粵海制革有限公司
GUANGDONG TANNERY LIMITED

(Incorporated in Hong Kong with limited liability)

(Stock Code: 1058)

INTERIM RESULTS ANNOUNCEMENT FOR THE SIX MONTHS ENDED 30 JUNE 2017

Unaudited financial highlights for the six months ended 30 June

	2017	2016	Changes
	HK$'000	HK$'000	%
Revenue	**155,140**	212,671	-27.1
Loss attributable to shareholders of the Company	**(32,464)**	(21,836)	-48.7
Loss per share — Basic	**HK(6.03)cents**	HK(4.06)cents	-48.5

CONDENSED CONSOLIDATED FINANCIAL INFORMATION
FOR THE SIX MONTHS ENDED 30 JUNE 2017

The board of directors (the "Board") of Guangdong Tannery Limited (the "Company") announces the unaudited consolidated results of the Company and its subsidiaries (collectively referred to as the "Group") for the six months ended 30 June 2017 together with comparative figures. The interim financial information has not been audited, but has been reviewed by the Company's audit committee (the "Audit Committee") and auditors, Messrs. Ernst & Young.

CONDENSED CONSOLIDATED STATEMENT OF PROFIT OR LOSS
FOR THE SIX MONTHS ENDED 30 JUNE 2017

	Notes	**2017** ***HK$'000*** **(Unaudited)**	2016 *HK$'000* (Unaudited)
REVENUE			
Processing and sale of leather	*3*	**155,140**	212,671
Cost of sales		**(167,716)**	(211,876)
Gross profit / (loss)		**(12,576)**	795
Other income and gains	*3*	**714**	832
Selling and distribution expenses		**(951)**	(1,202)
Administrative expenses		**(12,742)**	(16,692)
Impairment on items of property, plant and equipment		**(3,300)**	(2,817)
Finance costs	*4*	**(3,578)**	(2,752)
LOSS BEFORE TAX	*4*	**(32,433)**	(21,836)
Income tax expense	*5*	**(31)**	-
LOSS FOR THE PERIOD		**(32,464)**	(21,836)
LOSS PER SHARE	*6*		
- Basic		**HK(6.03) cents**	HK(4.06) cents
- Diluted		**HK(6.03) cents**	HK(4.06) cents

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
FOR THE SIX MONTHS ENDED 30 JUNE 2017

	2017	2016
	HK$'000	*HK$'000*
	(Unaudited)	(Unaudited)
LOSS FOR THE PERIOD	**(32,464)**	(21,836)
OTHER COMPREHENSIVE INCOME/(LOSS)		
Other comprehensive income not to be reclassified to the statement of profit or loss in subsequent periods:		
Surplus on revaluation of buildings	**1,012**	504
Income tax effect	**(253)**	(126)
	759	378
Other comprehensive income/(loss) to be reclassified to the statement of profit or loss in subsequent periods:		
Exchange differences on translation of foreign operations	**10,846**	(8,248)
OTHER COMPREHENSIVE INCOME/(LOSS) FOR THE PERIOD, NET OF TAX	**11,605**	(7,870)
TOTAL COMPREHENSIVE LOSS FOR THE PERIOD	**(20,859)**	(29,706)

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION
30 JUNE 2017

	Notes	**30 June 2017** *HK$'000* **(Unaudited)**	31 December 2016 *HK$'000* (Audited)
NON-CURRENT ASSETS			
Property, plant and equipment		**82,467**	87,308
Prepaid land lease payments		**12,005**	11,789
Total non-current assets		**94,472**	99,097
CURRENT ASSETS			
Inventories		**317,720**	258,591
Receivables, prepayments and deposits	*8*	**101,178**	138,030
Tax recoverable		**-**	4
Pledged bank balances		**16,042**	11,610
Cash and bank balances		**25,426**	48,291
Total current assets		**460,366**	456,526
CURRENT LIABILITIES			
Trade payables	*9*	**60,207**	61,275
Other payables and accruals		**41,612**	36,149
Interest-bearing bank borrowings		**100,669**	85,966
Due to a PRC joint venture partner		**1,131**	1,131
Provision		**3,674**	3,565
Tax payable		**26**	-
Total current liabilities		**207,319**	188,086
NET CURRENT ASSETS		**253,047**	268,440
TOTAL ASSETS LESS CURRENT LIABILITIES		**347,519**	367,537
NON-CURRENT LIABILITIES			
Loans from the immediate holding company		**140,532**	139,925
Deferred tax liabilities		**2,454**	2,220
Total non-current liabilities		**142,986**	142,145
Net assets		**204,533**	225,392
EQUITY			
Share capital		**75,032**	75,032
Other reserves		**129,501**	150,360
Total equity		**204,533**	225,392

Notes:

(1) ACCOUNTING POLICIES

The unaudited interim condensed consolidated financial information is prepared in accordance with Hong Kong Accounting Standard ("HKAS") 34 "Interim Financial Reporting" issued by the Hong Kong Institute of Certified Public Accountants. The unaudited interim financial information does not include all the information and disclosures required in the annual financial statements, and should be read in conjunction with the Group's annual financial statements as at 31 December 2016.

