



2010

INTERIM REPORT

CHAORYUE GROUP LIMITED

(Incorporated in Bermuda with limited liability)
(Stock Code: 00147)

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CORPORATE INFORMATION

BOARD OF DIRECTORS

Executive Directors

Yuen Leong
Luan Li

Independent Non-Executive Directors

Lam Man Kit, Dominic
Yap Yung
Zhang Guang Sheng

COMPANY SECRETARY

Chung Yau Tong

AUDITOR

Deloitte Touche Tohmatsu

AUDIT COMMITTEE

Yap Yung (*Chairman*)
Lam Man Kit, Dominic
Zhang Guang Sheng

REMUNERATION COMMITTEE

Lam Man Kit, Dominic (*Chairman*)
Yap Yung
Zhang Guang Sheng

NOMINATION COMMITTEE

Zhang Guang Sheng (*Chairman*)
Lam Man Kit, Dominic
Yap Yung

REGISTERED OFFICE

Clarendon House
Church Street
Hamilton HM 11
Bermuda

HEAD OFFICE AND PRINCIPAL PLACE OF BUSINESS IN HONG KONG

Unit 2302, 23rd Floor
China Insurance Group Building
141 Des Voeux Road Central
Hong Kong

PRINCIPAL SHARE REGISTRAR

Butterfield Fulcrum Group (Bermuda) Limited
Rosebank Centre
11 Bermudiana Road
Pembroke, HM 08
Bermuda

HONG KONG BRANCH SHARE REGISTRAR

Tricor Secretaries Limited
26/F, Tesbury Centre
28 Queen's Road East
Hong Kong

STOCK CODE

00147

COMPANY WEBSITE

www.chaoyuehk.com

REPORT ON REVIEW OF INTERIM FINANCIAL INFORMATION



TO THE BOARD OF DIRECTORS OF CHAOYUE GROUP LIMITED

超越集團有限公司

(incorporated in Bermuda with limited liability)

INTRODUCTION

We have reviewed the interim financial information set out on pages 5 to 39 which comprise the condensed consolidated statement of financial position of Chaoyue Group Limited (the “Company”) and its subsidiaries (collectively referred to as the “Group”) as of 30 September 2010 and the related condensed consolidated statement of comprehensive income, statement of changes in equity and statement of cash flows for the six-month period then ended and certain explanatory notes. The Main Board Listing Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of a report on interim financial information to be in compliance with the relevant provisions thereof and Hong Kong Accounting Standard 34 “Interim Financial Reporting” (“HKAS 34”) issued by the Hong Kong Institute of Certified Public Accountants. The directors of the Company are responsible for the preparation and presentation of this interim financial information in accordance with HKAS 34. Our responsibility is to express a conclusion on this interim financial information based on our review, and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

REPORT ON REVIEW OF INTERIM FINANCIAL INFORMATION

(Continued)

SCOPE OF REVIEW

We conducted our review in accordance with the Hong Kong Standard on Review Engagements 2410 “Review of Interim Financial Information Performed by the Independent Auditor of the Entity” issued by the Hong Kong Institute of Certified Public Accountants. A review of interim financial information consists of making enquires, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly we do not express an audit opinion.

CONCLUSION

Based on our review, nothing has come to our attention causes us to believe that the interim financial information is not prepared, in all material respects, in accordance with HKAS 34.

Deloitte Touche Tohmatsu

Certified Public Accountants

Hong Kong

26 November 2010

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the six months ended 30 September 2010

	NOTES	Six months ended 30 September	
		2010 HK\$'000 (<i>unaudited</i>)	2009 HK\$'000 (<i>unaudited</i>) (restated)
Continuing operations			
Revenue	3	15,747	42,173
Cost of sales		(22,981)	(21,469)
Gross (loss) profit		(7,234)	20,704
Other income, gains and losses	4	2,723	5,706
Distribution and selling expenses		(6,143)	(14,223)
Administrative and other expenses		(88,698)	(32,577)
Finance costs	5	(553)	(2,786)
Impairment loss on property, plant and equipment	11	(63,302)	–
Impairment loss on intangible assets	12	(23,516)	(55,094)
Impairment loss on goodwill	13	(27,085)	–
Changes in fair value of derivative financial instruments		–	(4,324,025)
Changes in fair value of derivative warrant liabilities		–	(2,838,197)
Loss before taxation		(213,808)	(7,240,492)
Income tax credit	6	6,456	15,427
Loss for the period from continuing operations	8	(207,352)	(7,225,065)
Discontinued operation			
Loss for the period from discontinued operation	7	–	(57)
Loss for the period		(207,352)	(7,225,122)

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME *(Continued)*

For the six months ended 30 September 2010

		Six months ended 30 September	
		2010	2009
		HK\$'000	HK\$'000
NOTES		(unaudited)	<i>(unaudited)</i> (restated)
Other comprehensive income for the period			
	Exchange differences on translation	(721)	3
	Total comprehensive expense for the period	(208,073)	(7,225,119)
	Loss for the period attributable to:		
	Owners of the Company	(206,372)	(7,225,122)
	Non-controlling interests	(980)	–
		(207,352)	(7,225,122)
	Total comprehensive expense attributable to:		
	Owners of the Company	(207,159)	(7,225,119)
	Non-controlling interests	(914)	–
		(208,073)	(7,225,119)
	Loss per share – Basic and diluted	10	
	From continuing and discontinued operations	HK(1.10) cents	HK(61.69) cents
	From continuing operations	HK(1.10) cents	HK(61.69) cents

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

At 30 September 2010

		30 September	31 March
		2010	2010
		HK\$'000	HK\$'000
	NOTES	(unaudited)	<i>(audited)</i>
NON-CURRENT ASSETS			
Property, plant and equipment	11	23,262	95,491
Intangible assets	12	138,598	173,851
Goodwill	13	–	27,085
Receivables in respect of sales of direct drinking water purification machines	15	–	27,680
		161,860	324,107
CURRENT ASSETS			
Inventories		1,697	1,948
Amounts due from customers for contract work		17,197	11,296
Trade and other receivables	15	11,117	51,274
Bank balances and cash		69,627	83,618
		99,638	148,136
CURRENT LIABILITIES			
Amounts due to customers for contract work		2,290	2,249
Trade and other payables	16	52,228	46,756
Amount due to a director of a subsidiary	17	23,806	23,464
Tax payable		2,700	2,769
Borrowings	18	9,265	9,099
Warranty provision		1,771	1,281
Deferred income		7,101	7,238
		99,161	92,856

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION *(Continued)*

At 30 September 2010

	NOTES	30 September 2010 HK\$'000 <i>(unaudited)</i>	31 March 2010 HK\$'000 <i>(audited)</i>
NET CURRENT ASSETS		477	55,280
TOTAL ASSETS LESS CURRENT LIABILITIES		162,337	379,387
NON-CURRENT LIABILITIES			
Deferred income		20,798	23,852
Deferred taxation		–	6,750
		20,798	30,602
		141,539	348,785
CAPITAL AND RESERVES			
Share capital	20	18,824	18,824
Reserves		117,743	324,075
Equity attributable to owners of the Company		136,567	342,899
Non-controlling interests		4,972	5,886
		141,539	348,785

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the six months ended 30 September 2010

