GDH

粤海制革有限公司

GUANGDONG TANNERY LIMITED

(Incorporated in Hong Kong with limited liability)

(Stock Code: 1058)

2010 ANNUAL RESULTS ANNOUNCEMENT

The board of directors (the "Board") of Guangdong Tannery Limited (the "Company") announces the consolidated results of the Company and its subsidiaries (the "Group") for the year ended 31 December 2010 together with comparative figures.

CONSOLIDATED INCOME STATEMENT

	Notes	**2010** *HK$'000*	2009 *HK$'000*
REVENUE	*4*	**520,737**	467,259
Cost of sales		**(488,857)**	(417,795)
Gross profit		**31,880**	49,464
Other income and gains	*4*	**12,561**	10,256
Selling and distribution costs		**(2,192)**	(2,505)
Administrative expenses		**(23,188)**	(24,131)
Finance costs	*5*	**(4,781)**	(6,731)
PROFIT BEFORE TAX	*5*	**14,280**	26,353
Income tax expense	*6*	**(8,068)**	(11,653)
PROFIT FOR THE YEAR		**6,212**	14,700
EARNINGS PER SHARE	*7*		
- Basic		**HK1.16 cents**	HK2.73 cents
- Diluted		**HK1.15 cents**	HK2.73 cents

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	2010	2009
	HK$'000	*HK$'000*
PROFIT FOR THE YEAR	**6,212**	14,700
OTHER COMPREHENSIVE INCOME		
Surplus/(deficit) on revaluation of buildings	**123**	(4)
Deferred tax	**(31)**	1
	92	(3)
Exchange differences on translation of foreign operations	**15,026**	(1,051)
OTHER COMPREHENSIVE INCOME/(LOSS) FOR THE YEAR, NET OF TAX	**15,118**	(1,054)
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	**21,330**	13,646

CONSOLIDATED BALANCE SHEET

	Notes	2010 HK$'000	2009 HK$'000
NON-CURRENT ASSETS			
Property, plant and equipment		**103,519**	90,423
Investment property		**-**	1,990
Prepaid land lease payments		**8,133**	7,963
Total non-current assets		**111,652**	100,376
CURRENT ASSETS			
Inventories		**151,878**	106,373
Receivables, prepayments and deposits	*9*	**168,121**	165,435
Tax recoverable		**514**	-
Pledged deposits		**32,314**	1,353
Restricted bank balances		**8,226**	6,246
Cash and cash equivalents		**107,718**	157,014
Total current assets		**468,771**	436,421
CURRENT LIABILITIES			
Trade payables	*10*	**46,539**	54,596
Other payables and accruals		**43,777**	49,021
Interest-bearing bank and other borrowings		**39,011**	-
Due to a PRC joint venture partner		**1,131**	1,131
Loans from the immediate holding company		**87,779**	-
Provision		**3,748**	3,622
Convertible notes	*11*	**-**	63,327
Tax payable		**-**	6,235
Total current liabilities		**221,985**	177,932
NET CURRENT ASSETS		**246,786**	258,489
TOTAL ASSETS LESS CURRENT LIABILITIES		**358,438**	358,865
NON-CURRENT LIABILITIES			
Loans from the immediate holding company		**-**	22,779
Loan from a fellow subsidiary		**54,600**	54,600
Deferred tax liabilities		**717**	462
Total non-current liabilities		**55,317**	77,841
Net assets		**303,121**	281,024
EQUITY			
Issued capital		**53,762**	53,762
Reserves		**249,359**	227,262
Total equity		**303,121**	281,024

Notes:

(1) BASIS OF PREPARATION

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") (which include all Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants, accounting principles generally accepted in Hong Kong and the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for an investment property and buildings, which have been measured at fair value. These financial statements are presented in Hong Kong dollars ("HK$") and all values are rounded to the nearest thousand (HK$'000) except when otherwise indicated.

Basis of consolidation

The consolidated financial statements include the financial statements of the Group for the year ended 31 December 2010. The financial statements of the subsidiaries are prepared for the same reporting period as the Company, using consistent accounting policies. The results of subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. All intra-group balances, transactions, unrealised gains and losses resulting from intra-group transactions and dividends are eliminated on consolidation in full.

Adjustments are made to bring into line any dissimilar accounting policies that may exist.

Losses within a subsidiary are attributed to the non-controlling interest even if that results in a deficit balance.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction.