The accounting policies and basis of preparation adopted in the preparation of this unaudited interim condensed consolidated financial information are the same as those used in the annual financial statements for the year ended 31 December 2016, except for the adoption of the new and revised Hong Kong Financial Reporting Standards ("HKFRSs") (which also include Hong Kong Accounting Standards ("HKSA") and Interpretation) effective as at 1 January 2017. The Group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

The financial information relating to the year ended 31 December 2016 included in this unaudited interim financial information for the six months ended 30 June 2017 as comparative information does not constitute the statutory annual consolidated financial statements of the Company for that year but is derived from those consolidated financial statements. Further information relating to these statutory financial statements required to be disclosed in accordance with section 436 of the Hong Kong Companies Ordinance (Chapter 622) is as follows:

The Company has delivered the consolidated financial statements for the year ended 31 December 2016 to the Registrar of Companies as required by section 662(3) of, and Part 3 of Schedule 6 to, the Hong Kong Companies Ordinance (Chapter 622).

The Company's auditors have reported on those consolidated financial statements. The auditors' report was unqualified; did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report; and did not contain a statement under sections 406(2), 407(2) or (3) of the Hong Kong Companies Ordinance (Chapter 622).

The Group has adopted the following new and revised HKFRSs for the first time for the current period's unaudited interim condensed consolidated financial information.

Amendments to HKAS 7	*Disclosure Initiative*
Amendments to HKAS 12	*Recognition of Deferred Tax Assets for Unrealised Losses*
Amendments to HKFRS 12 included in *Annual Improvements 2014-2016 Cycle*	*Disclosure of Interests in Other Entities*

The adoption of these new and revised HKFRSs has had no material financial effect on the unaudited interim condensed consolidated financial information.

(2) OPERATING SEGMENT INFORMATION

No separate analysis of segment information is presented by the Group as over 90% of the Group's revenue, results and assets relate to the processing and sale of semi-finished and finished leather in the People's Republic of China (the "PRC" or "Mainland China").

Information about a major customer

During the period, revenue of approximately HK$24,377,000 (six months ended 30 June 2016: HK$35,223,000) was derived from sales to a single customer, which contributed approximately 16% (six months ended 30 June 2016: 17%) of the total revenue.

(3) 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.

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

	For the six months ended	
	30 June 2017	30 June 2016
	HK$'000	*HK$'000*
	(Unaudited)	(Unaudited)
Revenue		
Processing and sale of leather	**155,140**	212,671
Other income and gains		
Interest income	**40**	26
Sale of scrap materials	**595**	694
Others	**79**	112
	714	832

(4) LOSS BEFORE TAX

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

	For the six months ended	
	30 June 2017	30 June 2016
	HK$'000	*HK$'000*
	(Unaudited)	(Unaudited)
Cost of inventories sold*	**163,276**	212,773
Depreciation	**5,547**	5,667
Provision for impairment of trade receivables	**501**	-
Foreign exchange differences, net	**(1,584)**	2,643
Loss on disposal of property, plant and equipment	**368**	44
Interest on:		
Bank loans	**1,646**	1,044
Loans from the immediate holding company	**1,932**	1,708
	3,578	2,752
Provision/(reversal of provision) for inventories*	**4,440**	(897)

*Included in "Cost of sales" on the face of the condensed consolidated statement of profit or loss.

(5) INCOME TAX

No provision for Hong Kong and PRC profits tax have been made as the Group did not generate any assessable profits arising in Hong Kong during the period (six months ended 30 June 2016: 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.

	For the six months ended	
	30 June	30 June
	2017	2016
	HK$'000	*HK$'000*
	(Unaudited)	(Unaudited)
Group - Mainland China		
Provision for the period	**47**	-
Overprovision in prior years	**(16)**	-
Total tax expense for the period	**31**	-

(6) LOSS PER SHARE

The calculation of basic loss per share amounts is based on the loss for the period of HK$32,464,000 (six months ended 30 June 2016: HK$21,836,000) and the weighted average number of ordinary shares of 538,019,000 (30 June 2016: 538,019,000) in issue during the period.

