,015)
Amount due after one year	**122,500**	120,000

In 2005, the Group had two bank borrowings amounting to HK$50,000,000 in aggregate which were repayable within one year and carried fixed interest rates ranging from 3.825% to 3.900% per annum and two borrowings amounting to approximately HK$157,015,000 in aggregate which carried floating interest rates at Hong Kong Inter-bank Offered Rate ("HIBOR") plus 0.75% per annum and LIBOR plus 2.725% to 2.325% per annum.

In 2006, the Group has a bank borrowing amounting to approximately HK$9,558,000 which is repayable within one year and carries fixed interest rate of 6.75% per annum and the remaining bank borrowings amounting to approximately HK$167,555,000 which carry floating interest rate of HIBOR plus 0.75% per annum and LIBOR plus 1% per annum, respectively.

The Group's borrowings denominated in currencies other than the functional currencies of the relevant group entities are set out below:

	USD$'000	EUR'000	HK$'000
As at December 31, 2006	648	930	–
As at December 31, 2005	–	–	50,000

28. DEFERRED TAX

The major deferred tax liabilities (assets) recognised by the Group and movements thereon during the current and prior years are as follows:

	Accelerated tax depreciation HK$'000	Allowance for doubtful debts HK$'000	Unrealised profit for inventories HK$'000	Others HK$'000	Total HK$'000
At January 1, 2005	908	(2,708)	(550)	(350)	(2,700)
Charge (credit) to the consolidated income statement for the year	97	(378)	(522)	350	(453)
At December 31, 2005 and January 1, 2006	1,005	(3,086)	(1,072)	–	(3,153)
Charge (credit) to the consolidated income statement for the year	102	152	(1,436)	–	(1,182)
At December 31, 2006	**1,107**	**(2,934)**	**(2,508)**	**–**	**(4,335)**

For the purpose of balance sheet presentation, certain deferred tax assets and liabilities have been offset. The following is the analysis of the deferred tax (assets) liabilities for financial reporting purposes:

	2006 HK$'000	2005 HK$'000
Deferred tax assets	**(5,525)**	(4,268)
Deferred tax liabilities	**1,190**	1,115
	(4,335)	(3,153)

At the balance sheet date, the Group had unused tax losses of approximately HK$156,000,000 (2005: HK$63,000,000) available for offset against future profits. No deferred tax asset has been recognised in respect of the tax losses due to the unpredictability of future profit streams. Included in unrecognised tax losses are losses of approximately HK$9,600,000 (2005: HK$9,600,000), HK$2,900,000 (2005: HK$2,900,000), HK$5,400,000 (2005: HK$5,400,000) and HK$6,700,000 (2005: Nil) that will expire in 2010, 2011, 2012 and 2013 respectively. Other losses may be carried forward indefinitely.

29. SHARE CAPITAL OF THE COMPANY

	2006 HK$'000	2005 HK$'000
Authorised:		
1,000,000,000 ordinary shares of HK$0.10 each	**100,000**	100,000
Issued and fully paid:		
At January 1, 2005 and January 1, 2006: 560,378,285 ordinary shares of HK$0.10 each	**56,038**	56,038
Repurchase of shares	**(196)**	–
At December 31, 2006: 558,416,285 (December 31, 2005: 560,378,285) ordinary shares of HK$0.10 each	**55,842**	56,038

During the year ended December 31, 2006, the Company repurchased its own shares through the Stock Exchange as follows:

Month of repurchase	No. of ordinary shares of HK$0.10 each	Price per share Highest HK$	Price per share Lowest HK$	Aggregate consideration paid HK$'000
June	362,000	4.85	4.85	1,756
July	1,384,000	4.875	4.725	6,696
August	30,000	4.87	4.87	146
November	186,000	5.06	5.04	941
	1,962,000			9,539

The above shares were cancelled upon repurchase and accordingly the issued share capital of the Company was reduced by the nominal value of these shares. The premium on repurchase amounting to approximately HK$9,343,000 was charged against share premium. An amount of approximately HK$196,000 equivalents to the nominal value of the cancelled shares was transferred from retained profits to capital redemption reserve.