If the Group loses control over a subsidiary, it derecognises (i) the assets (including goodwill) and liabilities of the subsidiary, (ii) the carrying amount of any non-controlling interest and (iii) the cumulative translation differences recorded in equity; and recognises (i) the fair value of the consideration received, (ii) the fair value of any investment retained and (iii) any resulting surplus or deficit in profit or loss. The Group’s share of components previously recognised in other comprehensive income is reclassified to profit or loss or retained profits, as appropriate.

(2) IMPACT OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARD

The Group has adopted the following new and revised HKFRSs for the first time for the current year's financial statements.

HKFRS 1 (Revised)	*First-time Adoption of Hong Kong Financial Reporting Standards*
HKFRS 1 Amendments	Amendments to HKFRS 1 *First-time Adoption of Hong Kong Financial Reporting Standards – Additional Exemptions for First-time Adopters*
HKFRS 2 Amendments	Amendments to HKFRS 2 *Share-based Payment – Group Cash-settled Share-based Payment Transactions*
HKFRS 3 (Revised)	*Business Combinations*
HKAS 27 (Revised)	*Consolidated and Separate Financial Statements*
HKAS 39 Amendment	Amendment to HKAS 39 *Financial Instruments: Recognition and Measurement – Eligible Hedged Items*
HK(IFRIC)-Int 17	*Distributions of Non-cash Assets to Owners*

HKFRS 5 Amendments included in *Improvements to HKFRSs* issued in October 2008	Amendments to HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations – Plan to sell the controlling interest in a Subsidiary*
Improvements to HKFRSs 2009	Amendments to a number of HKFRSs issued in May 2009
HK Interpretation 4 Amendment	Amendment to HK Interpretation 4 *Leases – Determination of the Length of Lease Term in respect of Hong Kong Land Leases*
HK Interpretation 5	*Presentation of Financial Statements – Classification by the Borrower a Term Loan that Contains a Repayment of Demand Clause*

Other than as further explained below regarding the impact of HKFRS 3 (Revised), HKAS 27 (Revised), amendments to HKAS 7 and HKAS 17 included in *Improvements to HKFRSs 2009* and HK Interpretation 4 (Revised in December 2009), the adoption of the new and revised HKFRSs has had no significant financial effect on these financial statements.

The principal effects of adopting these new and revised HKFRSs are as follows:

(a) HKFRS 3 (Revised) *Business Combinations* and HKAS 27 (Revised) *Consolidated and Separate Financial Statements*

HKFRS 3 (Revised) introduces a number of changes in the accounting for business combinations that affect the initial measurement of non-controlling interests, the accounting for transaction costs, the initial recognition and subsequent measurement of a contingent consideration and business combinations achieved in stages. These changes will impact the amount of goodwill recognised, the reported results in the period that an acquisition occurs, and future reported results.

HKAS 27 (Revised) requires that a change in the ownership interest of a subsidiary without loss of control is accounted for as an equity transaction. Therefore, such a change will have no impact on goodwill, nor will it give rise to a gain or loss. Furthermore, the revised standard changes the accounting for losses incurred by the subsidiary as well as the loss of control of a subsidiary. Consequential amendments were made to various standards, including, but not limited to HKAS 7 *Statement of Cash Flows*, HKAS 12 *Income Taxes*, HKAS 21 *The Effects of Changes in Foreign Exchange Rates*, HKAS 28 *Investments in Associates* and HKAS 31 *Interests in Joint Ventures.*

The changes introduced by these revised standards are applied prospectively and affect the accounting of acquisitions, loss of control and transactions with non-controlling interests after 1 January 2010.

(b) *Improvements to HKFRSs 2009* issued in May 2009 sets out amendments to a number of HKFRSs. There are separate transitional provisions for each standard. While the adoption of some of the amendments results in changes in accounting policies, none of these amendments has had a significant financial impact on the Group. Details of the key amendments most applicable to the Group are as follows:

- HKAS 7 *Statement of Cash Flows*: Requires that only expenditures that result in a recognised asset in the balance sheet can be classified as a cash flow from investing activities.

- HKAS 17 *Leases*: Removes the specific guidance on classifying land as a lease. As a result, leases of land should be classified as either operating or finance leases in accordance with the general guidance in HKAS 17.

Amendment to HK Interpretation 4 *Leases – Determination of the Length of Lease Term in respect of Hong Kong Land Leases* is revised as a consequence of the amendment to HKAS 17 *Leases* included in *Improvements to HKFRSs 2009.* Following this amendment, the scope of HK Interpretation 4 has been expanded to cover all land leases, including those classified as finance leases. As a result, this interpretation is applicable to all leases of property accounted for in accordance with HKAS 16, HKAS 17 and HKAS 40.