No adjustment has been made to the basic loss per share amounts presented for the periods ended 30 June 2017 and 30 June 2016 in the calculation of diluted loss per share as there are no dilutive events during the periods ended 30 June 2017 and 30 June 2016.

(7) DIVIDEND

The Board has resolved not to declare the payment of an interim dividend for the six months ended 30 June 2017 (six months ended 30 June 2016: Nil).

(8) RECEIVABLES, PREPAYMENTS AND DEPOSITS

As at 30 June 2017, included in the Group's receivables, prepayments and deposits were trade and bills receivables with a net balance of HK$90,286,000 (31 December 2016: HK$130,143,000) 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 60 days of issuance, except for certain well-established customers, where the terms are extended to 150 days. 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. The Group does not hold any collateral or other credit enhancements over its trade receivable balances. Trade receivables are non-interest-bearing. The carrying amounts of trade receivables approximate their fair values.

An aging analysis of the Group's trade and bills receivables as at the end of reporting period, based on the settlement due date, is as follows:

	30 June 2017	31 December 2016
	HK$'000	*HK$'000*
	(Unaudited)	(Audited)
Current	**88,209**	129,976
Less than 3 months	**1,658**	167
More than 3 months	**930**	-
	90,797	130,143
Impairment	**(511)**	-
	90,286	130,143

(9) TRADE PAYABLES

An aging analysis of the Group's trade payables as at the end of reporting period, based on the date of receipt of goods, is as follows:

	30 June 2017	31 December 2016
	HK$'000	*HK$'000*
	(Unaudited)	(Audited)
Within 3 months	**32,011**	43,179
3 to 6 months	**25,201**	15,243
Over 6 months	**2,995**	2,853
	60,207	61,275

The trade payables of the Group are non-interest-bearing and are normally settled on terms of 90 days.

BUSINESS AND FINANCIAL REVIEW

Results

The unaudited consolidated loss attributable to shareholders for the six months ended 30 June 2017 of the Group was HK$32,464,000, representing an increase of loss of HK$10,628,000, or 48.7% as compared to the loss of HK$21,836,000 for the same period of last year.

The unaudited net asset value of the Group as at 30 June 2017 was HK$204,533,000, representing a decrease of HK$56,376,000 and HK$20,859,000 as compared to the net asset value as at 30 June 2016 and 31 December 2016, respectively.

The Board resolved not to declare the payment of an interim dividend for the six months ended 30 June 2017 (six months ended 30 June 2016: Nil).

Business Review

In the first half of the year, the overall shrinking of the tannery industry, overcapacity, sharp drop in downstream demand, downward trend of shoe production, coupled with impact of new materials, ultra-fiber and cloth, resulted in a significant decrease in use of footwear leather during the period. In recent years, the central and local governments have continuously enforced stricter environmental protection policies, laws and regulations of the tannery industry, and greatly enhanced the bottom line of environmental protection and operation in compliance with the laws, which gave rise to a substantial increase in the cost of environmental protection, and posed heavy pressure on the production and operation of leather processing enterprises. During the period, the Group adhered to the sound business strategy, and set up the "stable operation to ensure asset safety" as the main operation strategy for the first half of the year. Under the circumstances of rising production costs, falling selling prices and declining gross profit margins, the Group's operating losses were further expanded. During the period, in order to improve the efficiency of management and further reduce the production cost, the Group reasonably adjusted the production plan after taking into accounts of the sales budget in the second half of the year and the sales in the first half of the year, and controlled the production cost through the measures of output reduction. In addition, the Group actively responded to the unfavourable environment of the market. On the one hand, the Group adjusted the product portfolio and strictly implemented the product quality control to ensure the stability of product quality, while it strengthened the market access for its products and explored the external processing business model to improve the utilization of production platform and reduce the fixed cost. On the other hand, the Group increased the environmental protection management and control, and promoted the application of clean production technology. It strengthened the implementation of classification and disposal of solid wastes, and reduced the total sludge to ensure that the discharge of sewage meets the treatment standards. The above measures reduced the operational risk under the weak economic environment to a certain extent.

During the period, the total production volume of cowhides was 8,477,000 sq. ft., representing a decrease of 1,623,000 sq. ft. or 16.1% as compared to 10,100,000 sq. ft. for the same period of last year. The production volume of grey hides was 4,641 tons, representing an increase of 1,798 tons or 63.2% as compared to 2,843 tons for the same period of last year. During the period, the total sales volume of cowhides was 7,863,000 sq. ft., representing a decrease of 2,968,000 sq. ft. or 27.4% as compared to 10,831,000 sq. ft. for the same period of last year. The sales volume of grey hides was 4,655 tons, representing an increase of 2,152 tons or 86.0% as compared to 2,503 tons for the same period of last year.