	Attributable to owners of the Company										
	Share capital	Non-voting convertible preference	Share premium	Contributed surplus	Capital redemption reserve	Share option reserve	Translation reserve	Accumulated losses	Total	Non-controlling interests	Total
		shares			reserve	reserve					
HK\$'000	HK\$'000 (Note i)	HK\$'000	HK\$'000	HK\$'000 (Note ii)	HK\$'000 (Note iii)	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	
At 1 April 2009 (audited)	3,370	41,170	23,685	51,655	3,781	13,900	12	(65,105)	72,468	-	72,468
Exchange difference arising on translation of foreign operations	-	-	-	-	-	-	3	-	3	-	3
Loss for the period	-	-	-	-	-	-	-	(7,225,122)	(7,225,122)	-	(7,225,122)
Total comprehensive expense for the period	-	-	-	-	-	-	3	(7,225,122)	(7,225,119)	-	(7,225,119)
Conversion of convertible bonds into ordinary shares	12,300	-	3,639,200	-	-	-	-	-	3,651,500	-	3,651,500
Shares issued on exercise of share options	6	-	4,407	-	-	(1,221)	-	-	3,192	-	3,192
Exercise of warrants	2,075	-	2,529,463	-	-	-	-	-	2,531,538	-	2,531,538
Share-based payments	-	-	-	-	-	3,016	-	-	3,016	-	3,016
Share options lapsed	-	-	-	-	-	(1,758)	-	1,758	-	-	-
At 30 September 2009 (unaudited)	17,751	41,170	6,196,755	51,655	3,781	13,937	15	(7,288,469)	(963,405)	-	(963,405)
At 1 April 2010 (audited)	18,824	41,170	7,382,924	51,655	3,781	15,330	426	(7,171,211)	342,899	5,886	348,785
Exchange difference arising on translation of foreign operations	-	-	-	-	-	-	(787)	-	(787)	66	(721)
Loss for the period	-	-	-	-	-	-	-	(206,372)	(206,372)	(980)	(207,352)
Total comprehensive expense for the period	-	-	-	-	-	-	(787)	(206,372)	(207,159)	(914)	(208,073)
Share-based payments	-	-	-	-	-	827	-	-	827	-	827
At 30 September 2010 (unaudited)	18,824	41,170	7,382,924	51,655	3,781	16,157	(361)	(7,377,583)	136,567	4,972	141,539

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY *(Continued)*

For the six months ended 30 September 2010

Notes:

- (i) The non-voting convertible preference shares represent the consideration for acquisition of 100% equity interests in Park Wealth International Limited and its subsidiaries (the "Park Wealth Group"). For details, please refer to note 19.
- (ii) The capital redemption reserve represents amounts transferred from contributed surplus upon the repurchase of the Company's shares.
- (iii) The share option reserve represents the reserve recognised as a result of the grant of share options of the Company to certain directors and employees of the Group.

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

For the six months ended 30 September 2010

	Six months ended 30 September	
	2010 HK\$'000 (<i>unaudited</i>)	2009 HK\$'000 (<i>unaudited</i>) (restated)
OPERATING ACTIVITIES		
Loss before taxation	(213,808)	(7,240,549)
Adjustments for:		
Depreciation of property, plant and equipment	10,088	7,686
Amortisation of intangible assets	9,802	9,400
Impairment loss on property, plant and equipment	63,302	–
Impairment loss on goodwill	27,085	–
Impairment loss on intangible assets	23,516	55,094
Allowance on bad and doubtful debts	39,813	1,784
Impairment loss on advances to suppliers	12,338	–
Bank interest income	(92)	(114)
Finance costs	553	2,786
Share-based payment expenses	827	3,016
Gain loss on disposal of property, plant and equipment	–	(1,733)
Changes in fair value of derivative financial instruments	–	4,324,025
Changes in fair value of derivative warrant liabilities	–	2,838,197
Other non-cash-items	491	390
Operating cash flows before movements in working capital	(26,085)	(18)
Decrease (increase) in inventories	251	(1,675)
Increase in amounts due from customers for contract work	(5,901)	(2,727)
Increase in receivables in respect of sales of direct drinking water purification machines	–	(9,275)
Decrease in trade and other receivables	15,686	15,623
Increase (decrease) in amounts due to customers for contract work	41	(948)
Increase (decrease) in trade and other payables	6,183	(175)
Increase in deferred income	(3,714)	(8,979)
Other operating cash flows	(294)	(3,041)
NET CASH USED IN OPERATING ACTIVITIES	(13,833)	(11,215)

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS *(Continued)*

For the six months ended 30 September 2010

	Six months ended 30 September	
	2010	2009
	HK\$'000	HK\$'000
	(unaudited)	<i>(unaudited)</i> (restated)
INVESTING ACTIVITIES		
Purchases of property, plant and equipment	(267)	(27,206)
Proceeds from disposal of property, plant and equipment	10	–
Interest received	92	114
NET CASH USED IN INVESTING ACTIVITIES	(165)	(27,092)
FINANCING ACTIVITIES		
Proceeds from issue of new shares upon exercise of warrants	–	31,125
Proceeds from issue of new shares upon exercise of share options	–	3,192
Repayment to a director of a subsidiary	–	(1,760)
NET CASH FROM FINANCING ACTIVITIES	–	32,557
NET DECREASE IN CASH AND CASH EQUIVALENTS	(13,998)	(5,750)
CASH AND CASH EQUIVALENTS AT BEGINNING OF THE PERIOD	83,618	147,142
Effect of Foreign Exchange Rate Changes	7	9
CASH AND CASH EQUIVALENTS AT END OF THE PERIOD represented by bank balances and cash	69,627	141,401

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended 30 September 2010

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 and with the Hong Kong Accounting Standard (“HKAS”) 34 “Interim Financial Reporting” issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”).

The functional currency of the Company is Renminbi (“RMB”) as the Group’s operation is mainly in the People’s Republic of China (the “PRC”). The condensed consolidated financial statements are presented in Hong Kong Dollars (“HKD”). The directors consider that HKD is the appropriate presentation currency as the management of the Company controls and monitors the performance and financial position of the Group by using HKD.

2. SIGNIFICANT ACCOUNTING POLICIES

The condensed consolidated financial statements have been prepared on the historical cost convention, except for certain financial instruments, which are measured at fair values, as appropriate.

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 31 March 2010, except for as below.

In the current interim period, the Group has applied, for the first time, a number of new and revised standards, amendments and interpretations (“new and revised HKFRSs”) issued by the HKICPA.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

The Group applies HKFRS 3 (Revised) *Business Combinations* prospectively to business combinations for which the acquisition date is on or after 1 April 2010. The requirements in HKAS 27 (Revised) *Consolidated and Separate Financial Statements* in relation to accounting for changes in ownership interests in a subsidiary after control is obtained and for loss of control of a subsidiary are also applied prospectively by the Group on or after 1 April 2010.

As there was no transaction during the current interim period in which HKFRS 3 (Revised) and HKAS 27 (Revised) are applicable, the application of HKFRS 3 (Revised), HKAS 27 (Revised) and the consequential amendments to other HKFRSs had no impact on the condensed consolidated financial statements of the Group for the current or prior accounting periods.

Results of the Group in future periods may be affected by future transactions for which HKFRS 3 (Revised), HKAS 27 (Revised) and the consequential amendments to the other HKFRSs are applicable.

The application of the other new and revised HKFRSs had no material effect on the condensed consolidated financial statements of the Group for the current or prior accounting periods.

