Arts Group

ARTS OPTICAL INTERNATIONAL HOLDINGS LIMITED

雅視光學集團有限公司*

(Incorporated in Bermuda with limited liability)

(Stock Code: 1120)

INTERIM RESULTS
FOR THE SIX MONTHS ENDED 30TH JUNE, 2008

INTERIM RESULTS

The board of directors (the "Board") of Arts Optical International Holdings Limited (the "Company") is pleased to announce the unaudited consolidated results of the Company and its subsidiaries (together, the "Group") for the six months ended 30th June, 2008 together with comparative figures for the corresponding period in 2007.

CONDENSED CONSOLIDATED INCOME STATEMENT

FOR THE SIX MONTHS ENDED 30TH JUNE, 2008

		Six months ended	
		30.6.2008	30.6.2007
	Notes	***HK$'000***	*HK$'000*
		(unaudited)	(unaudited)
Revenue	3	**669,473**	609,420
Cost of sales		**(503,709)**	(435,573)
Gross profit		**165,764**	173,847
Other income		**21,897**	11,639
Distribution and selling expenses		**(22,743)**	(19,805)
Administrative expenses		**(75,540)**	(74,477)
Other expenses		**(4,967)**	(753)
Finance costs	4	**(479)**	(124)
Profit before taxation		**83,932**	90,327
Taxation	5	**(8,580)**	(8,706)
Profit for the period	6	**75,352**	81,621
Attributable to:			
Equity holders of the parent		**74,765**	81,893
Minority interests		**587**	(272)
		75,352	81,621
Dividend paid	7	**30,692**	26,856
Earnings per share	8		
– Basic		**19.5 HK cents**	21.3 HK cents

CONDENSED CONSOLIDATED BALANCE SHEET

AT 30TH JUNE, 2008

	Notes	30.6.2008 HK$'000 (unaudited)	31.12.2007 HK$'000 (audited)
Non-current Assets			
Investment property		**7,400**	7,400
Property, plant and equipment		**547,771**	501,674
Prepaid lease payments		**35,109**	33,565
Deposits paid for acquisition of property, plant and equipment		**5,177**	4,783
Intangible assets		**4,680**	4,680
Loan receivable		**13,572**	14,137
Available-for-sale investments		**5,858**	5,858
Deferred tax assets		**53**	53
		619,620	572,150
Current Assets			
Inventories		**218,973**	210,980
Debtors, deposits and prepayments	9	**378,111**	353,241
Loan receivable		**2,262**	2,262
Prepaid lease payments		**878**	834
Tax recoverable		**–**	108
Short-term bank deposit		**5,001**	7,506
Bank balances and cash		**79,133**	100,934
		684,358	675,865
Assets classified as held for sale		**–**	3,227
		684,358	679,092
Current Liabilities			
Creditors and accrued charges	10	**277,447**	286,348
Bank borrowings		**19,419**	36,835
Tax liabilities		**9,061**	1,967
		305,927	325,150
Net Current Assets		**378,431**	353,942
Total Assets less Current Liabilities		**998,051**	926,092
Capital and Reserves			
Share capital		**38,365**	38,365
Reserves		**939,022**	869,551
Equity attributable to equity holders of the parent		**977,387**	907,916
Minority interests		**3,989**	1,552
Total Equity		**981,376**	909,468
Non-current Liabilities			
Deferred tax liabilities		**15,566**	15,566
Loan from a minority shareholder of a subsidiary		**1,109**	1,058
		16,675	16,624
		998,051	926,092

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PREPARATION

The condensed consolidated financial statements have been prepared in accordance with the applicable disclosure requirements of Appendix 16 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") and with Hong Kong Accounting Standard ("HKAS") 34 "Interim Financial Reporting" issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA").

2. PRINCIPAL ACCOUNTING POLICIES

The condensed consolidated financial statements have been prepared on the historical cost basis except for investment property which is measured at fair value.

The accounting policies used in the condensed consolidated financial statements are consistent with those followed in the preparation of the Group's annual financial statements for the year ended 31st December, 2007.