During the period, the consolidated turnover of the Group was HK$155,140,000, representing a decrease of HK$57,531,000 or 27.1% from HK$212,671,000 for the same period of last year, of which the sales value of cowhides amounted to HK$139,569,000 (six months ended 30 June 2016: HK$203,381,000), representing a decrease of 31.4%; and the sales value of grey hides and other products amounted to HK$15,571,000 (six months ended 30 June 2016: HK$9,290,000), representing an increase of 67.6%. During the period, as the demand in the footwear leather market continued to shrink, the intensified market competition led to the higher product requirements of customers, reduced demand for orders, declined sales volume and unit selling price as well as the gross profit turning negative, while the grey hides market was in the doldrums, demand dropped sharply, and the sales price continuously fluctuated at a low level, which increased the gross loss of grey hides. These combined to turn the gross profit of the Group into loss as a whole.

In terms of sales, the leather market mainly streamed to the production of thin shoes and sandals for the first half of the year, with sales volume of low-grade leather accounting for a high proportion and a variety of low-grade leather from different sources flooding to impact the leather market. Coupled with the emergence of on-line sales, the price war has become an accelerator of fierce competition, forced the brand footwear manufacturers to join the price war, resulting in an increase in demand for low-priced finished leather and the downward composite selling price. To confront the above difficulties, the Group strengthened the access of its products during the period, grasped the market changes and fashion trend of products, and adjusted production pursuant to the style demand to improve product quality and demand. In addition, the Group differentiated sales according to the market positioning and product grade, to improve the utilization of finished products through the adjustment of production technique, increase efforts on product research and development, and strive to keep up with the market rhythm for enhancement of the added value of products.

In terms of purchasing, the Group implemented the raw material purchasing strategy according to the production demand. During the period, the Group paid close attention to the changes of international cowhides market and purchased when appropriate to control the risk of huge price fluctuation of the cowhides. In addition, the Group initiated negotiations with chemical material suppliers for lower prices, while it strengthened the dynamic management of the warehouse to reduce the risks of deterioration and overstocking of chemical materials. During the period, total purchases amounted to HK$221,209,000, representing an increase of 71.2% as compared to the same period of last year.

As at 30 June 2017, the Group's consolidated inventory amounted to HK$317,720,000 (31 December 2016: HK$258,591,000), representing an increase of HK$59,129,000 or 22.9% over that of 31 December 2016. During the period, the Group set up a research and development project team to carry out special research and development as well as classified rectification and marketing of inventory. Meanwhile, it adjusted production techniques, and reasonably ordered grouping to actively destock the inventory for meeting customers' needs and for turning the slow-moving inventory into cash flow, so as to satisfy the financial needs in the normal operation of the Group.

Financial Review

As at 30 June 2017, the Group's cash and cash equivalents amounted to HK$25,426,000 (31 December 2016: HK$48,291,000), representing a decrease of HK$22,865,000 or 47.3% as compared to the same as at 31 December 2016, which were denominated in Hong Kong dollars (4.9%), Renminbi (93.4%) and United States dollars (1.7%). During the period, net cash outflows from operating activities was HK$18,731,000, which mainly attributable to an increase in inventory and trust receipt loans, resulting in an increase in net cash outflow. The net cash outflows from investing activities was HK$5,107,000, which mainly represented the increase in secured deposit and the payment of expenditures for the acquisition of machinery and equipment.

As at 30 June 2017, the Group's interest-bearing borrowings amounted to HK$188,448,000 (31 December 2016: HK$173,745,000), of which interest-bearing borrowings in Hong Kong dollars amounted to HK$65,000,000, and interest-bearing borrowings in United States dollars amounted to HK$123,448,000. The Group's borrowings mainly consisted of: (1) balances of short-term loans provided by the bank of HK$100,669,000, which were secured by bank balances of RMB13,923,000; and (2) balances of long-term unsecured intra-group borrowings of HK$87,779,000. The above interest-bearing borrowings were charged at floating interest rates.

As at 30 June 2017, the Group's gearing ratio of the interest-bearing borrowings to shareholders' equity plus interest-bearing borrowings was 48.0% (31 December 2016: 43.5%). During the period, the annual interest rate of the borrowings was approximately 2.0% to 3.2%. Of the Group's total borrowings, all were repayable within one year except for the loans from the immediate holding company amounting to HK$87,779,000. The Group's interest expenses during the period amounted to HK$3,578,000, representing an increase of 30.0% from the same period of last year, which was mainly attributable to the increase in bank loans during the period.

