GDH

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 2018

Unaudited financial highlights for the six months ended 30 June

	2018 **HK$'000**	2017 HK$'000	Changes %
Revenue	**122,260**	155,140	-21.2
Loss attributable to shareholders of the Company	**(48,015)**	(32,464)	-47.9
Loss per share — Basic	**HK(8.92)cents**	HK(6.03)cents	-47.9

CONDENSED CONSOLIDATED FINANCIAL INFORMATION
FOR THE SIX MONTHS ENDED 30 JUNE 2018

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 2018 together with comparative figures for the corresponding period in 2017. These results have not been audited, but have 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 2018

	Notes	**2018**	2017
		HK$'000	*HK$'000*
		(Unaudited)	(Unaudited)
REVENUE			
Processing and sale of leather	*3*	**122,260**	155,140
Cost of sales		**(142,573)**	(167,716)
Gross loss		**(20,313)**	(12,576)
Other income and gains	*3*	**1,174**	714
Selling and distribution expenses		**(1,210)**	(951)
Administrative expenses		**(15,060)**	(12,742)
Impairment on items of property, plant and equipment		**(9,091)**	(3,300)
Finance costs	*4*	**(3,461)**	(3,578)
LOSS BEFORE TAX	*4*	**(47,961)**	(32,433)
Income tax expense	*5*	**(54)**	(31)
LOSS FOR THE PERIOD		**(48,015)**	(32,464)
LOSS PER SHARE	*6*		
- Basic		**HK(8.92) cents**	HK(6.03) cents
- Diluted		**HK(8.92) cents**	HK(6.03) cents

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR THE SIX MONTHS ENDED 30 JUNE 2018

	2018 *HK$'000* (Unaudited)	2017 *HK$'000* (Unaudited)
LOSS FOR THE PERIOD	**(48,015)**	(32,464)
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	**231**	1,012
Income tax effect	**(58)**	(253)
	173	759
Other comprehensive income/(loss) to be reclassified to the statement of profit or loss in subsequent periods:		
Exchange differences on translation of foreign operations	**(1,111)**	10,846
OTHER COMPREHENSIVE INCOME/(LOSS) FOR THE PERIOD, NET OF TAX	**(938)**	11,605
TOTAL COMPREHENSIVE LOSS FOR THE PERIOD	**(48,953)**	(20,859)

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION
30 JUNE 2018

	Notes	**30 June 2018** *HK$'000* **(Unaudited)**	31 December 2017 *HK$'000* (Audited)
NON-CURRENT ASSETS			
Property, plant and equipment		**55,428**	65,887
Prepaid land lease payments		**12,058**	12,313
Total non-current assets		**67,486**	78,200
CURRENT ASSETS			
Inventories		**171,513**	218,900
Receivables, prepayments and deposits	*8*	**97,440**	93,641
Pledged bank balances		**1,488**	1,066
Cash and bank balances		**9,145**	29,108
Total current assets		**279,586**	342,715
CURRENT LIABILITIES			
Trade payables	*9*	**56,394**	49,551
Other payables and accruals		**29,348**	28,902
Contract liabilities		**3,034**	-
Interest-bearing bank borrowings		**5,320**	-
Due to a PRC joint venture partner		**1,131**	1,131
Loan from a fellow subsidiary		**-**	41,177
Provision		**3,784**	3,816
Tax payable		**31**	33
Total current liabilities		**99,042**	124,610
NET CURRENT ASSETS		**180,544**	218,105
TOTAL ASSETS LESS CURRENT LIABILITIES		**248,030**	296,305
NON-CURRENT LIABILITIES			
Loans from the immediate holding company		**141,758**	141,138
Deferred tax liabilities		**3,953**	3,895
Total non-current liabilities		**145,711**	145,033
Net assets		**102,319**	151,272
EQUITY			
Share capital		**75,032**	75,032
Other reserves		**27,287**	76,240
Total equity		**102,319**	151,272

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 and the applicable disclosure requirements of Appendix 16 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited. The unaudited interim financial information does not include all 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 2017.