In the current interim period, the Group has applied, for the first time, the following new interpretations ("new Interpretations") issued by the HKICPA, which are effective for the Group's financial year beginning on 1st January, 2008.

HK(IFRIC) – Int 11	HKFRS 2: Group and Treasury Share Transactions
HK(IFRIC) – Int 12	Service Concession Arrangements
HK(IFRIC) – Int 14	HKAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction

The adoption of these new Interpretations had no material effect on the results or financial position of the Group for the current or prior accounting periods. Accordingly, no prior period adjustement has been recognised.

The Group has not early applied the following new or revised standards, amendments or interpretations that have been issued but are not yet effective.

HKAS 1 (Revised)	Presentation of Financial Statements[1]
HKAS 23 (Revised)	Borrowing Costs[1]
HKAS 27 (Revised)	Consolidated and Separate Financial Statements[2]
HKAS 32 & 1 (Amendments)	Puttable Financial Instruments and Obligations Arising on Liquidation[1]
HKFRS 2 (Amendment)	Vesting Conditions and Cancellations[1]
HKFRS 3 (Revised)	Business Combinations[2]
HKFRS 8	Operating Segments[1]
HK(IFRIC) – Int 13	Customer Loyalty Programmes[3]
HK(IFRIC) – Int 15	Agreements for the Construction of Real Estate[1]
HK(IFRIC) – Int 16	Hedges of a Net Investment in a Foreign Operation[4]

[1]Effective for annual periods beginning on or after 1st January, 2009.
[2]Effective for annual periods beginning on or after 1st July, 2009.
[3]Effective for annual periods beginning on or after 1st July, 2008.
[4]Effective for annual periods beginning on or after 1st October, 2008.

The adoption of HKFRS 3 (Revised) may affect the accounting for business combination for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1st July, 2009. HKAS 27 (Revised) will affect the accounting treatment for changes in a parent's ownership interest in a subsidiary that do not result in a loss of control, which will be accounted for as equity transactions. The directors of the Company anticipate that the application of the other new or revised standards, amendments or interpretations will have no material impact on the results and the financial position of the Group.

3. SEGMENT INFORMATION

Revenue

Revenue represents the amounts received and receivable for goods sold to outside customers during the period.

Business segments

The Group is principally engaged in the design, manufacture and sales of optical products. No business segment analysis is presented as management considers this as one single business segment.

Geographical segments

The Group's operations and assets are located in Hong Kong and elsewhere in the People's Republic of China (the "PRC"). Segment information of the Group by location of customers is presented as below:

	Six months ended			
	30.6.2008	**30.6.2008**	30.6.2007	30.6.2007
	Revenue	**Results**	Revenue	Results
	HK$'000	***HK$'000***	*HK$'000*	*HK$'000*
Europe	**440,426**	**78,778**	377,116	75,918
United States	**180,472**	**31,995**	181,451	35,958
Asia	**32,102**	**12,722**	36,262	7,366
Other regions	**16,473**	**1,737**	14,591	2,245
	669,473	**125,232**	609,420	121,487
Unallocated income		**4,898**		4,285
Unallocated corporate expenses		**(45,897)**		(36,064)
Interest income on bank deposits		**178**		743
Finance costs		**(479)**		(124)
Profit before taxation		**83,932**		90,327
Taxation		**(8,580)**		(8,706)
Profit for the period		**75,352**		81,621

4. FINANCE COSTS

	Six months ended	
	30.6.2008	30.6.2007
	HK$'000	*HK$'000*
Interest on bank borrowings wholly repayable within five years	**428**	79
Imputed interest on loan from a minority shareholder of a subsidiary	**51**	45
	479	124

5. TAXATION

	Six months ended	
	30.6.2008	30.6.2007
	HK$'000	*HK$'000*
The charge comprises:		
Current taxation		
Hong Kong Profits Tax	**8,580**	9,846
Deferred taxation		
Current year	**–**	(1,140)
	8,580	8,706

Hong Kong Profits Tax is recognised based on the management's best estimate of the weighted average annual income tax rate expected for the full financial year. On 26th June, 2008, the Hong Kong Legislative Council passed the Revenue Bill 2008 which includes the reduction in corporate profits tax rate by 1% to 16.5% effective from the year of assessment 2008-2009. The effect of such decrease has been reflected in measuring the current tax for the six months ended 30th June, 2008. The estimated average annual tax rate used is 16.5% (2007: 17.5%) for the six months ended 30th June, 2008. The change in tax rate has no material impact on deferred tax balances.