The Group has not early applied the new and revised standards, amendments or interpretations that have been issued but are not yet effective. The directors of the Company anticipate that the application of those new and revised standards, amendments or interpretations will have no material impact on the results and the financial position of the Group.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

For the six months ended 30 September 2010

3. REVENUE AND SEGMENT INFORMATION

An analysis of the Group's revenue for the period is as follows:

	Six months ended 30 September	
	2010 HK\$'000 (unaudited)	2009 HK\$'000 (unaudited)
Continuing operations		
Sale of goods	2,906	11,987
Contract revenue	8,242	5,774
Rental income	3,750	24,027
Royalty fee income	849	385
	15,747	42,173

The Group's operating segments, based on information reported to the chief operating decision maker for the purposes of revenue allocation and performance assessment, are as follows:

Continuing operations

- Direct drinking water – Lease of direct drinking water purification machines and royalty income for use of the Group's brand name
- Purification equipment – Manufacturing and sales of air purification and water purification equipments
- Environmental engineering – Construction and installation of air purification and sewage treatment system
- Mining – Exploration of gold and copper

Discontinued operation

- Garment – The Group was involved in manufacturing and sales of garment business, which was reported as a separate segment under HKAS 14 Segment Reporting in previous period. This operation was discontinued with effect from July 2009 (note 7).

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

3. REVENUE AND SEGMENT INFORMATION (Continued)

Segment results represent the results from each segment without allocation of central administration costs and directors' salaries, some items of other income, finance costs, changes in fair value of derivative financial instruments, changes in fair value of derivative warrant liabilities. This is the measure reported to the chief operation decision maker for the purposes of resource allocation and performance assessment.

The following is an analysis of the Group's revenue and results by operating segments for the period under review:

Six months ended 30 September 2010

	Continuing operations					
	Direct drinking water	Purification equipment	Environmental engineering	Mining	Elimination	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
REVENUE						
External sales	4,599	2,906	8,242	-	-	15,747
RESULT						
Segment loss	(177,937)	(3,971)	(363)	(13,128)	-	(195,399)
Unallocated income						92
Unallocated corporate expenses						(17,948)
Finance costs						(553)
Loss before taxation						(213,808)
<i>Amounts included in the measure of segment loss:</i>						
Allowance on bad and doubtful debts	39,153	-	660	-	-	39,813
Impairment loss on advances to suppliers	12,338	-	-	-	-	12,338
Amortisation on intangible assets	3,484	-	-	6,318	-	9,802
Impairment loss on property, plant and equipment	63,302	-	-	-	-	63,302
Impairment loss on intangible assets	23,516	-	-	-	-	23,516
Impairment loss on goodwill	27,085	-	-	-	-	27,085

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

3. REVENUE AND SEGMENT INFORMATION (Continued)

Six months ended 30 September 2009

	Continuing operations					
	Direct drinking water HK\$'000	Purification equipment HK\$'000	Environmental engineering HK\$'000	Mining HK\$'000	Elimination HK\$'000	Total HK\$'000
REVENUE						
External sales	24,412	11,987	5,774	-	-	42,173
Inter-segment sales	-	18,945	-	-	(18,945)	-
Total	24,412	30,932	5,774	-	(18,945)	42,173
RESULT						
Segment profit (loss)	(51,942)	(2,643)	(1)	-	171	(54,415)
Unallocated income						114
Unallocated corporate expenses						(21,183)
Finance costs						(2,786)
Changes in fair value of derivative financial instruments						(4,324,025)
Changes in fair value of derivative warrant liabilities						(2,838,197)
Loss before taxation						(7,240,492)
<i>Amounts included in the measure of segment profit (loss):</i>						
Allowance on bad and doubtful debts	1,784	-	-	-	-	1,784
Amortisation on intangible assets	9,400	-	-	-	-	9,400
Impairment loss on intangible assets	55,094	-	-	-	-	55,094

Note: Inter-segment sales are charged at terms agreed by both parties.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

For the six months ended 30 September 2010

3. REVENUE AND SEGMENT INFORMATION *(Continued)*

The following is an analysis of the Group's assets by operating segment:

	30 September 2010 HK\$'000 (unaudited)	31 March 2010 HK\$'000 (audited)
ASSETS		
<i>Segment assets</i>		
Direct drinking water	21,227	152,874
Purification equipment	10,632	56,861
Environmental engineering	18,038	25,811
Mining	138,598	146,851
Total segment assets	188,495	382,397
<i>Unallocated assets</i>		
– Bank balance and cash	69,627	83,618
– Others	3,376	6,228
Total unallocated assets	73,003	89,846
Consolidated total assets	261,498	472,243

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

For the six months ended 30 September 2010

4. OTHER INCOME, GAINS AND LOSSES

	Six months ended	
	30 September	
	2010	2009
	HK\$'000	HK\$'000
	<i>(unaudited)</i>	<i>(unaudited)</i>
Continuing operations		
Bank interest income	92	114
Gain on disposal of property, plant and equipment <i>(Note)</i>	–	1,733
Sale of scrap materials	2,514	2,310
Others	117	1,549
	2,723	5,706

Note: During the six months ended 30 September 2009, the Group disposed of certain direct drinking water purification machines, which were leased out under operating leases and classified under property, plant and equipment, with carrying amount of approximately HK\$26,874,000 at a consideration of approximately HK\$26,874,000, payable by interest free installments over a period of five years. The present value of the consideration receivable as at 30 September 2009, net of related tax payable, amounted to approximately HK\$20,058,000. Upon the disposal, deferred income amounting to approximately HK\$8,549,000 which represents rental received in advance for the drinking water purification machine from the existing lessees has been released to profit and loss and forms part of the gain on disposal of the assets.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

5. FINANCE COSTS

	Six months ended 30 September	
	2010	2009
	HK\$'000	HK\$'000
	(unaudited)	<i>(unaudited)</i>
Continuing operations		
Interests on convertible bonds	–	2,241
Interest on borrowing wholly repayable within five years	553	545
	553	2,786

6. INCOME TAX CREDIT

	Six months ended 30 September	
	2010	2009
	HK\$'000	HK\$'000
	(unaudited)	<i>(unaudited)</i>
		<i>(restated)</i>
Continuing operations		
Current tax – PRC Enterprise Income Tax	294	696
Deferred taxation	(6,750)	(16,123)
	(6,456)	(15,427)

No provision for Hong Kong Profits Tax has been made for both periods as the Group has no assessable profit arising in Hong Kong.

The income tax expense is recognised based on management best estimate of the weighted average annual income tax rate expected for full financial year.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

For the six months ended 30 September 2010

6. INCOME TAX CREDIT *(Continued)*

The Group's PRC subsidiary, Shanghai Comfort Environment and Science Company Limited ("Shanghai Comfort"), which is registered in Shanghai Pudong New Area and regarded as advanced technology enterprises by local tax bureau. Shanghai Comfort is entitled to the PRC income tax at concessionary rate of 15% from year 2008 to 2010.

The deferred tax credit arises as a result of the amortisation and impairment loss recognised on intangible assets of the Group.

7. DISCONTINUED OPERATION

Due to the continuous adverse operating environment as a result of the economic downturn since the second half of year 2008, the Group had encountered significant difficulties in obtaining orders from customers for its garment business. In light of this, the management had resolved to abandon the garment business of the Group and hence had ceased to accept any new garment trading business and have laid off all of the staffs within the garment business in July 2009. As the amount of assets employed in the garment business was not significant, the management did not consider the discontinuation of the garment business would have any material impact on the Group's financial result.