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 2017, except for the adoption of the new and revised Hong Kong Financial Reporting Standards ("HKFRSs") (which also include HKASs and Interpretation) effective as at 1 January 2018. 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 2017 that is included in this unaudited interim condensed financial information for the six months ended 30 June 2018 as comparative information does not constitute the statutory annual consolidated financial statements of the Company for the 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 2017 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 auditor has reported on those consolidated financial statements. The auditor's report was unqualified; did not include a reference to any matters to which the auditor drew attention by way of emphasis without qualifying its 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 HKFRS 2	*Classification and Measurement of Share-based Payment Transactions*
Amendments to HKFRS 4	*Applying HKFRS 9 Financial Instruments with HKFRS 4 Insurance Contracts*
HKFRS 9	*Financial Instruments*
HKFRS 15	*Revenue from Contracts with Customers*
Amendments to HKFRS 15	*Clarifications to HKFRS 15 Revenue from Contracts with Customers*
Amendments to HKAS 40	*Transfers of Investment Property*
HK(IFRIC)-Int 22	*Foreign Currency Transactions and Advance Consideration*
Annual Improvements 2014-2016 Cycle	Amendments to HKFRS 1 and HKAS 28

Other than as further explained below regarding the impact of HKFRS 9 and HKFRS 15, the adoption of the new and revised HKFRSs has had no material impact on the unaudited interim financial information of the Group. The principal effects for adopting HKFRS 9 and HKFRS 15 are as follows:

(a) HKFRS 9 Financial Instruments

HKFRS 9 brings together all phases of the financial instruments project to replace HKAS 39 and all previous versions of HKFRS 9 for annual periods on or after 1 January 2018. The Group has not restated comparative information for 2017 for financial instruments in the scope of HKFRS 9. Therefore, the comparative information for 2017 is reported under HKAS 39 and is not comparable to the information presented for 2018.

<u>Classification and measurement</u>
The Group initially measures a financial asset at its fair value and, in the case of a financial asset not at fair value through profit or loss ("FVPL"), plus transaction costs.

Under HKFRS 9, debt financial instruments are subsequently measured at FVPL, amortised cost, or fair value through other comprehensive income ("FVOCI"). The classification is based on two criteria: the Group's business model for managing the assets; and whether the instruments' contractual cash flows represent 'solely payments of principal and interest' on the principal amount outstanding (the "SPPI criterion").

The new classification and measurement of the Group's financial assets is, as follows:

- Debt instruments at amortised cost for financial assets that are held within a business model with the objective to hold the financial assets in order to collect contractual cash flows that meet the SPPI criterion. This category includes the Group's trade receivables, and financial assets included in receivables, deposits and other receivables pledged bank balances, and cash and bank balances.

- Debt instruments at FVOCI, with recycling of gains or losses to profit or loss on derecognition, include bills receivables which are debt instruments which the Group intends to hold for the foreseeable future and both to collect contractual cash flows and to sell the instruments.

The assessment of the Group's business models was made as of the date of initial application, 1 January 2018, and applied to those financial assets that were not derecognised before 1 January 2018. The assessment of whether contractual cash flows on debt instruments are solely comprised of principal and interest was made based on the facts and circumstances as at the initial recognition of the assets. Bills receivables are classified as loans and receivables at amortised cost under HKAS 39. Upon adoption of HKFRS 9, the bills receivables are measured at FVOCI.

The accounting for the Group's financial liabilities remains largely the same as it was under HKAS 39. Similar to the requirements of HKAS 39, HKFRS 9 requires contingent consideration liabilities to be treated as financial instruments measured at fair value, with the changes in fair value recognised in profit or loss.

Under HKFRS 9, embedded derivatives are no longer separated from a host financial asset. Instead, financial assets are classified based on their contractual terms and the Group's business model. The accounting for derivatives embedded in financial liabilities and in non-financial host contracts has not changed from that required by HKAS 39. Other than the above, the adoption of HKFRS 9 has no material impact on classification and measurement of the Group's financial assets.

Impairment
The adoption of HKFRS 9 has fundamentally changed the Group's accounting for impairment losses for financial assets by replacing HKAS 39's incurred loss approach with a forward-looking expected credit loss ("ECL") approach.