The Group has reassessed its leases in the People's Republic of China (the "PRC" or "Mainland China"), previously classified as operating leases, upon the adoption of the amendments. The classification of leases in the Mainland China remained as operating leases.

The Group has not applied the following new and revised HKFRSs, that have been issued but are not yet effective, in these financial statements.

HKFRS 1 Amendment	Amendment to HKFRS 1 *First-time Adoption of Hong Kong Financial Reporting Standards – Limited Exemption from Comparative HKFRS 7 Disclosures for First-time Adopters* [2]
HKFRS 1 Amendments	Amendments to HKFRS 1 *First-time Adoption of Hong Kong Financial Reporting Standards – Severe Hyperinflation and Removal of Fixed Dates for First-Time Adopters* [4]
HKFRS 7 Amendments	Amendments to HKFRS 7 *Financial Instruments: Disclosures – Transfers of Financial Assets* [4]
HKFRS 9	*Financial Instruments* [6]
HKAS 12 Amendments	Amendments to HKAS 12 *Income Taxes – Deferred Tax: Recovery of Underlying Assets* [5]
HKAS 24 (Revised)	*Related Party Disclosures* [3]
HKAS 32 Amendment	Amendment to HKAS 32 *Financial Instruments: Presentation – Classification of Rights Issues* [1]
HK(IFRIC)-Int 14 Amendments	Amendment to HK(IFRIC) – Int 14 *Prepaymments of a Minimum Funding Requirement* [3]
HK(IFRIC)-Int 19	*Extinguishing Financial Liabilities with Equity Instruments* [2]

Apart from the above, the HKICPA has issued *Improvements to HKFRSs 2010* which sets out amendments to a number of HKFRSs primarily with a view to removing inconsistencies and clarifying wording. The amendments to HKFRS 3 and HKAS 27 are effective for annual periods beginning on or after 1 July 2010, whereas the amendments to HKFRS 1, HKFRS 7, HKAS 1, HKAS 34 and HK(IFRIC)-Int 13 are effective for annual periods beginning on or after 1 January 2011 although there are separate transitional provisions for each standard.

[1] Effective for annual periods beginning on or after 1 February 2010
[2] Effective for annual periods beginning on or after 1 July 2010
[3] Effective for annual periods beginning on or after 1 January 2011
[4] Effective for annual periods beginning on or after 1 July 2011
[5] Effective for annual periods beginning on or after 1 January 2012
[6] Effective for annual periods beginning on or after 1 January 2013

The Group is in the process of making an assessment of the impact of these new and revised HKFRSs upon initial application. So far, the Group considers that except for the adoption of HKAS 24 (Revised) and HKAS 27 (Revised), these new and revised HKFRSs are unlikely to have a significant impact on the Group's results of operations and financial position.

(3) OPERATING SEGMENT INFORMATION

No separate analysis of operating segment information is presented by the Group as over 90% of the Group's revenue, results and assets related to the processing and sale of semi-finished and finished leather in Mainland China during the year.

Information about a major customer

Revenue of approximately HK$103,200,000 (2009:HK$45,030,000) was derived from sales to a single customer, which constituted 20% (2009:10%) of total revenue, during the year ended December 2010.

(4) REVENUE, OTHER INCOME AND GAINS

Revenue, which is also the Group's turnover, represents the net invoiced value of goods sold, after allowances for returns and trade discounts and value-added tax, during the year.

An analysis of revenue, other income and gains is as follows:

	2010	2009
	HK$'000	*HK$'000*
Revenue		
Processing and sale of leather	**520,737**	467,259
Other income		
Gross rental income	**97**	367
Interest income	**937**	1,103
Sale of scrap materials	**2,084**	1,651
Others	**6,514**	6,893
	9,632	10,014
Gains		
Surplus on revaluation of buildings	**895**	-
Foreign exchange gain, net	**99**	242
Gain on disposal of an investment property	**1,570**	-
Gain on disposal of items of property, plant and equipment	**365**	-
	2,929	242
	12,561	10,256

(5) PROFIT BEFORE TAX

The Group's profit before tax is arrived at after charging/(crediting):

	2010	2009
	HK$'000	*HK$'000*
Cost of inventories sold	**488,512**	413,752
Auditors' remuneration	**1,128**	1,085
Depreciation	**8,277**	7,564
Interest on:		
Bank loans and discounting bills receivable to banks	**225**	253
Convertible notes	**2,620**	4,016
Loans from the immediate holding company	**917**	1,145
Loan from a fellow subsidiary	**1,019**	1,317
	4,781	6,731