PRC enterprise income tax is calculated at the applicable rates in accordance with the relevant rules and regulations in the PRC.

A portion of the Group's profits neither arises in, nor is derived from, Hong Kong. Accordingly, that portion of the Group's profit is not subject to Hong Kong Profits Tax. Further, in the opinion of the directors of the Company, that portion of the Group's profit is not subject to taxation in any other jurisdiction in which the Group operates for the period.

6. PROFIT FOR THE PERIOD

	Six months ended	
	30.6.2008	30.6.2007
	HK$'000	*HK$'000*
Profit for the period has been arrived at after charging (crediting):		
Cost of inventories recognised as an expense	**503,709**	435,573
Depreciation of property, plant and equipment	**38,893**	32,735
Gain on disposal of assets classified as held for sale	**6,226**	–
Gain on disposal of partial interest in a subsidiary	**4,442**	–
Loss (gain) on disposal of property, plant and equipment	**63**	(28)
Net foreign exchange loss (gain)	**4,435**	(3,836)
Release of prepaid lease payments	**412**	340

7. DIVIDEND PAID

	Six months ended	
	30.6.2008	30.6.2007
	HK$'000	*HK$'000*
Final dividend paid in respect of 2007 of 8 HK cents (2007: 7 HK cents in respect of 2006) per share	**30,692**	26,856

The interim dividend in respect of 2008 of 7 HK cents (2007: 8 HK cents) per share amounting to a total of HK$26,856,000 (2007: HK$30,692,000) has been declared by the board of directors on 18th September, 2008.

8. EARNINGS PER SHARE

The calculation of the basic earnings per share attributable to the ordinary equity holders of the Company is based on the following data:

	Six months ended	
	30.6.2008	30.6.2007
	HK$'000	*HK$'000*
Earnings for the purpose of basic earnings per share	**74,765**	81,893
	Number of shares	
Number of shares for the purpose of basic earnings per share	**383,650,000**	383,650,000

9. DEBTORS, DEPOSITS AND PREPAYMENTS

The Group has a policy of allowing an average credit period of 30 days to 120 days to its trade debtors.

Included in the Group's debtors, deposits and prepayments are trade debtors of HK$371,445,000 (31st December, 2007: HK$347,158,000), an aging analysis of which at the balance sheet date is as follows:

	30.6.2008	31.12.2007
	HK$'000	*HK$'000*
Current	**288,474**	272,264
1 to 90 days overdue	**80,356**	72,526
More than 90 days overdue	**2,615**	2,368
	371,445	347,158

10. CREDITORS AND ACCRUED CHARGES

Included in the Group's creditors and accrued charges are trade creditors of HK$173,428,000 (31st December, 2007: HK$179,403,000), an aging analysis of which at the balance sheet date is as follows:

	30.6.2008	31.12.2007
	HK$'000	*HK$'000*
Current	**153,739**	118,146
1 to 90 days overdue	**15,351**	52,120
More than 90 days overdue	**4,338**	9,137
	173,428	179,403

DIVIDEND

The Board has resolved to declare an interim dividend of 7 HK cents per share for the six months ended 30th June, 2008 (2007: 8 HK cents per share). The interim dividend will be payable on 20th October, 2008 to shareholders whose names appear on the register of members of the Company on 13th October, 2008.