HKFRS 9 requires the Group to record an allowance for ECLs for all loans and other debt financial assets not held at FVPL.

The ECL allowance is based on difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Group expects to receive. The shortfall is then discounted at an approximation to the asset's original effective interest rate ("EIR").

For trade receivables and other financial assets stated at amortised cost, the Group has applied the standard's simplified approach and has calculated ECLs based on lifetime expected credit losses. Assessment is based on the Group's historical credit loss experience, adjusted for forward-looking factors specific to the debtors and the economic environment.

Financial assets stated at FVOCI are assessed for impairment based on 12-month ECLs: 12-month ECLs are the portion of lifetime ECLs that result from default events that are possible within the 12 months after the reporting date (or a shorter period if the expected life of the asset is less than 12 months). However, when there has been a significant increase in credit risk since origination, the allowance will be based on the lifetime ECL.

The adoption of the ECL requirements of HKFRS 9 does not have material impact on the carrying amounts of the Group's financial assets.

(b) HKFRS 15 Revenue from Contracts with Customers

HKFRS 15 supersedes HKAS11 *Construction Contracts,* HKAS 18 *Revenue* and related interpretations and it applies to all revenue arising from contracts with customers, unless those contracts are in the scope of other standards. The new standard establishes a five-step model to account for revenue arising from contracts with customers. Under HKFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer.

The standard requires entities to exercise judgement, taking into consideration all of the relevant facts and circumstances when applying each step of the model to contracts with their customers. The standard also specifies the accounting for the incremental costs of obtaining a contract and the costs directly related to fulfilling a contract.

The Group has elected to apply the modified retrospective approach for transition to the new revenue standard. Under this transition approach, comparative information for prior periods is not restated, the Group recognises the cumulative effect of initially applying the guidance as adjustments to the opening balance of retained profits (or other component of equity, as appropriate) on 1 January 2018, and the Group applies the new requirements only to contracts that are not yet completed on that date.

The adoption from 1 January 2018 resulted in changes in accounting policies for revenue recognition as detailed below.

Revenue from contracts with customers
Under HKFRS 15, revenue is measured based on the consideration specified in a contract with a customer and excludes amounts collected on behalf of third parties. The Group recognised revenue when it transfers control over a product or service to a customer. This may be at a single point in time or over time.

Under HKFRS 15, the Group satisfied a performance obligation and recognises revenue over time, if one of the following criteria is met:

(i) The customer simultaneously receives and consumes the benefits provided by the Group's performance as the Group performs.

(ii) The Group's performance creates or enhances an asset that the customer controls as the asset is created or enhanced.

(iii) The Group's performance does not create an asset with an alternate use to the Group and the Group has an enforceable right to payment for performance completed to date.

If none of the above conditions are met, the Group recognises revenue at a single point in time at which the performance obligation is satisfied for the sale of that good or service.

Revenue from sale of leather is recognised at the point when the control of the goods is transferred to the customers.

Contract assets and contract liabilities
A receivable is recognised only if the Group has an unconditional right to consideration. If the Group recognises the related revenue before being unconditionally entitled to the consideration for the promised goods and services in the contract, then the entitlement to consideration is classified as a contract asset. Similarly, a contract liability, rather than a payable, is recognised when a customer pays consideration, or is contractually required to pay consideration and the amount is already due, before the Group recognises the related revenue. For a single contract with the customer, either a net contract asset or a net contract liability is presented. For multiple contracts, contract assets and contract liabilities of unrelated contracts are not presented on a net basis. The Group recognises the incremental costs of obtaining a contract with a customer within contract assets if the Group expects to recover those costs.

Generally, the Group receives advances from its customers which are short-term in nature. Advances from customers of HK$1,308,000 in total meet the definition of contract liabilities as at 1 January 2018 previously included in other payables and accruals are reclassified as contract liabilities.

Apart from the above, there was no other material impact upon adoption of HKFRS 15.

(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$7,686,000 (six months ended 30 June 2017: HK$24,377,000) was derived from sales to a single customer, which contributed approximately 6% (six months ended 30 June 2017: 16%) 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 and is recognised at a point in time.