	2010	2009
Employee benefit expense (excluding directors' remuneration):		
Wages and salaries	**26,743**	22,424
Pension scheme contribution (defined contribution schemes)*	**2,694**	2,074
Equity-settled share option expense	**239**	48
	29,676	24,546
Provision for inventories	**345**	4,043
Minimum lease payments under operating leases in respect of land and buildings	**675**	683
Amortisation of prepaid land lease payments	**172**	138
Rental income on investment property less direct operating expenses of HK$26,000 (2009: HK$103,000)	**(71)**	(264)
Fair value loss on an investment property	**-**	130
Deficit/(surplus) on revaluation of buildings	**(895)**	2,067
Write-off of items of property, plant and equipment	**-**	78
Loss/(gain) on disposal of items of property, plant and equipment	**(365)**	469
Impairment of trade and other receivables, net	**258**	990

* At the balance sheet date, the Group had no forfeited contribution available to reduce its contributions to the pension schemes in future years.

(6) INCOME TAX

No provision for Hong Kong profits tax has been made as the Group did not generate any assessable profits arising in Hong Kong during the year (2009: Nil). Taxes on profits assessable in Mainland China have been calculated at the rate of tax prevailing in Mainland China in which the Group operates.

	2010 *HK$'000*	2009 *HK$'000*
Group:		
Current - Mainland China	**7,844**	12,170
Deferred	**224**	(517)
Total tax charge for the year	**8,068**	11,653

(7) EARNINGS PER SHARE

The calculation of basic earnings per share amount is based on the profit for the year and the weighted average number of ordinary shares of 537,619,000 (2009: 537,539,918) in issue during the year.

The calculation of diluted earnings per share amount is based on the profit for the year, adjusted to reflect the interest on the convertible notes, where applicable (see below). The weighted average number of ordinary shares used in the calculation is the number of ordinary shares in issue during the year, as used in the basic earnings per share calculation and the weighted average number of ordinary shares assumed to have been issued at no consideration on the deemed exercise or conversion of all dilutive potential ordinary shares into ordinary shares.

No adjustment has been made to the basic earnings per share amounts presented for the years ended 31 December 2010 and 2009 in respect of a dilution as the impact of the convertible notes outstanding had an anti-dilutive effect on the basic earnings per share amounts presented.

The calculations of basic and diluted earnings per share are based on:

	2010	2009
	HK$'000	*HK$'000*
Earnings		
Profit for the year, used in the basic earnings per share calculation	**6,212**	14,700
Interest on convertible notes	**2,620***	4,016*
Profit for the year, before interest on convertible notes	**8,832**	18,716

	Number of shares	
	2010	2009
Shares		
Weighted average number of ordinary shares in issue during the year used in the basic earnings per share calculation	**537,619,000**	537,539,918
Effect of dilution - weighted average number of ordinary shares:		
Share options	**3,020,316**	313,881
Convertible notes	**19,864,456***	32,368,421*
	560,503,772	570,222,220

* Because the diluted earnings per share amount is increased when taking convertible notes into account, the convertible notes had an anti-dilutive effect on the basic earnings per share for the year and were ignored in the calculation of diluted earnings per share. Therefore, diluted earnings per share amount is based on the profit for the year of HK$6,212,000 and the weighted average number of ordinary shares of 540,639,316 in issue during the year.

(8) DIVIDEND

The Board does not recommend the payment of a final dividend (2009: Nil).

(9) RECEIVABLES, PREPAYMENTS AND DEPOSITS

As at 31 December 2010, included in the Group's receivables, prepayments and deposits were trade and bills receivables with a net balance of HK$161,109,000 (2009: HK$162,157,000) due from the Group's customers.

The Group's trading terms with customers are mainly on credit, except for new customers, where payment in advance is normally required. Invoices are normally payable within 30 days of issuance, except for certain well-established customers, where the terms are extended to two to three months. Each customer has a maximum credit limit. The Group seeks to maintain tight control over its outstanding receivables in order to minimise credit risk. Overdue balances are reviewed regularly by senior management. In view of the aforementioned and the fact that the Group's trade receivables relate to a large number of diversified customers, there is no significant concentration of credit risk. Trade receivables are non-interest-bearing.

An aged analysis of the trade and bills receivables as at the balance sheet date, based on the settlement due date, is as follows:

	2010	2009
	HK$'000	*HK$'000*
Current	**160,771**	158,157
Less than 3 months	**902**	4,037
3 to 6 months	**115**	309
Over 6 months	**375**	417
	162,163	162,920
Impairment	**(1,054)**	(763)
	161,109	162,157

Movements in the provision for impairment of trade receivables are as follows:

	2010	2009
	HK$'000	*HK$'000*
At 1 January	**763**	460
Impairment losses recognised	**567**	484
Impairment losses reversed	**(309)**	(181)
Exchange realignment	**33**	-
At 31 December	**1,054**	763

The above provision for impairment of trade receivables is a provision for individually fully impaired trade receivables. The individually impaired trade receivables relate to customers that were in default or delinquency payments. The Group does not hold any collateral or other credit enhancements over these balances.