The results of the garment business, which were included in the condensed consolidated statement of comprehensive income, is as follow:

	Six months ended 30 September 2009 HK\$'000 <i>(unaudited)</i>
Other income	98
Administrative and other expenses	(155)
Loss for the period	(57)

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

For the six months ended 30 September 2010

8. LOSS FOR THE PERIOD

Loss for the period has been arrived at after charging:

	Six months ended	
	30 September	
	2010	2009
	HK\$'000	HK\$'000
	(unaudited)	(unaudited)
		(restated)
Continuing operations		
Directors' emoluments	906	662
Other staff costs	5,580	10,293
Share-based payment	827	3,016
Other staff retirement benefit scheme contributions	557	1,293
Total staff costs	7,870	15,264
Cost of inventories recognised as expenses	15,087	14,863
Depreciation of property, plant and equipment	10,088	7,686
Amortisation of intangible assets included in administrative and other expenses	9,802	9,400
Allowance on bad and doubtful debts included in administrative and other expenses <i>(Note 15)</i>	39,813	1,784
Impairment loss on advances to suppliers included in administrative and other expenses <i>(Note 15)</i>	12,338	–

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

For the six months ended 30 September 2010

9. DIVIDENDS

No dividends were paid, declared or proposed during the reported period. The directors do not recommend the payment of an interim dividend.

10. LOSS PER SHARE

From continuing and discontinued operations

The calculation of the basic and diluted loss per share for the period attributable to the owners of the Company is based on the following data:

	Six months ended 30 September	
	2010	2009
	HK\$'000	HK\$'000
	(unaudited)	<i>(unaudited)</i> <i>(restated)</i>
Loss		
Loss for the period attributable to owners of the Company for the purpose of loss per share	(206,372)	(7,225,122)

	Six months ended 30 September	
	2010	2009
Number of shares		
Weighted average number of shares for the purpose of loss per share	18,824,435,160	11,711,069,723 <i>(Note)</i>

Note: The weighted average number of ordinary shares for the purpose of loss per share has been restated to include adjustment for the subdivision during the six months ended 30 September 2009.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

10. LOSS PER SHARE (Continued)

From continuing operations

The calculation of the basic and diluted loss per share for the period from continuing operations attributable to the owners of the Company is based on the following data:

	Six months ended 30 September	
	2010 HK\$'000 (unaudited)	2009 HK\$'000 (unaudited)
Loss		
Loss for the period attributable to owners of the Company	(206,372)	(7,225,122)
Less: Loss for the period from discontinued operation	-	(57)
Loss for the purposes of loss per share from continuing operations	(206,372)	(7,225,065)

The denominators used are the same as those detailed above for loss per share from continuing and discontinued operations.

From discontinued operation

Basic and diluted loss per share from discontinued operation for the period ended 30 September 2009 is approximately HK0.0005 cents per share, based on the loss for the period from discontinued operation of approximately HK\$57,000, and the denominators detailed above for loss per share from continuing and discontinued operations.

The computation of diluted loss per share for the period ended 30 September 2010 and 2009 does not take into account the effect of share options granted, convertible preference shares and the warrants issued by the Company as these would result in a decrease in loss per share.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

11. PROPERTY, PLANT AND EQUIPMENT

The movements in property, plant and equipment during the period is summarised as follows:

	HK\$'000
Carrying amounts as at 1 April 2010 (audited)	95,491
Additions	267
Depreciation	(10,088)
Disposal	(10)
Impairment loss recognised (Note)	(63,302)
Exchange adjustments	904
Carrying amounts as at 30 September 2010 (unaudited)	23,262

Note: Details of the impairment testing are set out in note 14.

12. INTANGIBLE ASSETS

The movements in intangible assets during the period is summarised as follows:

	Patents	Mining licence	Total
	HK\$'000	HK\$'000	HK\$'000
	(Note a)	(Note b)	
Carrying amounts as at 1 April			
2010 (audited)	27,000	146,851	173,851
Amortisation	(3,484)	(6,318)	(9,802)
Impairment loss recognised	(23,516)	–	(23,516)
Exchange adjustments	–	(1,935)	(1,935)
Carrying amounts as at 30 September			
2010 (unaudited)	–	138,598	138,598

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

For the six months ended 30 September 2010

12. INTANGIBLE ASSETS *(Continued)*

Notes:

- a. The patents arise on acquisition of Park Wealth Group in relation to the design and production of direct drinking water purification machines which have finite useful lives. Such patents are amortised on a straight-line basis over the estimated useful life of approximately five years.

Details of impairment testing are set out in note 14.

- b. The mining licence represents exploration and evaluation assets which arose on acquisition of Eagle Mountain Holdings Limited and its subsidiaries (the "Eagle Mountain Group") in November 2009. At subsequent reporting periods, mining licence is measured using the cost model subject to impairment.

The mining licence cost is amortised on a straight line method until the end of the terms of the mining rights in 2021 if no mining activity is carried out. During the period, the mine was not operated and accordingly, amortisation on the mining rights was amortised under straight line method. Such mining licence will be transferred to mining rights, another sub-category of intangible assets, when the technical feasibility and commercial viability of extracting the mineral resources in the mine are demonstrated. On the other hand, when it is established that the mining is not economically viable, the net carrying amount of the mining licence will be written off. Amortisation is provided to write off the cost of the mining rights using the units of production method based on the proven and probable mineral reserves under the assumption that the Group can renew the mining rights till all proven and probable mineral reserves have been depleted if the mining activity is carried out.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

13. GOODWILL

	HK\$'000
<hr/>	
COST	
At 1 April 2010 (audited)	27,085
Impairment loss recognised	(27,085)
<hr/>	
At 30 September 2010 (unaudited)	–
<hr/>	

During the six months ended 30 September 2010, the Group recognised an impairment loss of HK\$27,085,000 in relation on goodwill arising on acquisition of the Park Wealth Group. Details of impairment testing are set out in note 14.

14. IMPAIRMENT TESTING ON DIRECT DRINKING WATER BUSINESS

At 30 September 2010, the directors determined that the direct drinking water purification machines included in the Group's property, plant and equipment, which relates to the direct water business ("Direct Drinking Water Unit") was impaired such that an impairment loss of approximately HK\$63,302,000 has been recognised. The impairment loss is attributable to the reduction in the expected revenue of Direct Drinking Water Unit as the actual revenue did not turn out as previously expected. The recoverable amounts of the direct drinking water purification machines have been determined on the basis of their value in use. The discount rate in measuring the amount of value in use was 23.5%.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

For the six months ended 30 September 2010

14. IMPAIRMENT TESTING ON DIRECT DRINKING WATER BUSINESS *(Continued)*

In addition to above, at 30 September 2010, management appointed an independent valuer, BMI Appraisals Limited, to perform a business valuation on the Direct Drinking Water Unit. The recoverable amount of the Direct Drinking Water Unit has been determined based on a value in use calculation. That calculation uses estimation of the cash flow projections based on financial budgets approved by management covering a 4-year period and a discount rate of 23.5%. Another key assumption for the value in use calculations is the budgeted gross margin, which is determined based on the cash generating unit (“CGU”) past performance and management’s expectations for the market development. The carrying amount of goodwill and patents as at 30 September 2010 allocated to this CGU is determined to be fully impaired with reference to the above valuation and the decrease was as a result of the reduction in the expected revenue of the Direct Drinking Water Unit since the actual revenue did not turn out as previously expected.