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

	For the six months ended	
	30 June 2018	30 June 2017
	HK$'000	*HK$'000*
	(Unaudited)	(Unaudited)
Revenue		
Processing and sale of leather	**122,260**	155,140
Other income and gains		
Government grants	**355**	11
Interest income	**24**	40
Sale of scrap materials	**332**	595
Processing of second-layer grey leather	**459**	-
Others	**4**	68
	1,174	714

(4) LOSS BEFORE TAX

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

	For the six months ended	
	30 June 2018	30 June 2017
	HK$'000	*HK$'000*
	(Unaudited)	(Unaudited)
Cost of inventories sold*	**133,250**	163,276
Depreciation	**2,493**	5,547
Provision for impairment of trade receivables	**134**	501
Foreign exchange differences, net	**284**	(1,584)
Loss on disposal of property, plant and equipment	**-**	368
Interest on:		
Bank loans and discounting bills receivables to banks	**656**	1,646
Loans from the immediate holding company	**2,142**	1,932
Loan from a fellow subsidiary	**663**	-
	3,461	3,578
Provision for inventories*	**9,323**	4,440

*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 profits tax has been made as the Group did not generate any assessable profits arising in Hong Kong during the period (six months ended 30 June 2017: 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 2018	30 June 2017
	HK$'000	*HK$'000*
	(Unaudited)	(Unaudited)
Group - Mainland China		
Provision for the period	**54**	47
Overprovision in prior years	**-**	(16)
Total tax expense for the period	**54**	31

(6) LOSS PER SHARE

The calculation of basic loss per share amounts is based on the loss for the period of HK$48,015,000 (six months ended 30 June 2017: HK$32,464,000) and the weighted average number of ordinary shares of 538,019,000 (30 June 2017: 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 2018 and 30 June 2017 in the calculation of diluted loss per share as there are no dilutive events during the periods ended 30 June 2018 and 30 June 2017.

(7) DIVIDEND

The Board has resolved not to declare the payment of an interim dividend for the six months ended 30 June 2018 (six months ended 30 June 2017: Nil).

(8) RECEIVABLES, PREPAYMENTS AND DEPOSITS

As at 30 June 2018, included in the Group's receivables, prepayments and deposits were trade and bills receivables with a net balance of HK$93,973,000 (31 December 2017: HK$90,536,000) 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 2018 *HK$'000* **(Unaudited)**	31 December 2017 *HK$'000* (Audited)
Current	**87,811**	89,618
Less than 3 months	**4,074**	2,085
More than 3 months	**3,880**	510
	95,765	92,213
Impairment	**(1,792)**	(1,677)
	93,973	90,536

(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 2018 *HK$'000* **(Unaudited)**	31 December 2017 *HK$'000* (Audited)
Within 3 months	**41,234**	32,104
3 to 6 months	**11,715**	14,266
Over 6 months	**3,445**	3,181
	56,394	49,551

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

MANAGEMENT DISCUSSION AND ANALYSIS

Results

The unaudited consolidated loss attributable to shareholders for the six months ended 30 June 2018 of the Group was HK$48,015,000, representing an increase of loss of HK$15,551,000, or 47.9% as compared to the loss of HK$32,464,000 for the same period of last year.

The unaudited net asset value of the Group as at 30 June 2018 was HK$102,319,000, representing a decrease of HK$102,214,000 and HK$48,953,000 as compared to the net asset value as at 30 June 2017 and 31 December 2017, respectively.

The Board resolved not to declare the payment of an interim dividend for the six months ended 30 June 2018 (six months ended 30 June 2017: Nil).