The aged analysis of the trade and bills receivables, that are not considered to be impaired is as follows:

	2010	2009
	HK$'000	*HK$'000*
Neither past due nor impaired	**160,771**	158,156
Less than 1 month past due	**236**	3,522
1 to 3 months past due	**102**	417
Over 3 months past due	**-**	62
	161,109	162,157

Receivables that were neither past due nor impaired relate to a large number of diversified customers for whom there was no recent history of default.

Receivables that were past due but not impaired relate to a number of independent customers that have a good track record with the Group. Based on past experience, the directors of the Company are of the opinion that no provision for impairment is necessary in respect of these balances as there has not been a significant change in the credit quality and the balances are still considered fully recoverable. The Group does not hold any collateral or other credit enhancements over these balances.

(10) TRADE PAYABLES

An aged analysis of the trade payables as at the balance sheet date, based on the payment due date, is as follows:

	2010	2009
	HK$'000	*HK$'000*
Within 3 months	**23,481**	24,836
3 to 6 months	**18,691**	22,487
Over 6 months	**4,367**	7,273
	46,539	54,596

The trade payables of the Group are non-interest-bearing and are normally settled on terms of 60 to 90 day. Other payables of the Group and the Company are non-interest-bearing and have an average term of three months.

(11) CONVERTIBLE NOTES

On 13 August 2007, the Company issued 61,500,000 1% convertible notes with a nominal value of HK$61,500,000 to GDH Limited ("GDH"), with a maturity date on the third anniversary of the date of issue of the convertible notes (the "Maturity Date"). GDH has the right to convert the whole or part of the principal amount of the convertible notes into shares at any time and from time to time, from the 7th day after the date of the issue of the convertible notes up to the day which is 7 days prior to the Maturity Date, on the basis of one ordinary share for every 1.9 HK$1 notes held. There was no movement in the number of these convertible notes during the year. Any convertible notes not converted will be redeemed on the Maturity Date at a price of HK$1.0623 per HK$1 note. The notes carried interest at a rate of 1% per annum, payable semi-annually in arrears on 13 February and 13 August.

The convertible notes have been split as to the liability and equity components as follows:

	2010	2009
	HK$'000	HK$'000
Nominal value of convertible notes	**61,500**	61,500
Equity component	**(5,599)**	(5,599)
Direct transaction costs attributable to the liability component	**(537)**	(537)
Liability component at the issuance date	**55,364**	55,364
Interest expense	**11,813**	9,193
Interest paid	**(1,845)**	(1,230)
Redeemed during the year	**(65,332)**	-
Liability component at 31 December	**-**	63,327

No convertible notes were converted, and the Company redeemed in full, the convertible notes on the Maturity Date, i.e. 12 August 2010 at a price of HK$1.0623 per HK$1 note.

CHAIRMAN'S STATEMENT

Results

I would like to present to the shareholders that the consolidated profit attributable to shareholders of the Group for 2010 was HK$6,212,000 (2009: HK$14,700,000), a decrease of 57.7% over last year. Basic earnings per share was HK1.16 cents (2009: HK2.73 cents), a decrease of 57.5% compared with last year.

Dividend

The Board does not recommend the payment of a final dividend for the year ended 31 December 2010 (2009: nil).

Review

In the first half of 2010, with the sound operation of its macroeconomic environment, China had successfully shaken off the adverse impacts of the international financial and economic crisis and resumed its normal growth track. Likewise, full recovery was seen in the first half of 2010 as the China tannery industry also extended its good run since the second half of 2009. However, as a traditional production industry, it was driven into an unprecedented tight corner in the second half of 2010 by changes in the international and domestic economic situation as well as the deepening effects of the domestic macroeconomic policies. In the first place, continual increases in costs of raw materials and labour began to pounder the stable operations of the enterprises with additional pressures; secondly, domestic sales demands within the industry shrank significantly due to the mismatching between product sales and extreme weather conditions. Concurrently, overseas sales of footwear products did not see obvious changes due to continuous extension of trade barriers by the European Union. As a result of the ferocious competition in export markets, sales prices of leather goods remained in tatters and prevailed with difficulties for the sustainable development of the enterprises. Amidst significant inflated raw material prices, increasing labour costs and ongoing environmental protection pressures, the Group managed to develop its tasks closely interwoven with the guiding directions of "ensuring operating efficiency, completing plant removals, optimising team building, and deepening the basic management". These have sustained production capacity, stabilised profitability, reduced obsolete stocks and enhanced inventory structure.

