



Chairman — Mr. Zhang Fangyou

To all shareholders,

I hereby present the annual report of Denway Motors Limited (the “Company”) and the audited consolidated results of the Company and its subsidiaries (together the “Group”), non-consolidated subsidiaries, associated companies and a jointly controlled entity for the year ended 31 December 2004.

BUSINESS REVIEW

For the year ended 31 December 2004, the turnover of the Group was approximately HK\$1,314,705,000, representing a decrease of 14.3% over that of the previous year (2003: HK\$1,534,779,000). The audited consolidated profit attributable to shareholders was approximately HK\$2,062,447,000, representing an increase of 22.3% as compared to that of the previous year (2003: HK\$1,686,709,000). Earnings per share amounted to HK28.8 cents, representing an increase of 19.5% over that of the previous year (2003: HK24.1 cents).

Year 2004 was an exceptional year for the auto industry of the PRC. Despite the tightening of auto financing, the drop in sedan price and the surge in oil price, a relatively steady and fast growing trend was sustained. The PRC has become the third largest country in terms of sales of motor

vehicles in the world. The aggregate output and sales of motor vehicles for the year were approximately 5,070,500 units and 5,071,100 units respectively, representing an increase of approximately 14.11% and 15.50% respectively over those of the previous year; out of which approximately 2,316,300 units and 2,326,500 units respectively were the total output and sales of sedans, representing an increase of approximately 11.99% and 15.17% respectively over those of the previous year. After recent adjustments, the auto industry of the PRC has reached the stage of stable but rapid development.

During 2004, the Group produced and sold an aggregate of 203,459 units and 203,374 units of motor vehicles respectively through a jointly controlled entity (the "Sedan Company") and its subsidiary (the "Bus Company"), representing an increase of approximately 72% over that of the previous year. Among the total, the output and sales of the Sedan Company accounted for 202,209 units and 202,066 units respectively, representing an increase of approximately 72% over that of the previous year whilst the output and sales of the Bus Company accounted for 1,250 units and 1,308 units respectively, representing an increase of about 22% and 30% respectively over those of the previous year.

In 2004, the performance of all other businesses of the Group, including the trading of motor vehicles, the manufacturing of vehicle-related equipment and parts as well as the manufacturing and trading of audio equipment met our expectations.

FUTURE PROSPECTS

In 2005, the PRC will maintain its prudent approach in adopting stable fiscal and monetary policies so as to strengthen and improve the effectiveness of the austerity measures. It is expected that economic development will sustain a quick and steady pace for a long period of time. The close correlation between the consumption demand for motor vehicles and the GDP implies a high rate of consumption growth and an increasingly stronger spending power on motor vehicles in the PRC in the future. According to the forecast of China Association of Automobile Manufacturers, a total of 5,600,000 units of motor vehicles will be manufactured this year, of which sedans will account for more than 2,600,000 units.

Following the promulgation of the Policies on Auto Industry Development last year, it is expected that the Policies on Motor Vehicles Trading, Measures Governing Auto Brand Selling and Measures Governing Second-hand Motor Vehicles Trading will be implemented this year. We believe that the promulgation of the new policies will have a positive influence on the regulation of the market, facilitating vehicle consumption and establishing a strategic position of the industry. Its impact on the PRC auto industry and market will be overwhelming.

The Sedan Company plans to produce and sell 230,000 units of sedans in 2005, adopting a market-oriented approach whereby more products, which may satisfy market demands and be welcomed by customers, will be introduced. Meanwhile, the Sedan Company will continue to expand and perfect the sales services system. Efforts will be dedicated to product technology, quality and services so as to continue to enhance customers' satisfaction and provide efficient services with higher quality. The Sedan Company persists on a roll-over principle for its development and endeavours to ensure that the construction of the new plant will be completed on schedule in addition to the implementation of the sales and production plans so as to achieve targets at higher levels.

Year 2005 will be a year of rapid development for the auto industry of Guangzhou. The Group will continue to pursue for better development opportunities in relation to the automobile business. The Board believes that the Group will be able to seize such opportunities for further development, thereby generating attractive and better returns for its shareholders.

FINANCIAL SUMMARY

The Group's turnover for the year ended 31 December 2004 was about HK\$1,314,705,000, representing a decrease of about 14.3% compared to that of 2003. The turnover of the trading of motor vehicles decreased by HK\$286,011,000 which represented a decrease of about 28.6% compared to that of 2003. However, the decrease in turnover was compensated by the increase in the second major revenue source of the Group, the manufacturing and assembly of motor vehicles, which recorded a turnover of around HK\$344,298,000, representing an increase of about 34.4% compared to that of 2003. The turnover of other business of manufacturing and trading of audio equipment achieved an increase of about 7.1% as compared to that of 2003. However, the operating profit of this segment decreased by about HK\$4,612,000, or a decrease of 28.3%, due to the increase of cost of goods sold. The orders on hand of the Group for the business of the manufacturing and trading of audio equipment were about HK\$20,000,000 as at 31 December 2004.

The total bank loans of the Group increased from HK\$57,197,000 at the end of year 2003 to HK\$70,625,000 at the end of year 2004. However, the Group maintained a low ratio of borrowings relative to total equity at 1.0% as at 31 December 2004. The ratio of total liabilities (including minority interests) relative to total equity decreased to only 8.8% at 31 December 2004 as compared with the ratio of 13.1% at 31 December 2003. The Group's bank borrowings were secured by land and buildings and investment properties with a total net book value of HK\$60,143,000 and bank balances of HK\$57,671,000. As at 31 December 2004, the Group had contingent liabilities of about HK\$75,978,000 which mainly represented guarantees for bank loans borrowed by an associated company and independent third parties.

The Group had at the end of 2004 cash and bank balances of about HK\$2,594,666,000. This included the cash outflow from operating activities of around HK\$46,336,000. During the year, the payment of dividend by the Company was financed by the receipt of cash dividend from the investments.

General and administrative expenses for the Group in 2004 were about HK\$140,966,000, representing an increase of about 4.2% as compared to that of 2003 mainly due to increase in depreciation expenses. The finance costs increased by around 58.4% due to increase in the total bank loans. The interest cover remained at a high level of 585 multiples in 2004 as compared to that of 751 multiples in 2003. The Group did not experience any significant exchange rate fluctuation in terms of Renminbi, the major operating currency of the Group, during 2004.

Share of net profits of non-consolidated subsidiaries were about HK\$102,000, representing a decrease of 94.3% as compared to that of 2003. Further, share of profits from associated companies, Shanghai Guangchee Automotive Trading and Services Company Limited and Guangzhou Hua De Automobile Spring Company Limited, for the year ended 31 December 2004 was HK\$6,479,000, representing an increase of about 109.8% as compared to that of 2003.

Share of after-tax profit from a jointly-controlled entity was the major source of profit for the Group, which contributed about HK\$2,077,320,000, and represented an increase of about 22.3% as compared to that of 2003 due to strong growth in sales of sedans in 2004.

EMPLOYEES AND REMUNERATION POLICY

As at 31 December 2004, the Group employed approximately 3,000 (2003: 3,000) staffs in the PRC, Hong Kong and Australia.

The remuneration package adopted by the Group includes discretionary bonus and share options being granted to eligible staff based on the Group's performance and individual performance. Staff training and development programs are conducted on a regular basis.

ACKNOWLEDGEMENTS

I would like to extend my appreciation to all shareholders for their support and to thank the Directors for their guidance and the staff members for their dedication and hard work.

Zhang Fangyou
Chairman

Hong Kong, 14 April 2005