Business Review

Given the drastic changes in the external market environment, increasing varieties of footwear materials and the strengthening substitution effect of new materials in recent years, de-capacity has further intensified within the tannery industry. In addition, nationwide environmental inspections and supervisions have been commenced due to the nation's more stringent environmental requirements for footwear manufacturing industry, resulting into the closing down or production suspension of a large number of medium-sized and small-sized footwear manufacturers. All of these have led to the shrinking demand of the whole downstream leather market, thereby exerting hefty pressure on the production and operations of the leather processing enterprises. During the period, the Group adhered to its prudent operating strategy with "stable operations to ensure asset safety" as its principal operating strategy in the first half year. Under the circumstances of the fall of both sales volume and selling prices and surging production costs, the Group recorded further operating loss. During the period, the Group proactively rolled out various measures in response to the unfavorable downstream environment of the industry. On one hand, the Group adjusted product portfolio and expanded markets to reinforce de-stocking, while stepping up efforts in expanding the external subcontracting business to strive for reduction of fixed cost. On the other hand, the Group continued to push forward the application of clean production technology to ensure that the discharge of sewage meets the treatment standards and appropriate measures are in place against the environmental risks. 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 7,506,000 sq. ft., representing a decrease of 971,000 sq. ft. or 11.5% as compared to 8,477,000 sq. ft. for the same period of last year. The production volume of grey hides was 1,379 tons, representing a decrease of 3,262 tons or 70.3% as compared to 4,641 tons for the same period of last year. During the period, the total sales volume of cowhides was 6,554,000 sq. ft., representing a decrease of 1,309,000 sq. ft. or 16.7% as compared to 7,863,000 sq. ft. for the same period of last year. The sales volume of grey hides was 1,379 tons, representing a decrease of 3,276 tons or 70.4% as compared to 4,655 tons for the same period of last year.

During the period, the consolidated turnover of the Group was HK$122,260,000, representing a decrease of HK$32,880,000 or 21.2% from HK$155,140,000 for the same period of last year, of which the sales value of cowhides amounted to HK$117,580,000 (six months ended 30 June 2017: HK$139,569,000), representing a decrease of 15.8%; and the sales value of grey hides and other products amounted to HK$4,680,000 (six months ended 30 June 2017: HK$15,571,000), representing a decrease of 69.9%. During the period, against the backdrop of prolonged downward trend of cowhides prices, weak purchasing power of footwear manufacturers, coupled with the substitution effect of the up-and-coming new materials which led to intense market competition, the overall demand for footwear leather shrank, resulting into a drop of both the sales volume and price, and therefore the sales revenue of the Group's footwear leather products was decreased.

In terms of sales, in light of the consumers' diversified demands for footwear and their preference for polyurethane-based materials or other emerging materials, leather market has seen slumping demand. In addition, facing with the shrinking demand and tightening environmental control and treatment, some of the branded footwear manufacturers in the PRC have been experiencing difficult operations, financial strain and loss-making for consecutive years, whereas the medium-sized and small sized footwear manufacturers have also announced production suspension or closing down. All the above directly leaded to a plunge in the number of orders received by footwear tannery manufacturers. To confront such difficulties, during the period, the Group put strenuous effort in expanding and exploring markets, ramping up the sales in middle-ended and low-ended markets and optimizing customer portfolio. In parallel with these, the Group endeavored to scale up marketing efforts and initiated more site-visiting to various markets to understand market changes and product trends, strengthen product research and development and press on destocking.

In terms of purchasing, during the period, taking destocking and generating operating cash flows as top priorities, the Group implemented a procurement strategy featured with small quantities, frequent procurements and targeted replenishment to ensure that its production needs were satisfied. Meanwhile, during the period, the Group performed in-depth analysis on changes in slaughtering volume, supply and the market of products, closely monitored the trends of leather price in both international and domestic markets, and intensified the study and research on market conditions to prevent procurement risk. During the period, the total purchases amounted to HK$82,240,000 representing a decrease of 62.8% as compared to the same period last year.

As at 30 June 2018, the Group's consolidated inventory amounted to HK$171,513,000 (31 December 2017: HK$218,900,000), representing a decrease of HK$47,387,000 or 21.7% over that of 31 December 2017. During the period, the Group enhanced the synergy between production, supply and distribution, spared no effort in reducing existing inventory level and conducted theme-based research, classification and rectification as well as product portfolio diversification based on existing inventory, in an effort to satisfy customers' needs on one hand, and to generate cash flows from the slow-moving inventory on the other hand, so as to ensure funding for the Group's normal operations. In consideration of the higher inventory cost and the increasing production cost of leather and the absence of a corresponding increase in the selling price of cowhides, the Group revaluated the ageing of inventory and its net realizable value and a provision for inventories of HK$9,323,000 (six months ended 30 June 2017: provision for inventories of HK$4,440,000) was made for the six months ended 30 June 2018.