The impairment losses recognised during the period to reduce the carrying amounts of each class of assets to their recoverable amounts are as follows:

	HK\$'000
Direct drinking water purification machines	63,302
Goodwill	27,085
Patents	23,516
	113,903

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

For the six months ended 30 September 2010

15. TRADE AND OTHER RECEIVABLES

	30 September 2010 HK\$'000 (unaudited)	31 March 2010 HK\$'000 (audited)
Trade receivables	8,170	14,312
Advances to suppliers <i>(Note a)</i>	2,027	21,637
Other receivables	307	1,180
Receivables in respect of sales of direct drinking water purification machines <i>(Note b)</i>	–	39,761
Prepayments and deposits	613	2,064
	11,117	78,954
Analysis of trade and other receivables for reporting purposes as:		
– Non-current asset in respect of sales of direct drinking water purification machines	–	27,680
– Current asset	11,117	51,274
	11,117	78,954

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

15. TRADE AND OTHER RECEIVABLES (Continued)

Notes:

- a. During the year ended 31 March 2010, the Group has paid deposits to certain suppliers for purchasing raw materials.

During the six months ended 30 September 2010, the Group did not receive the raw materials on the agreed schedule from certain suppliers. The directors of the Company consider the recoverability of the aforesaid advances are doubtful and accordingly the Group has made impairment loss amounting to HK\$12,338,000 during this interim period.

- b. During the year ended 31 March 2010, the Group sold direct drinking water purification machines to certain independent third parties. The consideration was payable in interest free instalments over a period of five years.

During the six months ended 30 September 2010, the purchasers of the direct drinking water purification machines defaulted in payment of the instalments. The directors of the Company consider the recoverability of the aforesaid receivables are doubtful and accordingly the Group has made full impairment loss amounting to HK\$39,153,000 during this interim period.

Other than cash sales, the Group generally allows an average credit period of 30 days to 180 days to its trade customers.

The following is an aged analysis of trade receivables of the Group net of allowance for doubtful debts presented based on invoice date at the end of the reporting period:

	30 September 2010 HK\$'000 (unaudited)	31 March 2010 HK\$'000 (audited)
0 to 30 days	3,902	11,496
31 to 90 days	2,452	1,970
91 to 180 days	1,816	6,658
181 to 365 days	-	7,415
Over 1 year	-	285
	8,170	27,824

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

16. TRADE AND OTHER PAYABLES

	30 September 2010 HK\$'000 (unaudited)	31 March 2010 HK\$'000 (audited)
Trade payables	14,793	10,265
Bills payable	112	154
Other payables	7,269	7,348
Other tax payables	16,494	17,018
Receipt in advance from customers	7,859	8,250
Accruals	5,701	3,721
	52,228	46,756

Trade payables principally comprise amounts outstanding for purchase of raw materials and ongoing expenses. The average credit period for purchase of raw materials ranged from 30 days to 180 days.

The following is an aged analysis of trade payables and bills payable presented based on invoice date:

	30 September 2010 HK\$'000 (unaudited)	31 March 2010 HK\$'000 (audited)
0 – 30 days	112	4,858
31 – 90 days	3,472	3,154
91 – 180 days	6,778	1,405
181 – 365 days	3,551	708
Over 1 year	992	294
	14,905	10,419

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

17. AMOUNT DUE TO A DIRECTOR OF A SUBSIDIARY

	30 September 2010 HK\$'000 (unaudited)	31 March 2010 HK\$'000 (audited)
Xiao Shu (肖述)	23,806	23,464

Xiao Shu is a director and former shareholder of a subsidiary of the Company.

The amount represents the advance which is non-trade nature.

The amount is interest free, unsecured and repayable on demand.

18. BORROWINGS

As at 30 September 2010, the amounts represent unsecured fixed-rate loans with interest at 12% per annum from an independent third party with maturity period not exceeding one year.

19. NON-VOTING CONVERTIBLE PREFERENCE SHARES

In July 2010, the consideration for the acquisition of the Park Wealth Group and the aggregate fair value of the convertible preference shares was finalised to be HK\$41,170,000, which was satisfied by the issuance of an aggregate of 214,637,160 convertible preference shares with a par value of HK\$0.001 each (after adjustment for share subdivision) which can be converted into the Company's ordinary shares without maturity date. The convertible preference shares shall at all times rank equally among themselves and pari passu with all other ordinary shares of the Company in issue with respect of the right to any dividends or distributions declared.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

For the six months ended 30 September 2010

19. NON-VOTING CONVERTIBLE PREFERENCE SHARES *(Continued)*

In the event of liquidation or dissolution or winding up, or merger, or reorganisation that will result in any distribution of assets of the Company to the existing shareholders of the Company, the holders of the convertible preference shares will receive an amount equal to 100% of the face value of the convertible preference shares. In addition, the ranking of the convertible preference shares is higher than ordinary shares, but lower than creditor in case of liquidation.

The holder of each convertible preference shares shall not have any voting rights. The convertible preference shares shall be non-redeemable and will not be listed on any stock exchange.

The holders of the convertible preference shares shall be entitled to convert the convertible preference shares into ordinary shares in the following manner:

- (i) Up to 40% of the convertible preference shares anytime during the period commencing from the first business day following the second anniversary of the date of completion of the agreement until the third anniversary of the date of completion of the agreement;
- (ii) Up to 70% of the convertible preference shares anytime during the period commencing from the first business day following the third anniversary of the date of completion of the agreement until the fourth anniversary of the completion of the agreement;
- (iii) All the remaining convertible preference shares anytime after the first business day following the fourth anniversary of the date of completion of the agreement.

The holder of the convertible preference shares shall not exercise the conversion rights and the Company shall not issue any shares if, upon such conversion and/or issue, (i) the holder of the convertible preference shares and the parties acting in concert with it, will be interested in 30% (or such amount as may from time to time be specified in the Hong Kong Code on Takeovers and Mergers as being the level for triggering a mandatory general offer) or more of the then enlarged issued ordinary share capital of the Company on the relevant conversion date, or (ii) the shareholding in the Company held by the public will be less than 25% or the minimum prescribed percentage as set out in the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong (the "Listing Rules") from time to time.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

20. SHARE CAPITAL

	Number of shares	Amount HK\$'000
Authorised:		
Ordinary shares of HK\$0.001 each		
At 1 April 2010 and 30 September 2010	498,000,000,000	498,000
Non-voting convertible preference shares of HK\$0.001 each		
At 1 April 2010 and 30 September 2010	2,000,000,000	2,000
Issued and fully paid:		
Ordinary shares of HK\$0.001 each		
At 1 April 2010 and 30 September 2010	18,824,435,160	18,824
Non-voting convertible preference shares of HK\$0.001 each (Note 19)		
At 1 April 2010 and 30 September 2010	214,637,160	41,170

21. SHARE OPTION SCHEME

The Company's share option scheme (the "Scheme") was adopted on 17 September 2004 pursuant to a resolution passed by the Company's shareholders on 17 September 2004 for the primary purposes of providing incentives to any directors or full-time employees of the Company or any of its subsidiaries ("Eligible Employees") and will expire on 16 September 2014. Under the Scheme, the Board of Directors of the Company is authorised to grant options at a consideration of HK\$1 per option to the Eligible Employees to subscribe for shares in the Company.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

For the six months ended 30 September 2010

21. SHARE OPTION SCHEME *(Continued)*

The maximum number of shares issued or which may be issuable under the Scheme cannot exceed 10% of the issued share capital of the Company excluding any shares issued pursuant to the Scheme at the date of adoption. The number of shares in respect of which options granted and may be granted to any Eligible Employee is not permitted to exceed 30% of the aggregate number of shares for the time being issued and issuable under the Scheme.

