



山東晨鳴紙業集團股份有限公司

SHANDONG CHENMING PAPER HOLDINGS LIMITED*

(a joint stock company incorporated in the People's Republic of China with limited liability)

Stock code: 1812



08 annual report

* For identification purposes only

Important:

The board of directors (the “Board”), the supervisory committee (the “Supervisory Committee”) and the directors (the “Directors”), supervisors (the “Supervisors”) and senior management (the “Senior Management”) of the Company hereby warrant that there are no false representations, misleading statements or material omissions contained in this report (the “Report”), and jointly and severally accept full responsibility for the truthfulness, accuracy and completeness of its contents. This Report has been prepared in both Chinese and English. For any discrepancies, the Chinese version shall prevail.

Chen Hongguo, the chairman of the Company, Liu Junwu, the financial controller of the Company and Wang Chunfang, the head of the financial department, declare that they guarantee the truthfulness and completeness of the financial statements of the 2008 Annual Report.

Definitions: “Company”, “the Company”, and “Chenming Paper”, “us”, and “we” refer to Shandong Chenming Paper Holdings Limited, and the Company and its subsidiaries are collectively referred to as “the Group” in this report, unless otherwise specified.

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I Company Information

1. Legal Chinese name of the Company: 山東晨鳴紙業集團股份有限公司
Legal English name of the Company: SHANDONG CHENMING PAPER HOLDINGS LIMITED
Abbreviation of the English name: SCPH
2. Legal Representative of the Company: Chen Hongguo
3. Secretary to the Board of the Company: Hao Yun
Company Secretary: Poon Shiu Cheong
Securities Affairs Representatives: Fan Yingjie, Sun Wenke
Correspondence Address: No. 595 Shengcheng Road, Shouguang City, Shandong Province, People's Republic of China
Telephone: (86)-0536-2158011, (86)-0536-2156488
Facsimile: (86)-0536-2158640
Email address: chenmmingpaper@163.com
4. Registered Address and Office address of the Company: No. 595 Shengcheng Road, Shouguang City, Shandong Province, People's Republic of China
Postal Code: 262700
Website of the Company: <http://www.chenmingpaper.com>
5. Designated Newspapers for Information Disclosure: China Securities Journal and Hong Kong Commercial Daily
Designated Domestic Website for the Publication of the Annual Report as approved by China Securities Regulatory Commission: <http://www.cninfo.com.cn>
Designated Overseas Website for the Publication of the Annual Report: <http://www.hkex.com.hk>
Places for Inspection of the Company's Annual Report: Capital operation department of the Company

I Company Information

6. Stock Information:

A shares

Shenzhen Stock Exchange

Stock Abbreviation: 晨鳴紙業

Stock Code: 000488

B shares

Shenzhen Stock Exchange

Stock Abbreviation: 晨鳴B

Stock Code: 200488

H shares

The Stock Exchange of Hong Kong Limited

Stock Abbreviation: Chenming Paper

Stock Code: 1812

7. Share Registrar

A Share and B Share Registrar:

China Securities Depository and Clearing Corporation
Limited Shenzhen Branch
18th Floor, CITIC Plaza, 1093 Shennan Zhong Road,
Shenzhen

H Share Registrar:

Computershare Hong Kong Investor Services Limited
Shops 1712-16, 17/F, Hopewell Centre, 183 Queen's
Road East, Wanchai, Hong Kong

8. Other Relevant Information

Date of Change in Registration
of the Company:

27 September 2008

Registered Address:

No. 595 Shengcheng Road, Shouguang City, Shandong
Province, People's Republic of China

Legal Person Business License

Registration Number:

370000400001170

Taxation Registration Number:

370783613588986

Organization No.:

61358898-6

I Company Information

9. PRC and International Auditors Retained by the Company

PRC Auditors:	Deloitte Touche Tohmatsu Certified Public Accountants Ltd.
Office Address:	Beijing Branch, 8/F office Tower W2, The Towers, Oriental Plaza, 1 East Chang An Avenue, Beijing 100738, PRC
International Auditors:	Deloitte Touche Tohmatsu
Office Address:	35/F., One Pacific Place, 88 Queensway, Hong Kong