CLOSURE OF REGISTER OF MEMBERS

The register of members of the Company will be closed from 10th October, 2008 to 13th October, 2008, both days inclusive, during which period no transfer of shares will be effected. All transfers, accompanied by the relevant share certificates, must be lodged with the Company's share registrar in Hong Kong, Tricor Secretaries Limited at 26/F., Tesbury Centre, 28 Queen's Road East, Hong Kong for registration not later than 4:30 p.m. on 9th October, 2008 in order to qualify for the interim dividend mentioned above.

BUSINESS REVIEW

Profitability review and analysis

2008 is a very challenging year for the Group. The Group's consolidated revenue increased by 10% to HK$669.5 million (2007: HK$609.4 million) whereas the profit attributable to the equity holders of the Company decreased by 9% to HK$74.8 million (2007: HK$81.9 million) in the six months ended 30th June, 2008. Basic earnings per share decreased by 9% to 19.5 HK cents (2007: 21.3 HK cents) in the period under review.

The gross margin of the Group continued to be under pressure in 2008. Gross profit margin declined by 3.7% from 28.5% in the first half of 2007 to 24.8% in the corresponding period of 2008. Although modest adjustments were made to the selling prices of the Group's products, this could not offset the effects of escalating raw material costs, labour wages, record energy prices and gradual appreciation of Renminbi. The implementation of the Labour Contract Law in mainland China on 1st January, 2008 as well as the shortage of skilful labour in Southern China pushed up the labour wages significantly and limited the flexibility of the production capacity during critically peak seasons.

Despite the general inflationary business environment in both Hong Kong and mainland China, the management succeeded in containing the increase in general expenses. Total expenses to revenue ratio decreased slightly by 0.1% from 15.6% in the first half of 2007 to 15.5% in the corresponding period of 2008. As a result of reduction of gross profit margin by 3.7%, the net profit margin (ratio of profit attributable to the equity holders of the Company to revenue) also decreased by 2.2% from 13.4% to 11.2% in the first six months of 2008.

Original design manufacturing (ODM) division

The slowdown in global economy since the middle of 2007 continued to affect the demand for the products of the core ODM division of the Group. Sales to ODM customers recorded a relatively modest growth rate of 10% from HK$554.5 million in the first six months of 2007 to HK$607.9 million in the period under review. Sales to Europe increased by 18% to HK$411.4 million (2007: HK$350.1 million) whereas sales to the United Stated remained flat at HK$176.7 million (2007: HK$177.4 million). On a geographical basis, sales to Europe, United States, Asia and other regions accounted for 68%, 29%, 2% and 1% respectively of the sales of this division in the first six months of 2008 (2007: 63%, 32%, 3% and 2% respectively). Sales of prescription frames registered a satisfactory growth of 19% to HK$324.2 million in the first half of 2008 (2007: HK$271.3 million) whereas sales of sunglasses only grew by 1% to HK$275.0 million in the same period (2007: HK$273.0 million) as the market demand for sunglasses was generally more sensitive to the economic cycle. Sales of plastic frames, metal frames and spare parts accounted for 52%, 47% and 1% respectively of the sales of this division during the period under review (2007: 54%, 44%, 2% respectively).

Distribution and retailing divisions

For the purposes of optimizing efficiency and maximizing cross-selling opportunities, the Group had merged its two distribution companies under a single umbrella in March 2008. As an incentive to further improve the business performance, the Group had also sold a minority interest to the management team of the distribution division at the time of merger. Sales of the Group's own-branded and licensed branded products increased by 24% to HK$55.9 million in the six months ended 30th June, 2008 (2007: HK$45.0 million). Sales to Europe, Asia, North America and other regions accounted for 52%, 25%, 7% and 16% respectively of the Group's turnover of distribution division in the period under review (2007: 60%, 17%, 12% and 11% respectively). Double-digit sales growth was recorded in all major markets except for North America.

The Group has cut down the total number of retail shops by half by disposing all the 3 shops in Beijing and closing down 1 shop in Shenzhen in the first half of 2008. Turnover of the retailing division decreased by 42% to HK$5.7 million in the first half of 2008 (2007: HK$9.9 million). The Group operated a total of 4 shops in Shenzhen as at 30th June, 2008 (31st December, 2007: 5 shops in Shenzhen and 3 shops in Beijing).