In terms of strategic development, as a result of the land planning and development proposals issued by the People's Government of Xuzhou City in respect of environmental protection policies, the existing downstream finished leather product manufacturing operations of Xuzhou Nanhai Leather Factory Co. Ltd. were also relocated to and integrated into the new factory. The new factory has recently been completed. With the present upstream and downstream processing production scale of approximately 4 million sq.ft. for monthly production capacity, the Group has not only resolved the lack of synergy between the upstream and downstream processing issues but also improved the environmental protection problems.

During the year, the Group paid particular attention to the international and domestic economic situations and closely monitored the imported cowhides market so as to capitalise on its price trends by purchasing in time of needs and regularly in order to form a steady purchase format and avoid the significant fluctuation risks in cowhides. The Group also undertook the procurement strategy of direct purchases from large slaughter-houses to minimise the prices charged by intermediaries on cowhides and safeguard our supplies. Operating in an adverse industry environment with vibrant international and domestic economic conditions, the Group has analysed its actual situation genuinely by leveraging on the economic setup of the international and domestic industry on the basis of sales market and realigning the production and sales strategies timely through the establishment of mutually trustworthy strategic supply-and-sales relationship with large footwear manufacturers. Such strategies have not only laid down long-term and continuous cooperation foundation but also ensured that product prices are better with stable production volumes. Through our research and development, a series of new products have been launched in succession, with acclaims from customers and markets, which further strengthened our competitive advantages in the marketplace.

Prospects

The operating environment of the tannery industry in 2011 will not be optimistic as the space for development via the extension of production volume and expansion of size of the manufacturing industry is coming to its end. With the backdrop of shuffling the downstream footwear industry, and centralisation of market share in the hands of sizeable enterprises with brand-name, network, research and development and funding, it can be foreseen that the pre-requisite and foundation for survival and development in the tannery industry are rested in those with large operating scales, complete environmental protection formalities and healthy supply and distribution channels. With the opportunity made available by the Integration and Reorganisation Project of the upstream and downstream processing at the existing Xuzhou production plant, together with the "overall smoothing of all production and operation relationship and practical expansion of development foundation" as the objectives, the Group will accelerate its industry upgrade, reduce its energy consumption, enhance efficiency and mould its environmental-friendly plant. In respect of internal control management, the Group will continue to push the optimisation of its production technology; actively promote the integration between production process and workers' team, enhance the supply and distribution channels, strengthen the controls over raw material resources and optimise customer structure of sales and seek to achieve the enhancement of the overall industry status and operating results of the Group in 2012.

MANAGEMENT DISCUSSION AND ANALYSIS

Results

The Group's consolidated profit attributable to shareholders for the year ended 31 December 2010 was HK$6,212,000, representing a decrease of HK$8,488,000 or 57.7% as compared to the profit of HK$14,700,000 for last year.

The net asset value of the Group as at 31 December 2010 was HK$303,121,000, representing an increase of HK$22,097,000 and HK$455,000, as compared to the net asset values as at 31 December 2009 and 30 June 2010 respectively.

The Board does not recommend the payment of a final dividend for the year ended 31 December 2010.

Business Review

In 2010, the operation of enterprises faced new challenges under the hybrid economic model of inflation and deflation in China's macroeconomic environment and in the tannery industry. In consolidating the foundation of its existing scale of operation, the Group re-defined its directions of development, rebuilt its internal structure and optimised staff teams. To leverage on the economic setup of the international and domestic industry, the Group adjusted production and sales strategies timely to maintain basic production volume in terms of production requirements and orders and by establishing strategic cooperation relationship to ensure better product prices with stable production volumes. The Group also stabilised its production and operation aspects solidly by taking a positive role in production and operation by relocating the plants during the year so as to ensure profitability as its main purpose.

During the year, the total production volume of cowhides was 27,840,000 sq. ft., a decrease of 1,379,000 sq. ft. or 4.7% over 29,219,000 sq. ft. for the same period of last year. The production volume of greyhides was 12,704 tons, an increase of 2,037 tons or 19.1% over 10,667 tons for the same period of last year.