As at 30 June 2017, the total banking facilities of the Group was HK$207,396,000 (31 December 2016: HK$157,594,000), of which banking facilities of HK$100,669,000 (31 December 2016: HK$85,966,000) were utilised and banking facilities of HK$106,727,000 (31 December 2016: HK$71,628,000) were unutilised. Taking into account of the existing cash resources and available credit facilities, the Group had adequate financial resources to meet its day-to-day operational requirements.

Capital Expenditure

As at 30 June 2017, the net value of non-current assets including prepaid land lease payments and, property, plant and equipment amounted to HK$94,472,000, representing a decrease of HK$4,625,000 over the net value as at 31 December 2016 of HK$99,097,000. The capital expenditure for the period amounted to HK$1,191,000 (six months ended 30 June 2016: HK$3,885,000), which mainly represented the payment of expenditures for the acquisition of machinery and equipment to cope with the production requirements of the Group.

Pledge of Assets

As at 30 June 2017, certain of the Group's bank balances with a total of HK$16,042,000 (31 December 2016: HK$11,610,000) were pledged to banks 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. The Group is exposed to foreign currency risk primarily from import purchases from overseas suppliers that are denominated in a currency other than the functional currency of the operations to which they relate. The currency giving rise to this risk is mainly the United States dollars against Renminbi. The Group did not hedge its exposure to risks arising from fluctuations in exchange rates during the period. Should the Group consider that its exposure to foreign currency risk justifies hedging, the Group may use forward or hedging contracts to reduce the risks.

Remuneration Policy for Employees

As at 30 June 2017, a total of 529 employees (31 December 2016: 570) were employed by the Group. The 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 cash flow 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 insurances and pension schemes to all employees in different areas.

Prospects

In the second half of the year, the leather market is still in the status of "excessive output and disordered competition in the industry", and it is expected that in the second half of 2017, the overall trend of the leather industry is still not optimistic. In addition, labour and production costs and increased environmental pressures will further squeeze the profit margins of leather manufacturers, which will bring a more severe ordeal to the leather manufacturers. The Group will continuously implement the stable operating strategy with an aim of "maintaining stability and striving for survival" in response to the negative impact from the sluggish market. The Group will accelerate the integration of production capacity to promote the orderly release of production capacity with the overall operating stability as the prerequisite, so as to achieve the most economical scale of production. At the same time, the Group will strengthen the concert of production and research, improve product quality and increase inventory destocking to relieve the inventory pressure. Furthermore, the Group will continue to enhance the environmental protection control, intensify the internal control management mechanism, diversify the exploration of the new business model and actively promote the development of eco-leather, to strive to minimize various risks, overcome difficulties and reduce losses.

CORPORATE GOVERNANCE AND OTHER INFORMATION

Corporate Governance Code

The Company had complied with the code provisions and, where appropriate, the applicable recommended best practices in the Corporate Governance Code (the "CG Code") contained in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited throughout the six months ended 30 June 2017 except for the following:

The code provision A.2.1 of the CG Code provides that the roles of chairman and chief executive should be separate and should not be performed by the same individual (the Company regards that the term "chief executive" has the same meaning as the Managing Director of the Company).

Mr. Sun Jun serves as both the Chairman and the Managing Director of the Company with effect from February 2016. The Board believes that vesting the roles of both Chairman and Managing Director in the same person provides the Group with strong and consistent leadership and allows for effective and efficient planning and implementation of business strategies and decisions. It also considers that the current structure of vesting the roles of Chairman and Managing Director in the same person will not impair the balance of power and authority between the Board and the management of the Company. The Board will review the current structure from time to time to ensure appropriate and timely action to meet changing circumstances.

Review of Interim Results

The unaudited interim results of the Group and the Company's interim report for the six months ended 30 June 2017 have been reviewed by the Audit Committee and Messrs. Ernst & Young, the auditors of the Company.

Purchase, Sale and Redemption of the Company's Listed Securities

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities during the six months ended 30 June 2017.

By order of the Board
Sun Jun
Chairman and Managing Director

Hong Kong, 28 August 2017

As at the date of this announcement, the Board of the Company comprises one Executive Director, namely Mr. Sun Jun; three Non-Executive Directors, namely Mr. Xiao Zhaoyi, Mr. Kuang Hu and Mr. Ran Bo; and three Independent Non-Executive Directors, namely Mr. Fung Lak, Mr. Choi Kam Fai, Thomas and Mr. Chan Cheong Tat.