Financial position and liquidity

During the period under review, the Group's operating activities generated a net cash inflow of HK$70.2 million (2007: HK$161.6 million) and the reduction was mainly due to the increase in working capital used (increase of inventory and debtors balances less increase in creditors balance) which amounted to HK$41.0 million whereas a decrease in working capital of HK$38.6 million was recorded in the first six months of 2007. Capital expenditure incurred during the period amounted to HK$59.7 million (2007: HK$77.4 million) and dividend payment of HK$30.7 million was made (2007: HK$26.9 million). The net cash position of the Group (bank and cash balance less bank borrowing) decreased from HK$71.6 million as at 31st December, 2007 to HK$64.7 million as at 30th June, 2008.

The current ratio of the Group as at 30th June, 2008 was 2.2 to 1 (31st December, 2007: 2.1 to 1) with HK$684.4 million of current assets (31st December, 2007: HK$679.1 million) and HK$305.9 million of current liabilities (31st December, 2007: HK$325.2 million). The management continued its efforts of cutting down the delivery lead time for production and inventory turnover period (ratio of inventory balance to cost of sales) decreased slightly to 79 days in the first six months of 2008 from 80 days of the corresponding period of 2007 (or 83 days for the full year of 2007). On the other hand, customers were generally demanding longer credit period under the current sluggish economic environment and debtors turnover period (ratio of the trade debtors to sales) increased from 95 days in the first six months of 2007 (or 98 days for the full year of 2007) to 101 days in the first half of 2008.

The Group had 383,650,000 shares in issue as at both 30th June, 2008 and 31st December, 2007 with an equity attributable to equity holders of the Company amounting to HK$977.4 million and HK$907.9 million as at 30th June, 2008 and 31st December, 2007 respectively. Net asset value per share (equity attributable to equity holders of the Company divided by the total number of shares in issue) as at 30th June, 2008 was HK$2.55 (31st December, 2007: HK$2.37). Total long term liabilities and debt to equity ratio (expressed as a percentage of total long term liabilities over equity attributable to equity holders of the Company) were HK$16.7 million (31st December, 2007: HK$16.6 million) and 1.7% (31st December, 2007: 1.8%) respectively.

The Group had limited exposure to foreign exchange rate fluctuations as most of its transactions were conducted in either United States dollars, Hong Kong dollars and Renminbi and the exchange rates movements between these currencies were relatively stable during the period under review, except to the extent of the gradual continuous appreciation of Renminbi against United States dollars and Hong Kong dollars.

Contingent liabilities

	30.6.2008	31.12.2007
	HK$'000	*HK$'000*
Corporate guarantee to a financial institution in respect of banking facilities granted to a trade debtor	**9,750**	9,750

The directors of the Company consider that the fair values of the financial guarantee contract at its initial recognition and 31st December, 2007 and 30th June, 2008 are insignificant on the basis of short maturity periods and low applicable default rates. The Group has not recognised any deferred income in the condensed consolidated financial statements in relation to the above mentioned guarantee as its fair value is considered not significant.

PROSPECTS

ODM division

The management does not expect any significant rebound in market demand in the American and European markets in the second half of year 2008. Although customers are still cautious in their business expansion and procurement plan, the Group still manages to have a stable order book of three months sales order. The growth in the ODM business in the first half of 2008 suggests that the Group may be gaining market share in the ODM market as the Group has become a strategic vendor of most of the industry leaders which view the Group as a reliable and quality partner in its supply chain.

Distribution and retailing divisions

The performance of the distribution division in the first half of 2008 demonstrated the success of the merger of the two distribution companies of the Group. More marketing resources will be devoted to boost the sales performance of owned and licensed brands through the enlarged network of distributors. Although this division still only accounts for a relatively small portion of the Group's business, it will gradually evolve as the long term growth driver of the Group given its potential sales growth rate as well as higher margin contribution.