The offer of a grant of share options may be accepted within 21 days from the date of the offer together with the payment of nominal consideration of HK\$1 per option by the grantee.

The exercisable period of an option is determined by the directors at their discretion. The expiry date of the option may be determined by the Board of Directors of the Company which shall not be later than the expiry day of the Scheme.

The exercise price is determined by the directors of the Company, and will not be less than the greater of: (i) the closing price of the Company on the offer date; (ii) the average of the closing price of the Company's shares for the 5 trading days immediately preceding the offer of the options and (iii) the nominal value per share of the Company.

On 31 July 2009, a special resolution was passed by the shareholders of the Company to approve the subdivision of the issued and unissued ordinary shares and convertible preference shares into 10 subdivided ordinary shares and 10 subdivided convertible preference shares of HK\$0.001 each respectively. Pursuant to the terms and conditions of the Scheme and the requirements of Chapter 17 of the Listing Rules, the exercise price of the share options granted under the Scheme would be adjusted from HK\$5.32 per ordinary share to HK\$0.532 per subdivided share while the number of shares of the Company to be allotted and issued upon exercise of the subscription rights attaching to the share options would be adjusted from 8,400,000 ordinary shares to 84,000,000 subdivided ordinary shares as a result of the share subdivision. The total number of shares to be issued upon the exercise of all options granted under the Scheme is 66,000,000 as at 30 September 2010.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

21. SHARE OPTION SCHEME (Continued)

Details of the share options granted, exercised, and lapsed under the Scheme during the period ended 30 September 2010 and 2009 are as follows:

Category of Grantee	Date of grant	Exercise price		Vesting period	At	Granted	Exercised	Lapsed	At
		per share	Exercisable period		1 April 2010	during the period	during the period	during the period	30 September 2010
Directors	17 July 2008	HK\$0.532	7/17/2008 – 9/16/2014	N/A	6,000,000	-	-	-	6,000,000
			7/17/2009 – 9/16/2014	7/17/2008 – 7/16/2009	6,000,000	-	-	-	6,000,000
			7/17/2010 – 9/16/2014	7/17/2008 – 7/16/2010	6,000,000	-	-	-	6,000,000
					18,000,000	-	-	-	18,000,000
Employees	17 July 2008	HK\$0.532	7/17/2008 – 9/16/2014	N/A	15,999,980	-	-	-	15,999,980
			7/17/2009 – 9/16/2014	7/17/2008 – 7/16/2009	16,000,010	-	-	-	16,000,010
			7/17/2010 – 9/16/2014	7/17/2008 – 7/16/2010	16,000,010	-	-	-	16,000,010
					48,000,000	-	-	-	48,000,000
Exercisable at the end of the period									66,000,000
Weighted average share price at date of exercise									N/A

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

21. SHARE OPTION SCHEME (Continued)

Category of Grantee	Date of grant	Exercise price per share	Exercisable period	Vesting period	At 1 April 2009	Granted during the period	Exercised during the period	Lapsed during the period	At 30 September 2009
Directors	17 July 2008	HK\$0.532	7/17/2008 – 9/16/2014	N/A	12,000,000	-	(3,000,000)	(3,000,000)	6,000,000
			7/17/2009 – 9/16/2014	7/17/2008 – 7/16/2009	12,000,000	-	(3,000,000)	(3,000,000)	6,000,000
			7/17/2010 – 9/16/2014	7/17/2008 – 7/16/2010	12,000,000	-	-	(6,000,000)	6,000,000
					36,000,000	-	(6,000,000)	(12,000,000)	18,000,000
Employees	17 July 2008	HK\$0.532	7/17/2008 – 9/16/2014	N/A	15,999,980	-	-	-	15,999,980
			7/17/2009 – 9/16/2014	7/17/2008 – 7/16/2009	16,000,010	-	-	-	16,000,010
			7/17/2010 – 9/16/2014	7/17/2008 – 7/16/2010	16,000,010	-	-	-	16,000,010
					48,000,000	-	-	-	48,000,000
Exercisable at the end of the period									43,999,990
Weighted average share price at date of exercise									1.22

The Group recognised a total share-based compensation expense of HK\$827,000 for the period ended 30 September 2010 (period ended 30 September 2009: HK\$3,016,000) in relation to share options granted by the Company.

Note: The exercise price were adjusted for the share subdivision made during the six months ended 30 September 2009.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

22. RELATED PARTY TRANSACTIONS

The Group has the following transactions with related parties during the period:

Compensation of key management personnel

The remuneration of key management during the period was as follows:

	Six months ended 30 September	
	2010 HK\$'000 (Unaudited)	2009 HK\$'000 (Unaudited)
Short-term benefits (including share option expenses)	1,739	4,527
Retirement benefits scheme contribution	12	38
	1,751	4,565

The remuneration of key management is determined having regard to the performance of individuals and market trends.

23. COMPARATIVES

During the preparation of the annual consolidated financial statements of the Company for the year ended 31 March 2010 dated 16 July 2010, the Group has stated the embedded derivatives of the convertible bonds at fair value at 14 May 2009 and 29 June 2009, the dates of their conversion, which were arrived at with reference to the fair value of the ordinary shares and warrants issued at the respective dates of conversion of the convertible bonds. Accordingly, the comparative figures in the condensed consolidated financial statements in respect of the six months period ended 30 September 2009 have been restated to reflect the fair value of the embedded derivatives of the convertible bonds at these respective dates of conversion.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended 30 September 2010

23. COMPARATIVES (Continued)

The impacts on the condensed consolidated statement of comprehensive income for the six months ended 30 September 2009 are as follows:

Consolidated statement of comprehensive income

	Six months ended 30 September 2009 HK\$'000
Increase in change in fair value of derivative financial instruments	(4,333,902)
Decrease in loss on initial recognition of derivative warrant liabilities	829,204
Increase in impairment loss and amortisation of intangible assets, net of related deferred tax credit (Note)	(13,711)
Increase in loss for the period	(3,518,409)

Note: In February 2009, the Group acquired Park Wealth Group in which the consideration for this acquisition was settled by the Company by the allotment and issuance of non-voting convertible preference shares. The number of convertible preference shares to be issued was based on the audited profit of Park Wealth Group for the year ended 31 December 2009. In the consolidated financial statements of the Group for the year ended 31 March 2009, the estimated number and fair value, of convertible preference shares to be issued and the fair value of the assets and liabilities of Park Wealth Group acquired were determined on a provisional basis.

Subsequently during the year ended 31 March 2010, the management completed the accounting for the acquisition of Park Wealth Group and finalised the cost of the acquisition of Park Wealth Group. As a result of the reassessment, the Group revised the fair value of the intangible assets at date of acquisition and this resulted in additional impairment loss and amortisation of intangible assets net of related deferred tax credit amounting to approximately HK\$13,711,000 recognised during the six months ended 30 September 2009.

MANAGEMENT DISCUSSION AND ANALYSIS

The board of directors (the “Board” or the “Directors”) of Chaoyue Group Limited (the “Company”) is pleased to announce the unaudited condensed consolidated results of the Company and its subsidiaries (the “Group”) for the six months ended 30 September 2010 (the “Current Period”), together with the comparative figures.