10. PRC and Hong Kong Legal Advisers Retained by the Company

PRC Legal Advisers:	Hylands Law Firm 5A1, 5th Floor, East Zone, Hanwei Plaza, No. 7 Guanghua Road, Chaoyang District, Beijing City, PRC
Hong Kong Legal Advisers:	Li & Partners Solicitors 22nd Floor, World Wide House, Central, Hong Kong

11. Principal Bankers

Industrial and Commercial Bank of China, Shouguang Branch
No. 118 Guangchang Street, Shouguang City, Shandong Province, PRC

II Summary of Financial and Operating Results

I. Major financial data for the year of the Group

(I) Major financial data for the year of the Group prepared in accordance with Accounting Standards for Business Enterprises

Unit: RMB

No	Key financial indicators	Amount
1	Operating profit	1,292,771,697.51
2	Total profit	1,555,339,310.69
3	Net profit attributable to the equity holders of the Company	1,075,291,741.53
4	Net profit after extraordinary gains or losses attributable to the equity holders of the Company	854,268,917.39
5	Net cash flows from operating activities	1,934,140,803.04

Extraordinary gains or losses items (Unit: RMB)

Extraordinary gains or losses items	Amount
Gains and losses generated from held for trading financial assets, other than effective hedging activities associated with normal business operations of the Company	1,738,200.00
Reversal of impairment provision on receivables tested for impairment on individual basis	39,718,405.84
Net gain and loss from disposal of non-current assets	-1,219,356.66
Government grants received	178,084,185.07
Net gains or losses attributable to debt restructuring	103,365.66
The shortfall of the consideration for the acquisition of minority interests in comparison with the attributable book value of the identifiable net assets of the acquiree	28,209,117.78
Profit or loss arising from investment costs for acquisition of a subsidiary by the corporation being less than its share of fair value of identifiable net assets of the invested entity on acquisition	60,519.78
Non-operating net gain and loss other than the above	23,477,854.77
Effect of extraordinary gains or losses on income tax	-34,679,297.41
Effect of minority interests	-14,470,170.69
Total	221,022,824.14

II Summary of Financial and Operating Results

I. Major financial data for the year of the Group (continued)

(II) Financial highlights prepared in accordance with International Financial Reporting Standards

Unit: RMB in million

Results items	For the year ended 31 December			
	2008	2007	2006	2005
Revenue	15,430.9	14,878.9	11,714.0	9,625.8
Cost of sales	(12,472.9)	(11,845.6)	(9,461.7)	(7,662.5)
Gross profit	2,958.0	3,033.3	2,252.3	1,963.3
Other income	500.5	462.3	315.2	248.6
Gain on disposal of subsidiaries	—	—	35.9	—
Share of results of associates	(23.2)	(9.5)	(0.5)	0.6
Distribution expenses	(705.6)	(783.3)	(677.8)	(534.7)
Administrative expenses	(542.7)	(653.2)	(557.4)	(468.6)
Loss on change in conversion price of convertible loan notes	—	—	(229.4)	—
Gain on change in fair value of derivative financial instruments	1.7	6.0	—	—
Gain on change in fair value less estimated point-of-sale cost of biological assets	0.9	24.4	—	—
Impairment loss on property, plant and equipment	(8.5)	—	—	—
Allowance for inventory	(127.7)	(0.9)	—	—
Finance costs	(462.6)	(555.7)	(512.6)	(311.3)
Profit before tax	1,590.8	1,523.4	625.7	897.9
Income tax expense	(295.8)	(270.8)	(100.7)	(175.8)
Profit for the year from continuing operations	1,295.0	1,252.6	525.0	722.1
Discontinued operation				
(Loss) profit from discontinued operation for the year	—	—	36.3	(7.8)
Profit for the year	1,295.0	1,252.6	561.3	714.3
Profit attributable to:				
Equity holders of the Company	1,102.3	994.0	400.6	640.8
Minority interests	192.7	258.6	160.7	73.5
	1,295.0	1,252.6	561.3	714.3

II Summary of Financial and Operating Results

I. Major financial data for the year of the Group (continued)

(II) Financial highlights prepared in accordance with International Financial Reporting Standards (continued)