30. RESERVES AND MINORITY INTERESTS

	Attributable to equity holders of the parent							
	Share premium HK$'000	Dividend reserve HK$'000	Capital redemption reserve HK$'000	Translation reserve HK$'000	Retained profits HK$'000	Contributed surplus HK$'000	Total reserves HK$'000	Minority interests HK$'000
At January 1, 2005	198,725	78,453	1,477	(11,744)	442,368	25,582	734,861	1,747
Exchange difference arising on translation of overseas subsidiaries recognised directly in equity	–	–	–	35	–	–	35	–
Share of changes in equity of an associate and a jointly controlled entity	–	–	–	1,911	–	–	1,911	–
Net income recognised directly in equity	–	–	–	1,946	–	–	1,946	–
Realised on disposal of a subsidiary	–	–	–	1,863	–	–	1,863	–
Profit (loss) for the year	–	–	–	–	218,653	–	218,653	(457)
Total recognised income and expense for the year	–	–	–	3,809	218,653	–	222,462	(457)
Final dividend for 2004 paid	–	(39,227)	–	–	–	–	(39,227)	–
Final special dividend for 2004 paid	–	(39,226)	–	–	–	–	(39,226)	–
Interim dividend for 2005 paid	–	–	–	–	(44,830)	–	(44,830)	–
Interim special dividend for 2005 paid	–	–	–	–	(16,811)	–	(16,811)	–
Proposed final dividend for 2005	–	28,019	–	–	(28,019)	–	–	–
Proposed final special dividend for 2005	–	39,226	–	–	(39,226)	–	–	–
At December 31, 2005 and January 1, 2006	198,725	67,245	1,477	(7,935)	532,135	25,582	817,229	1,290
Exchange difference arising on translation of overseas subsidiaries recognised directly in equity	–	–	–	16,294	–	–	16,294	–
Share of changes in equity of an associate and jointly controlled entities	–	–	–	3,722	–	–	3,722	–
Net income recognised directly in equity	–	–	–	20,016	–	–	20,016	–
Profit for the year	–	–	–	–	260,033	–	260,033	–
Total recognised income and expense for the year	–	–	–	20,016	260,033	–	280,049	–
Repurchases of shares	(9,343)	–	196	–	(196)	–	(9,343)	–
Final dividend for 2005 paid	–	(28,019)	–	–	–	–	(28,019)	–
Final special dividend for 2005 paid	–	(39,226)	–	–	–	–	(39,226)	–
Interim dividend for 2006 paid	–	–	–	–	(44,688)	–	(44,688)	–
Interim special dividend for 2006 paid	–	–	–	–	(16,758)	–	(16,758)	–
Proposed final dividend for 2006	–	44,665	–	–	(44,665)	–	–	–
Proposed final special dividend for 2006	–	39,082	–	–	(39,082)	–	–	–
At December 31, 2006	189,382	83,747	1,673	12,081	646,779	25,582	959,244	1,290

30. RESERVES AND MINORITY INTERESTS *(Continued)*

The contributed surplus of the Group represents the difference between the nominal value of the share capital issued by the Company and the nominal value of the entire issued share capital of Fong's Manufacturers Company Limited, the then holding company, acquired pursuant to a corporate reorganisation on September 13, 1990.

31. SHARE OPTION SCHEME

A share option scheme (the "Scheme") of the Company was approved and adopted on May 26, 2003 for the purpose of providing a flexible means of giving incentive to, rewarding, remunerating, compensating and providing benefits to eligible participants, including the Executive Directors of the Company as determined by the Board of the Directors of the Company.

The Board of Directors of the Company may, at their discretion, grant options to the eligible participant including any employees, directors or consultants of the Group. The maximum number of shares of the Company which may be issued upon exercise of all options granted under the Scheme or any other share option scheme adopted by the Company must not exceed 30% of its issued share capital from time to time. The maximum number of shares issuable under the options to each eligible participant in any 12-month period is limited to 1% of the shares in issue unless it is approved by shareholders in a general meeting of the Company. Any share options granted to a substantial shareholder or an Independent Non-executive Director of the Company or to any of their associates, in excess of 0.1% of the shares in issue and with an aggregate value (based on the closing price of the shares at the date of the grant) in excess of HK$5 million, in any 12-month period, are subject to shareholders' approval in a general meeting of the Company.

Share options granted must be taken up within 28 days of the date of grant. Each of the grantees is required to pay HK$1 as cash consideration for the grant of the share options in accordance with the Scheme. The total number of shares in respect of which share options may be granted shall not exceed 10% of the issued ordinary share capital. The exercise price is determined by the Directors of the Company, and shall not be less than the higher of the closing price of the Company's shares on the date of grant, the average closing price of the shares for the five business days immediately preceding the date of grant and the nominal value of the share.