OVERALL RESULTS

The Group’s turnover HK\$15,747,000 (2009: HK\$42,173,000) for the Current Period were generated from the direct drinking water machines and air and water purification equipment and system businesses operated by Shanghai Comfort Environment and Science Co., Ltd. and its subsidiaries (the “SH Comfort Group”). A gross loss of HK\$7,234,000 (2009: gross profit of HK\$20,704,000) was recorded for the Current Period which was resulted from SH Comfort Group. No turnover or gross profit was contributed by the gold mine in Current Period as the mining work is not yet commenced.

The Group’s unaudited loss for the Current Period was HK\$207,352,000 (2009 (restated): HK\$7,225,122,000). The significant loss recorded in 2009 was mainly due to the changes in fair values of the convertible bonds and warrants and impairment loss on patents amounted to HK\$7,217,316,000 while the loss in Current Year was mainly resulted from: (1) the impairment losses amounted to HK\$113,903,000 in total on the property, plant and equipment, patents and goodwill; and (2) the allowance on bad and doubtful debts and impairment loss on advances to suppliers amounted to HK\$52,151,000.

MANAGEMENT DISCUSSION AND ANALYSIS (Continued)

REVIEW OF OPERATIONS

SH Comfort Group

SH Comfort Group engaged in direct drinking water machines business and air and water purification equipment and system businesses under the brand name of “OZONE COMFORT”.

For the direct drinking water machines business, SH Comfort Group adopted a new business model last year by engaging agents in major provinces in China to operate and manage the business on its behalf instead of dealing with the end users in different regions directly in order to save the administrative effort. However, the pace of expansion was far behind the targets set to the agents. Besides, the Group noted that the performance of certain agents in managing the business was well below our expectation and even defaulted in payment of the instalments. As a result, the Group stopped to sell direct drinking water machines to the agents and decided not to renew and terminate those agents before year end and revise the business strategy to minimise further losses. Only 4,537 new direct water drinking machines were installed in the Current Period. The turnover recorded in the Current Period was HK\$4,599,000 (2009: HK\$24,412,000) and the segment loss recorded was HK\$177,937,000 (2009: HK\$51,942,000). The increase in segment loss for the Current Period was mainly due to impairment losses on the property, plant and equipment, goodwill and patents as a result of the performance which was far behind the expectation and also the provision for doubtful debts from the agents as they defaulted in payment of the instalments.

For the air and water purification equipment and system business, the turnover recorded in the Current Period was HK\$11,148,000 (2009: HK\$17,761,000) and the segment loss was HK\$4,334,000 (2009: HK\$2,644,000). The drop in turnover and increase in segment loss were because most of the customers of SH Comfort Group slowed down their development and expansion plan as a result of the uncertainties of the global economy and the increase of the cost of the raw materials in the Current Period.

Gold Mine

Preliminary works, like design plans for the construction of roads to the mine, mining plant and supply of electricity, had commenced and an experienced management team was established to manage the operation. As more time is required for the preparation works before the exploration work commence, no turnover was recorded in the Current Period. The segment loss of HK\$13,128,000 in the Current Period represented mainly the amortization of the mining license and the expenses on preparation works.

MANAGEMENT DISCUSSION AND ANALYSIS (Continued)

FINANCIAL REVIEW

Liquidity

The Group recorded the net current assets of HK\$477,000 as at 30 September 2010 (31 March 2010: HK\$55,280,000) and the current ratio was 1.0 as at 30 September 2010 as compared to 1.6 as at 31 March 2010. Such drops were mainly due to the provision made on the doubtful receivable balances. The bank balance as at 30 September 2010 was HK\$69,627,000 (31 March 2010: HK\$83,618,000), of which most were denominated in Hong Kong dollars, US dollars and Renminbi.

Gearing ratio

The total borrowings as at 30 September 2010 amounted to approximately HK\$33,071,000, including: (1) borrowings of HK\$9,265,000 (31 March 2010: HK\$9,099,000) which were interest-bearing at 12% per annum; and (2) amount due to a director of a subsidiary of HK\$23,806,000 (31 March 2010: HK\$23,464,000) which was interest free. The gearing ratio of the Group, which was expressed as a percentage of total borrowings to shareholders' equity, as at 30 September 2010 was 24.2% as compared to 9.5% as at 31 March 2010. The increase in the gearing ratio is mainly due to the drop in shareholders' equity as a result of the loss incurred for the Current Period.

Financial resources

The Group currently finances its operations mainly by internally generated funds, and other loans. The management believes that the Group will generate its liquidity from business operations and will consider making use of further equity financing when necessary.

Capital structure

On 16 July 2010, 214,637,160 shares of Non-voting Convertible Preference Shares were issued as the consideration for the acquisition of Park Wealth Group, which is the holding company of SH Comfort Group.

As at 30 September 2010, the Group had 18,824,435,160 ordinary shares and 214,637,160 shares of Non-voting Convertible Preference Shares in issued and recorded a shareholders' equity of HK\$136,567,000.

MANAGEMENT DISCUSSION AND ANALYSIS *(Continued)*

FINANCIAL REVIEW *(Continued)*

Charges on assets

As at 30 September 2010, the Group had no charge on assets.

Contingent liabilities

As at 30 September 2010, the Group had no contingent liabilities.

Foreign exchange exposure

As part of the Group's assets and liabilities are denominated in Renminbi, US dollars and Hong Kong dollars, in order to minimize the foreign exchange risk, the Group aims to utilize the fund for transactions that are denominated in the same currency.

EMPLOYMENT AND REMUNERATION POLICY

As at 30 September 2010, the Group had approximately 10, 12 and 122 employees in Hong Kong, Kyrgyzstan and the PRC respectively. The employees salaries are reviewed and adjusted annually based on their performance and experience. The Group's employee benefits include performance bonus, medical scheme, mandatory provident fund for Hong Kong employees, social insurance packages for the PRC employees and education subsidy to encourage continuous professional development of staff. The Group also has a discretionary share option scheme which is designed to award employees for their performance.

MATERIAL ACQUISITIONS AND DISPOSAL OF SUBSIDIARIES AND ASSOCIATED COMPANIES

There were no material acquisitions and disposal of subsidiaries and associated companies during the Current Period.

MANAGEMENT DISCUSSION AND ANALYSIS *(Continued)*

FUTURE PLAN AND PROSPECTS

For the direct drinking water business and the air and water purification equipment and system business, the Company anticipates facing a very challenging environment in the coming future with the continuous increasing trend in cost of raw materials in Mainland China and the uncertain global economy. The management will explore different measures to tackle the challenges and exploring potential business partner to expand the market.

For the gold mine, exploration work and construction of the infrastructure near the mine will be carried out as anticipated. In view of the continuous rising trend of the gold price over the past years, the Directors expect that the gold mine will bring a wealthy return to the Group in the future.

In the mean time, the management continues to seek any potential investment opportunities to diversify the business scope and expanding the income source of the Group to enhance the profitability and maximize the value of the Group in order to thank you the strong support from all shareholders.