As at 30 June 2018, the Group's property, plant and equipment amounted to HK$55,428,000 (31 December 2017: HK$65,887,000), representing a decrease of HK$10,459,000 or 15.9% over that of 31 December 2017. Due to the decline in the operating results of the Group during the period, the recoverable amount of the property, plant and equipment was calculated by using a value in use calculation based on the discounted cash flow method and an impairment loss of HK$9,091,000 (six months ended 30 June 2017: HK$3,300,000) was made for the six months ended 30 June 2018.

Financial Review

As at 30 June 2018, the Group's cash and cash equivalents amounted to HK$9,145,000 (31 December 2017: HK$29,108,000), representing a decrease of HK$19,963,000 or 68.6% as compared to the same as at 31 December 2017, which were denominated in Hong Kong dollars (14.0%), Renminbi (81.0%) and United States dollars (5.0%). During the period, net cash inflows from operating activities was HK$23,196,000, which was mainly attributable to a decrease in inventory, resulting in an increase in net cash inflow. The net cash outflow from investing activities was HK$1,416,000, which mainly represented the payment of expenditures for the acquisition of machinery and equipment. Net cash outflow from a financial activity amounted to HK$42,106,000, which mainly represented the repayment of short-term loans from a fellow subsidiary.

As at 30 June 2018, the Group's interest-bearing borrowings amounted to HK$93,099,000 (31 December 2017: HK$128,956,000), 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$28,099,000 The Group's borrowings mainly consisted of: (1) balances of short-term loans provided by the bank of HK$5,320,000, which were secured by bank balances of RMB1,255,000; 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 2018, the Group's gearing ratio of the interest-bearing borrowings to shareholders' equity plus interest-bearing borrowings was 47.6% (31 December 2017: 46.0%). During the period, the annual interest rate of the borrowings was approximately 3.2% to 5.7%. 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$3,461,000, representing a decrease of 3.3% from the same period of last year, which was mainly attributable to the decrease in bank loans during the period.

As at 30 June 2018, the total banking facilities of the Group was HK$105,430,000 (31 December 2017: HK$119,630,000), of which banking facilities of HK$5,320,000 (31 December 2017: HK$0) were utilised and banking facilities of HK$100,110,000 (31 December 2017: HK$119,630,000) 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 2018, the net value of non-current assets including prepaid land lease payments and, property, plant and equipment amounted to HK$67,486,000, representing a decrease of HK$10,714,000 over the net value as at 31 December 2017 of HK$78,200,000. The capital expenditure for the period amounted to HK$971,000 (six months ended 30 June 2017: HK$1,191,000), 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 2018, certain of the Group's bank balances with a total of HK$1,488,000 (31 December 2017: HK$1,066,000) 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, European 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 and European 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 2018, a total of 421 employees (31 December 2017: 461) 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

It is expected that in the second half of 2018, the overall trend of the leather industry is still not optimistic. Economic downturn within the industry and sluggish demand will further squeeze the profit margins of leather manufacturers, which will bring a more severe ordeal to them. The Group will continue to implement its principal strategy of "stable operations to ensure asset safety" to mitigate the negative impact caused by the weak market. An array of measures will be rolling out in succession with the main theme of reducing inventory and maintaining stable operations. The Group will promote the research and development of new products and refined management with the specific focus on the product portfolios of the inventory, targeted markets and customers' demands, aiming to further press ahead with destocking and generation of cash flows from inventory. Meanwhile, risk control system will be enhanced to cover all exposures and strive to reduce various risks, thereby ensuring stable production, compliance with environmental protection requirements and loss reduction.

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 2018 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 26 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 for the six months ended 30 June 2018 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 on The Stock Exchange of Hong Kong Limited during the six months ended 30 June 2018.

By order of the Board
Sun Jun
Chairman and Managing Director

Hong Kong, 27 August 2018

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. Ding Yatao; and three Independent Non-Executive Directors, namely Mr. Fung Lak, Mr. Choi Kam Fai, Thomas and Mr. Chan Cheong Tat.