During the year, the consolidated turnover of the Group was HK$520,737,000, an increase of HK$53,478,000 or 11.4% over HK$467,259,000 for the same period of last year, of which cowhides amounted to HK$463,968,000 (2009: HK$439,170,000), an increase of 5.6% and greyhides and other products amounted to HK$56,769,000 (2009: HK$28,089,000), an increase of 102.1%. The increase in turnover was primarily due to the increase in selling price of both imported cowhides and greyhides but a decrease in sales volume. The prices for cowhides continued to increase, but the selling price in general failed to catch up. Faced with such unfavourable market environment, the Group proactively expanded the strategic supply-and-sales relationship with large footwear manufacturers, and entered into long-term sales orders with them. This not only achieved in lifting product prices earlier than planned, it also increased our share in the end user sales market with sound sales network established for the Group. More importantly, stability in production was secured, and the goal of lifting selling price in a ladder-shaped pattern was ultimately achieved.

Faced with the situation of tight raw material supply within the tannery industry and rising prices of cowhides beyond our control, the Group closely observed the changes in international and domestic economies. Close attention was paid to monitor the price movement trends of imported cowhides market. Purchases were made strictly in accordance with production capacity regularly in order to form a steady purchase format and avoid the significant fluctuation risks in cowhides. During the year, total purchases increased by 76.1% over last year to HK$478,789,000, which were flat in volume against last year, save for the surge in cowhides purchase prices.

Despite the decrease in the volume of inventory over last year, the Group’s consolidated inventory amount rose by HK$45,505,000 to HK$151,878,000 (31 December 2009: HK$106,373,000), an increase of 42.8%, which was subject to increases in cowhides purchase prices. During the year, the Group continued to aim at minimising the inventory level through active depletion of obsolete inventory. Solutions for disposals of obsolete products were rectified specifically. Obsolete inventory was successfully utilised through the application of a number of technical measures to open up diversified sales channel. The weighing of finished products to total inventory also fell from 26.7% at the end of 2009 to 20.2% as at 31 December 2010. At the same time, the inventory composition was further optimised.

In terms of strategic development, the Group realigned its development strategy timely according to the land planning and development proposals requested by the People’s Government of Xuzhou City in respect of its environmental protection policies by closing the old production plant of Xuzhou Nanhai Tannery in the third quarter of 2010. During the year, the existing downstream finished leather products manufacturing operations of Xuzhou Nanhai Leather Factory Co. Ltd. were also relocated to and integrated into the new factory. The new factory has recently been completed. After integration, the new factory has a total production capacity (downstream finished leather products) of 2,000,000 sq. ft. per month. With the present upstream and downstream processing production scale of approximately 4 million sq. ft. available for monthly production capacity, the Group has not only resolved the lack of synergy between upstream and downstream processing but also improved the environmental protection problems.

On 4 January 2011, the Company announced that it intended to put forward a proposal, for approval by shareholders, to reduce the share premium account of the Company by HK$393,345,845 to eliminate the accumulated losses by the same amount (the “Proposed Share Premium Reduction”), the purpose of which is to bring the Company to a position that might permit the payment of dividends if and when the Company's financial position allows and the Board considers appropriate in the future. The Proposed Share Premium Proposal has been passed by shareholders at the extraordinary general meeting held on 1 February 2011, and conditional upon the sanction by the High Court of Hong Kong.

Financial Review

Liquidity and Financial Resources

As at 31 December 2010, the Group's cash and cash equivalents amounted to HK$107,718,000 (as at 31 December 2009: HK$157,014,000), representing a decrease of HK$49,296,000 or 31.4% as compared to the same as at 31 December 2009, which were denominated in Hong Kong dollars (1.6%), Renminbi (97.4%) and United States dollars (1.0%) respectively. During the year, net cash outflow from operating activities was HK$7,934,000, which was mainly attributed to the increase in cash payment for the purchase of raw materials as a result of the increase in raw materials prices. The cash outflow from investing activities was HK$45,142,000, which mainly represented the increase in pledged bank deposits.

As at 31 December 2010, the Group's interest-bearing borrowings amounted to HK$181,390,000 (31 December 2009: HK$140,706,000), of which, interest-bearing borrowings in Hong Kong dollars amounted to HK$65,000,000 and interest-bearing borrowings in US dollars amounted to HK$116,390,000. The Group's borrowings mainly consist of: (1) balances of short-term loans provided by the bank of HK$39,011,000, which were secured by bank deposits of RMB27,496,000; and (2) balances of short-term unsecured inter-group borrowing of HK$87,779,000 and balances of long-term unsecured inter-group borrowings of HK$54,600,000. The above interest-bearing borrowings were charged at floating interest rate.