ADDITIONAL INFORMATION

SHARE OPTION SCHEME

The following table discloses details of option outstanding under the Company's share option scheme and movements during the period ended 30 September 2010:

Category of participant	Exercise period	Outstanding at 1 April 2010	Outstanding at 30 September 2010
Directors:			
Yuen Leong	17/7/2008 to 16/9/2014	3,000,000	3,000,000
	17/7/2009 to 16/9/2014	3,000,000	3,000,000
	17/7/2010 to 16/9/2014	3,000,000	3,000,000
Lam Man Kit, Dominic	17/7/2008 to 16/9/2014	3,000,000	3,000,000
	17/7/2009 to 16/9/2014	3,000,000	3,000,000
	17/7/2010 to 16/9/2014	3,000,000	3,000,000
Total directors		18,000,000	18,000,000
Employees:			
	17/7/2008 to 16/9/2014	16,000,000	16,000,000
	17/7/2009 to 16/9/2014	16,000,000	16,000,000
	17/7/2010 to 16/9/2014	16,000,000	16,000,000
Total employees		48,000,000	48,000,000
Grand total		66,000,000	66,000,000

These options were granted on 17 July 2008. The number of share options and exercised price had been adjusted after share subdivision on 3 August 2009. The adjusted exercise price is HK\$0.532 per ordinary share of the Company. No share options were exercised, lapsed or cancelled during the six months ended 30 September 2010.

ADDITIONAL INFORMATION (Continued)

DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS IN SHARES AND UNDERLYING SHARES

As at 30 September 2010, the interests and short positions of the directors and the chief executive and their associates in the shares of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) (a) which were required to be notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they were taken or deemed to have under such provisions of the SFO); or (b) which were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein; or (c) which were required to be notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies, were as follows:

(i) Long position in shares and underlying shares of the Company

Ordinary shares of HK\$0.001 each of the Company

Name of Director	Capacity in which interests are held	Options to Subscribe for Shares of the Company	Number of Shares interested	Interests as to % to the issued share capital of the Company
Yuen Leong	Interest of a controlled corporation	-	12,887,473,880 <i>(Note 1)</i>	68.46%
	Beneficial owner	9,000,000 <i>(Note 2)</i>	-	0.05%
Lam Man Kit, Dominic	Beneficial owner	9,000,000 <i>(Note 2)</i>	-	0.05%

Notes:

- (1) These 12,887,473,880 shares are held by Long Grand Limited which is legally and beneficially owned as to 70% by Mr. Yam Yu and as to 30% by Mr. Yuen Leong. By virtue of his 30% direct interest in Long Grand Limited, Mr. Yuen Leong is deemed or taken to be interested in the 12,887,473,880 shares held by Long Grand Limited for the purposes of the SFO.
- (2) Pursuant to the share option scheme adopted by a resolution of the Shareholders on 17 September 2004, these share options were granted on 17 July 2008 and are exercisable at HK\$0.532 per Share (after share subdivision on 3 August 2009) from 17 July 2008 to 16 September 2014.

ADDITIONAL INFORMATION *(Continued)*

DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS IN SHARES AND UNDERLYING SHARES *(Continued)*

(ii) Long position in shares and underlying shares of associated corporation

Name of Director	Name of associated corporation	Interest held by controlled corporation	Personal interest	Number of ordinary shares (long positions)		
				Family interest	Total number of shares held in associated corporation	Approximate percentage of issued share capital of associated corporation
Yuen Leong	Long Grand Limited	-	Beneficial owner	-	300	30%

Save as disclosed above, as at 30 September 2010, none of the Directors and the chief executive of the Company had any interest or short position in the shares, underlying shares and debentures of the Company or any of its associated corporation (within the meaning of Part XV of the SFO), (a) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they were taken or deemed to have under such provisions of the SFO) or (b) which were required, pursuant to Section 352 of the SFO, to be entered in the register referred to therein, or (c) which were required to be notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies.

DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBENTURES

Apart from the foregoing and save as disclosed under the heading "Share option scheme" and "Directors' and Chief Executives' Interests in Shares and Underlying Shares" above, at no time during the six months ended 30 September 2010 were rights to acquire benefits by means of the acquisition of shares in or debentures of the Company granted to any director or their respective spouse or minor children, or were any such rights exercised by them or was the Company, or any of its holding companies, its fellow subsidiaries or any of its subsidiaries a party to any arrangement to enable the directors, their respective spouse or minor children to acquire such rights in or any other body corporate.

ADDITIONAL INFORMATION *(Continued)*

SUBSTANTIAL SHAREHOLDERS

As at 30 September 2010, the following interest of 5% or more of the issued share capital of the Company were recorded in the register of interests required to be kept by the Company pursuant to section 336 of the SFO.

Long position:

Name	Interest in shares	Nature of interest	Percentage of the Company's issued share capital
Long Grand Limited (Note 1)	12,887,473,880	Direct Beneficial owner	68.46%

Note:

- (1) Long Grand Limited is legally and beneficially owned as to 70% by Mr. Yam Yu and as to 30% by Mr. Yuen Leong.

Save as disclosed above, as at 30 September 2010, no other person, other than the director of the Company, whose interests are disclosed under the heading "Directors' and Chief Executives' Interests in Shares and Underlying Shares" above, had registered an interest or short position in the shares or underlying shares of the Company that was required to be recorded pursuant to Section 336 of the SFO.

ADDITIONAL INFORMATION *(Continued)*

MODEL CODE FOR DIRECTORS' DEALING IN SECURITIES

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 of the Listing Rules. The Company has made specific enquiry of all Directors and all the Directors have complied with the required standard set out in the Model Code and its code of conduct regarding Directors' securities transactions.

PURCHASE, SALES OR REDEMPTION OF THE COMPANY'S SHARES

There was no purchase, sale or redemption by the Company, or any of its subsidiaries, of the Company's securities during the six months ended 30 September 2010.

AUDIT COMMITTEE

On 30 September 2010, the Audit Committee of the Company comprised of three Independent Non-executive Directors, namely, Mr Yap Yung (the Chairman), Dr Lam Man Kit, Dominic and Mr. Zhang Guang Sheng. The audit committee has reviewed the unaudited interim financial information for the six months ended 30 September 2010 and discussed with the management the accounting principle and practice adopted by the Group, internal controls and financial reporting matters of the Group.

At the request of the Audit Committee, the auditor of the Company, Deloitte Touche Tohmatsu, had carried out a review of the unaudited interim financial information for the six months ended 30 September 2010 in accordance with Hong Kong Standard on Review Engagement 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Hong Kong Institute of Certified Public Accountants. Based on their review, our auditor confirmed that nothing has come to their attention that caused them to believe that the interim financial information is not prepared, in all material respects, in accordance with Hong Kong Accounting Standard 34 "Interim Financial Reporting".

ADDITIONAL INFORMATION *(Continued)*

COMPLIANCE WITH THE CODE ON CORPORATE GOVERNANCE PRACTICES

The Company has complied with the code provisions set out in 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 (“the Listing Rules”) throughout the six months ended 30 September 2010 except for the deviation from the code provision A.2.1.

In accordance with the code provision A.2.1, the role of Chairman and Chief Executive Officer (“CEO”) should not be performed by the same individual. Currently, Mr. Yuen Leong serves the role of Chairman of the Board and also the CEO of the Company. Since the role of chief executive officer/general manager of the Company’s major operating subsidiaries are performed by other persons with the relevant expertise and they are directly accountable to the Board, the Board believes that the existing arrangement is adequate. Depending on the future development of the business of the Company, the Board will review the existing structure from time to time and consider the issue of nominating appropriate candidates to take up the title of Chairman and Chief Executive Officer.

By order of the Board
Chaoyue Group Limited
Yuen Leong
Executive Director

Hong Kong, 26 November 2010