An option is deemed to have been granted and accepted by the grantee upon his or her signing a duplicate letter comprising acceptance of the option and paying HK$1 by way of consideration for the grant thereof on or before the relevant acceptance date being a date within 28 days after the date on which the option is offered.

31. SHARE OPTION SCHEME *(Continued)*

An option may be exercised in accordance with the terms of the Scheme at any time during the option period after the option has been granted by the Board of Directors. An option period is a period to be determined by the Board of Directors at its absolute discretion and notified by Board of Directors to each grantee as being the period during which an option may be exercised, such period shall commence from the date of acceptance of the offer for the grant of the option and shall end not later than 10 years from the date on which the offer for grant of the option is made.

The Scheme is valid for a period of 10 years commencing on May 26, 2003 and will expire on May 25, 2013.

No share option has been granted by the Company under the Scheme since its adoption.

32. DISPOSAL OF A SUBSIDIARY

On December 20, 2005, the Group disposed of a subsidiary, Front Standard Limited. The net assets of Front Standard Limited at the date of disposal were as follows:

	HK$'000
NET ASSETS DISPOSED OF	
Interest in an associate	1,613
Exchange losses realised	1,863
	3,476
Loss on disposal	1,658
Total consideration	1,818
Satisfied by:	
Cash, which represents the cash inflow from disposal of a subsidiary	1,818

The impact of Front Standard Limited on the Group's results and cash flows in the prior years is insignificant.

33. CAPITAL COMMITMENTS

	2006	2005
	HK$'000	HK$'000
Capital expenditure contracted for but not provided in the consolidated financial statements in respect of the acquisition of property, plant and equipment	**35,301**	3,226

34. OPERATING LEASE ARRANGEMENTS

As lessee

Minimum lease payments paid under operating leases for rented premises during the year amounted to approximately HK$6,442,000 (2005: HK$6,620,000).

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

	2006	2005
	HK$'000	HK$'000
Within one year	**6,048**	6,380
In the second to fifth year inclusive	**462**	5,872
	6,510	12,252

Operating lease payments represent rentals payable by the Group for certain of its office premises and residential units for its employees. Leases are negotiated and rentals are fixed for an average term of three years.

35. RETIREMENT BENEFITS SCHEME

Schemes in Hong Kong

The Group has a defined contribution provident fund scheme (the “Scheme”) for its Hong Kong employees. The scheme assets are being held under a provident fund operated by AXA Rosenberg Investment Management Asia Pacific Limited with Messrs. Fong Sou Lam and Fong Kwok Chung, Bill as trustees and Hastings Service & Company Limited as an additional trustee.

The Group is required to make contributions to the Scheme calculated at 5% of the employees’ basic salaries on a monthly basis. The Group’s contribution will start with 5% and further increase proportionally to a maximum of 8% of each employee’s basic salary after completion of three years of service to the Group. The employees are entitled to 100% of the employers’ contribution and the accrued interest after 10 years of service, or at a reduced scale of between 30% to 100% after completion of 3 to 10 years’ service. The forfeited contributions and related accrued interest are to be used to reduce the employers’ contribution.

In 2000, the principal deed and the rules of the Scheme were amended to comply with the rules of the Mandatory Provident Fund Schemes Ordinance (“MPF Ordinance”).

With effect from December 1, 2000, the Group also participated in Mandatory Provident Fund Scheme (“MPF Scheme”). The MPF scheme assets are held under a mandatory provident fund operated by AXA Rosenberg Investment Management Asia Pacific Limited. Under the MPF Scheme, the Group is required to make contributions to the scheme calculated at lower of 5% of the employees’ relevant income or HK$1,000 (as defined in the MPF Ordinance) on a monthly basis.

The employees entitled to participate in the Scheme before December 1, 2000 were given an option to join the MPF Scheme or to continue making contributions to the Scheme. All other existing or newly employed employees are required to join the MPF Scheme. The Group is required to make contributions to either of the two schemes in accordance with the option selected by the employees.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(For the year ended December 31, 2006)

35. RETIREMENT BENEFITS SCHEME *(Continued)*

Schemes in Hong Kong *(Continued)*

The aggregate employers' contributions, net of forfeited contributions, which have been dealt with in the consolidated income statement of the Group amounted to:

	2006	2005
	HK$'000	HK$'000
Gross employers' contributions	**4,486**	4,166
Less: Forfeited contributions utilised to offset employers' contributions for the year	**(71)**	(63)
Net employers' contributions charged to the consolidated income statement	**4,415**	4,103

At the balance sheet date, there were no significant forfeited contributions available to offset future employers' contributions to the Scheme.