After the implementation of the down-sizing exercise of the retailing operations in recent years, the management expects the contribution of its retailing division will continue to remain relatively limited and will keep on evaluating its business value to the Group.

Liquidity and financial management

The management will continue to follow its guiding principles of prudent financial management which is particularly important under the current volatile and uncertain business environment. The Group has raised a HK$50 million five years term loan from its bank for the purposes of capital contribution to its wholly-owned manufacturing subsidiary in Shenzhen in July 2008 and the funds will be used for long term capital expenditure of this subsidiary. As at 12th September, 2008, the Group had a net cash position (bank and cash balance less bank borrowing) of approximately HK$86.3 million.

Summary

The Group is now experiencing the most challenging business environment since the shares of the Company were listed 12 years ago. Despite this, the management believes that the Group's solid financial position and earning capability enable the Group to meet these challenges and seize any new business opportunities.

EMPLOYEE AND REMUNERATION POLICIES

The Group employed approximately 12,500 full time staff in mainland China, Hong Kong and Europe as at 30th June, 2008 (31st December, 2007: 12,000). The Group remunerates its employees based on their performances, experiences, qualifications and prevailing market salaries while performance bonuses are granted on a discretionary basis after considering individual performance and the operating results of the Group. Other employee benefits include insurance and medical cover, subsidised educational and training programmes, provident fund schemes as well as a share option scheme.

CORPORATE GOVERNANCE

The Company has complied with all applicable code provisions set out in the Code on Corporate Governance Practices (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 30th June, 2008 except for deviations from code provision A.2.1 of the CG Code only. Code provision A.2.1 of the CG Code stipulates that the roles of chairman and chief executive officer should be separate and should not be performed by the same individual. Mr. Ng Hoi Ying, Michael ("Mr. Ng") is the founder and Chairman of the Group. The Company does not at present have any officer with the title "chief executive officer" and Mr. Ng has been carrying out the duties of both the chairman and chief executive officer since the establishment of the Group and the Company. The Board intends to maintain this structure in future as it believes that this structure ensures efficient and effective formulation and implementation of business strategies without compromising the balance of power and authority between the Board and the management of the Company.

An Audit Committee has been established by the Company since 1998 to act in an advisory capacity and make recommendations to the Board. The Audit Committee currently comprises Messrs. Wong Chi Wai (chairman of the Audit Committee), Chung Hil Lan Eric and Francis George Martin, all of whom are independent non-executive directors of the Company. The duties of the Audit Committee include review of the interim and annual reports of the Group as well as various auditing, financial reporting and internal control matters with the management and/or external auditors of the Company. The Group's unaudited financial statements for the six months ended 30th June, 2008 have been reviewed by the Audit Committee and the Company's auditor, Messrs. Deloitte Touche Tohmatsu.

A Remuneration Committee has been established by the Company since 2003 and currently comprises Messrs. Francis George Martin (chairman of the Remuneration Committee), Wong Chi Wai and Chung Hil Lan Eric, all of whom are independent non-executive directors of the Company. The duties of the Remuneration Committee include the determination of remuneration of executive directors of the Company and review of remuneration policy of the Group.

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

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed shares during the six months ended 30th June, 2008.

PUBLICATION OF INTERIM REPORT

The 2008 interim report will be despatched to the shareholders of the Company and available on the Company's website at www.artsgroup.com and Hong Kong Exchanges and Clearing Limited's website at www.hkexnews.hk on or about 26th September, 2008.

DIRECTORS

As at the date of this announcement, the Board comprises six directors, three of which are executive directors, namely Mr. Ng Hoi Ying, Michael, Mr. Ng Kim Ying and Mr. Lee Wai Chung, and three are independent non-executive directors, namely Mr. Francis George Martin, Mr. Wong Chi Wai and Mr. Chung Hil Lan Eric.

By Order of the Board
Ng Hoi Ying, Michael
Chairman

Hong Kong, 18th September, 2008

* *For identification purpose only*