As at 31 December 2010, the Group's gearing ratio of the interest-bearing borrowings to adjusted capital (including shareholders' equity) plus interest-bearing borrowings was 37.4% (31 December 2009: 18.4%). During the year, the annual interest rate of the borrowings was approximately 1.3% to 3.8%. Of the Group's total borrowings, all are repayable within one year, save for the loan from a fellow subsidiary amounting to HK$54,600,000. The Group's interest expenses for the year amounted to HK$4,781,000, representing a decrease of 29.0% over last year.

As at 31 December 2010, the total banking facilities of the Group was HK$135,148,000 (31 December 2009: HK$158,998,000), of which banking facilities of HK$39,011,000 (31 December 2009: HK$ nil) were utilised and HK$96,137,000 were unutilised (2009: HK$158,998,000). Taking into account of the existing cash resources and available credit facilities as well as the cash flow generated by the Group's operations, the Group had adequate financial resources to meet its day-to-day operational requirements.

Capital Expenditure

As at 31 December 2010, the net value of non-current assets, including prepaid land lease payments, property, machinery and equipment, amounted to HK$111,652,000, representing an increase of HK$11,276,000 over the net value as at 31 December 2009 of HK$100,376,000. The capital expenditure for the year amounted to HK$17,732,000 (2009: HK$36,095,000), which were primarily the payments for the construction works as well as the acquisition of machinery and equipment for new projects to cope with the production and development requirements of the Group.

Pledge of Assets

As at 31 December 2010, certain of the Group's bank balances with a total of HK$32,314,000 (31 December 2009: bank balances, plant and machinery with a total net book value of HK$16,208,000) were pledged to secure general banking facilities granted to the Group.

Risk of Exchange Rate

The assets, liabilities and transactions of the Group are basically denominated in Hong Kong dollars, United States dollars or Renminbi. During the year, the exchange rates of Hong Kong dollars and United States dollars were relatively stable and did not constitute any material foreign exchange risk; as to the appreciation of Renminbi, as the Group's sales are settled in Renminbi, and purchases are made in Renminbi and United States dollars, the Group does not have any material foreign exchange risk.

Remuneration Policy for Employees

As at 31 December 2010, a total of 849 employees (31 December 2009: 932) were employed by the Group. Our remuneration policy is based on the Group's operating results and the employees' performance. The Group has adopted a performance-based appraisal scheme for its employees focusing on "accountability and performance". The incentive bonuses to the management, key officers and staff with outstanding performance under the incentive scheme are determined by reference to the Group's operating net cashflow and profit after tax, calculated by various profit rankings and by applying a measure that links bonuses with the operating results of the Group and further taking into account of the individual performance of the staff concerned with an aim to motivate the contribution of its employees. In addition, the Group offered social and medical insurance and provident fund to all employees in different areas. The Company has adopted a new share option scheme in November 2008, with the purpose to provide incentives to the senior management to contribute to the Group, and to enable the Group to recruit and retain quality employees to serve the Group on a long-term basis.

CODE ON CORPORATE GOVERNANCE PRACTICES

The Group recognizes the importance of achieving and monitoring the highest standard of corporate governance consistent with the needs and requirements of its businesses and the best interest of all of its stakeholders and is fully committed to doing so. It is also with these objectives in mind that the Group has applied the principles of the Code on Corporate Governance Practices (the "CG Code") contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

In the opinion of the directors of the Company, the Company has met with the code provisions set out in the CG Code throughout the year ended 31 December 2010 except for the following:

Under the CG Code, there should be a clear division of responsibilities for the roles of chairman and chief executive officer and these two roles should be performed by two persons (the Company regards that the term "chief executive officer" has the same meaning as the Managing Director of the Company). On 20 September 2009, Mr. Ren Yingguo resigned as an Executive Director and the Managing Director of the Company. The Chairman of the Company took up the duties of the Managing Director temporarily while the Company was in the process of identifying the new Managing Director. Such temporary arrangement ended once Mr. Sun Jun was appointed as the new Managing Director on 5 February 2010.

AUDIT COMMITTEE

The audit committee of the Company has reviewed the annual results of the Group for the year ended 31 December 2010, including the accounting principles and practices adopted by the Group.

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

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

By order of the Board
Chen Hong
Chairman

Hong Kong, 11 March 2011

As at the date of this announcement, the Board comprises two Executive Directors, namely Mr. Chen Hong and Mr. Sun Jun; three Non-Executive Directors, namely Mr. Xiong Guangyang, Mrs. Ho Lam Lai Ping, Theresa and Mr. Qiao Jiankang; and three Independent Non-Executive Directors, namely Mr. Fung Lak, Mr. Choi Kam Fai, Thomas and Mr. Chan Cheong Tat.