Scheme in the PRC

The employees of the Company's subsidiaries which operate in the PRC are required to participate in a central pension scheme operated by the local municipal government. These PRC subsidiaries are required to contribute 8% to 10% of its payroll costs to the central pension scheme. The contributions are charged to the consolidated income statement as they become payable in accordance with the rules of the central pension scheme.

The total cost charged to the consolidated income statement for the scheme in the PRC amounted to approximately HK$3,692,000 (2005: HK$3,721,000).

Scheme in Germany

In Germany, the Group is obliged to contribute to a social pension programme for employees on a monthly basis at around 9.75% of the employee's gross income. The only obligation of the Group with respect to this social pension programme is to make the specified contribution.

The total cost charged to the consolidated income statement for the social pension programme in Germany amounted to approximately HK$7,488,000 (2005: HK$5,394,000).

35. RETIREMENT BENEFITS SCHEME *(Continued)*

Schemes in Switzerland

In Switzerland, the Group is obligated to contribute to a basic pension plan on a monthly basis at 5.05% of the employee's gross income plus administrative charges.

Besides, the Group also has to participate in a mandatory occupational benefit plan ("the Plan") for all the employees as regulated under the federal law. The Group is obligated to make contributions to the Plan, calculated at 4% to 11.25% of the employees' basic annual salary above CHF 22,257, depending on employees' age plus an individual risk surcharge of about 2%.

The total cost charged to the consolidated income statement for the schemes in Switzerland amounted to approximately HK$1,245,000 (2005: HK$1,085,000).

36. POST BALANCE SHEET EVENT

On April 1, 2007, Tycon Alloy Industries (Hong Kong) Company Limited ("Tycon"), an indirect wholly-owned subsidiary of the Company, entered into a three-year non-exclusive agency agreement (the "Agency Agreement") with PSP International Inc in relation to agency and marketing activities for the sales of its stainless steel casting products in the territories of the USA, Canada and Mexico with effect from April 1, 2007.

Under the Agency Agreement, PSP International Inc. is entitled to a monthly retainer fee and sales commission at the market rate of a prescribed percentage of the net sales proceeds of the sales contracts solicited or procured by it as specified therein. It is anticipated that the aggregate annual amount of the sales commission and other payables during the term of the Agency Agreement will not exceed HK$10 million.

PSP International Inc. is beneficially owned as to 30% by Mr. Peter Rainer Philipp (Mr. Peter Philipp). Mr. Peter Philipp is currently a director of certain operating subsidiaries of the Group, but not a director of Tycon. The transaction constituted a continuing connected transaction of the Company and is exempt from the independent shareholders' approval requirements but subject to the reporting and announcement requirements set out in Chapter 14A of the Listing Rules.

Details of the transaction were set out in the press announcement of the Company dated April 2, 2007.

37. RELATED PARTY DISCLOSURES

Apart from details of the balances with related parties disclosed in the consolidated balance sheet on page 38 and note 20 to the consolidated financial statements, the Group has also entered into the following transactions with related parties during the year:

	2006	2005
	HK$'000	HK$'000
Related parties in which Directors have beneficial interests		
Sale of goods	**299**	695
Service fee paid	**320**	–
Purchase of materials	**562**	283
Commission and agency fee paid	**7,546**	4,771
Management fee received	**–**	306
Management fee paid	**312**	–
Rental paid	**5,928**	5,928
Jointly controlled entities		
Sale of goods	**20,450**	14,108
Purchase of materials	**19,038**	16,262
Commission and management fee received	**20,544**	26,703
Royalty fee received	**72**	–
Engineering fee received	**121**	–

Compensation of key management personnel

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

	2006	2005
	HK$'000	HK$'000
Short-term benefits	**37,707**	45,709
Post-employment benefits	**1,523**	2,623
	39,230	48,332

The remuneration of Directors and key executives is determined by the Remuneration Committee of the Company having regard to the performance of individuals and market trends.

38. SUMMARISED BALANCE SHEET OF THE COMPANY

	2006 HK$'000	2005 HK$'000
Assets		
Amounts due from subsidiaries	**1,056,043**	381,885
Bank balances	**101,134**	332
Investments in subsidiaries	**36,585**	36,585
Other receivables	**264**	224
Tax recoverable	**–**	47
Total assets	**1,194,026**	419,073
Liabilities		
Convertible loan notes	**767,047**	–
Embedded derivative component of convertible loan notes	**25,798**	–
Tax liabilities	**2,215**	–
Other payables	**597**	350
Total liabilities	**795,657**	350
Net assets	**398,369**	418,723
Capital and reserves		
Share capital	**55,842**	56,038
Reserves	**342,527**	362,685
Total capital and reserves	**398,369**	418,723

39. PARTICULARS OF PRINCIPAL SUBSIDIARIES

Name of company	Place of incorporation or registration/ operations	Nominal value of issued capital/ registered capital	Proportion of share capital/ registered capital attributable to the Company indirectly held	Principal activities
Falmer Investments Ltd.	British Virgin Islands/ The PRC	US$1	100%	Research and development
Fong's Engineering Services Company Limited	Hong Kong	HK$10,000	100%	Trading in stainless steel products and provision of management services to group companies
Fong's National Engineering Company, Limited	Hong Kong	Ordinary – HK$100	100%	Trading of dyeing and finishing machines
		Deferred – HK$8,000,000 (Note)	–	
Fong's National Engineering (Shenzhen) Company Limited	The PRC *	US$22,500,000	100%	Manufacture of dyeing and finishing machines
Fong's Steels Supplies Company Limited	Hong Kong	HK$10,000	100%	Trading in stainless steel supplies
Goller (HK) Limited	Hong Kong	HK$1	100%	Trading in textile machinery
Goller Textilmaschinen GmbH	Germany	EUR25,000	100%	Trading and manufacture of textile machinery
Sunshine Glory Limited	British Virgin Islands/ The PRC	US$10	100%	Investment holding
Tycon Alloy Industries (Hong Kong) Company Limited	Hong Kong	HK$10,000	100%	Trading in stainless steels casting products
Tycon Alloy Industries (Shenzhen) Co. Ltd.	The PRC *	US$4,350,000	100%	Manufacture of stainless steels casting products

39. PARTICULARS OF PRINCIPAL SUBSIDIARIES *(Continued)*

Name of company	Place of incorporation or registration/ operations	Nominal value of issued capital/ registered capital	Proportion of share capital/ registered capital attributable to the Company indirectly held	Principal activities
THEN Maschinen (HK) Limited	Hong Kong	HK$1	100%	Trading in textile machinery and technical parts
THEN Maschinen GmbH	Germany	EUR1,900,000	100%	Trading and manufacture of textile machinery and technical parts
Xorella Hong Kong Limited	Hong Kong	US$3,500,000	100%	Trading in textile machinery and technical parts
Xorella AG	Switzerland	CHF350,000	100%	Trading and manufacture of textile machinery and technical parts

* A wholly-owned foreign enterprise

The above table lists the subsidiaries of the Company which, in the opinion of the Directors, principally affect 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.

Note: The deferred shares entitle the holders to dividends from one half of the remaining net profit after the first HK$10,000,000,000 has been distributed to holders of ordinary shares of HK$1 each of the company. The deferred shares also entitle the holders to participate in distribution of one half of the surplus assets on winding up after the first HK$20,000,000,000 has been distributed to holders of ordinary shares of HK$1 each of the company.

FINANCIAL SUMMARY

RESULTS

	Year ended December 31,				
	2002	2003	2004	2005	**2006**
	HK$'000	HK$'000	HK$'000	HK$'000	**HK$'000**
Revenue	1,142,419	1,350,380	1,743,873	2,012,252	**2,380,036**
Profit before tax	203,747	314,685	267,721	240,706	**308,939**
Income tax expense	(32,187)	(39,718)	(32,473)	(22,510)	**(48,906)**
Profit for the year	171,560	274,967	235,248	218,196	**260,033**
Attributable to:					
Equity holders of the parent	172,525	276,910	235,112	218,653	**260,033**
Minority interests	(965)	(1,943)	136	(457)	**–**
	171,560	274,967	235,248	218,196	**260,033**

ASSETS AND LIABILITIES

	As at December 31,				
	2002	2003	2004	2005	**2006**
	HK$'000	HK$'000	HK$'000	HK$'000	**HK$'000**
Total assets	861,423	963,333	1,254,335	1,322,163	**2,355,536**
Total liabilities	(277,643)	(243,778)	(461,689)	(447,606)	**(1,339,160)**
	583,780	719,555	792,646	874,557	**1,016,376**
Equity attributable to equity holders of the parent	580,226	717,944	790,899	873,267	**1,015,086**
Minority interests	3,554	1,611	1,747	1,290	**1,290**
	583,780	719,555	792,646	874,557	**1,016,376**