Assets and liabilities items	As at 31 December			
	2008	2007	2006	2005
Total assets	26,207.3	21,913.7	20,467.5	18,243.4
Total liabilities	12,550.3	11,733.4	13,011.5	11,368.4
Minority interests	1,744.8	1,809.1	1,703.6	1,663.1
Equity attributable to equity holders of the Company	11,912.2	8,371.2	5,752.4	5,211.9
Financial indicators	2008	2007	2006	2005
Earnings per share	0.58	0.62	0.29	0.47
Net assets per share	5.78	4.91	4.21	3.85
Rate of return on net assets	9.25%	11.87%	6.96%	12.29%

II. Effect of adjustment in accordance with International Financial Reporting Standards on net profit and net assets

Net profit in the Financial Statements 2008 prepared in accordance with Accounting Standards for Business Enterprises by the Company was RMB1,259,541,454.27, and net assets were RMB14,021,774,664.96. The main differences with the net profit and net assets set out in the financial statements prepared in accordance with International Financial Reporting Standards were as follows:

Items	Unit: RMB	
	As at 31 December 2008 Net assets	For the year ended 31 December 2008 Net profit
Amounts set out in the financial statements prepared in accordance with International Financial Reporting Standards	13,656,968,902.24	1,294,998,937.34
Special fund for treasury bonds and special payables received	344,948,245.89	-32,490,567.06
Exchange gains or losses from special foreign currency borrowings	19,857,516.83	-2,966,916.01
Amounts set out in the financial statements prepared in accordance with Accounting Standards for Business Enterprises	14,021,774,664.96	1,259,541,454.27

Explanation: In year prior to 2006, according to the principles of the PRC Accounting Standards of Business Enterprises (ASBEs), the Group will receive special fund for treasury bond received and special accounts payable related to construction of relevant fixed assets which are included in capital reserve. However, according to IFRS, the Group will account for special fund for treasury bond received and special accounts payable under deferred income and be amortized by installments over the useful lives of fixed assets.

II Summary of Financial and Operating Results

III. Major financial data and indicators of the last three years prepared in accordance with Accounting Standards for Business Enterprises

Unite: RMB

Items / Indicators	For the year ended 31 December 2008	For the year ended 31 December 2007	Increase / decrease (%)	For the year ended 31 December 2006 Before adjustments	After adjustments
Operating revenue	15,529,593,435.77	15,164,742,450.26	2.41%	11,814,092,426.36	11,983,464,568.89
Total profit	1,555,339,310.69	1,489,336,202.56	4.43%	891,269,259.51	615,690,757.28
Net profit attributable to the equity holders of the Company	1,075,291,741.53	967,636,172.39	11.13%	602,967,195.37	356,907,182.90
Net profit after extraordinary gains or losses attributable to the equity holders of the Company	854,268,917.39	878,418,573.66	-2.75%	436,232,957.51	396,061,925.60
Net cash flows from operating activities	1,934,140,803.04	1,324,263,125.01	46.05%	1,008,558,176.84	1,008,558,176.84
Basic earnings per share	0.57	0.60	-5.00%	0.4425	0.26
Diluted earnings per share	N/A	0.59	N/A	0.4415	N/A
Basic earnings per share after extraordinary gains or losses	0.45	0.54	-16.67%	0.3201	0.29
Rate of return on net assets on fully diluted basis	8.77%	11.06%	-2.29%	10.03%	5.80%
Rate of return on net assets on weighted average basis	10.24%	12.64%	-2.40%	10.83%	6.06%
Rate of return on net assets on fully diluted basis after extraordinary gains and losses	6.97%	10.04%	-3.07%	7.26%	6.44%
Rate of return on net assets on weighted average basis after extraordinary gains and losses	8.13%	11.47%	-3.34%	7.84%	6.73%
Net cash flows per share from operating activities	0.9380	0.7761	20.86%	0.7385	0.7385

II Summary of Financial and Operating Results

III. Major financial data and indicators of the last three years prepared in accordance with Accounting Standards for Business Enterprises (continued)

	As at 31 December 2008	As at 31 December 2007	Increase / decrease (%)	As at 31 December 2006 Before adjustments	After adjustments
Total assets	26,299,495,745.01	22,011,108,257.29	19.48%	20,547,990,949.39	20,558,560,560.77
Equity attributable to equity holders of the Company	12,259,078,901.99	8,745,035,011.85	40.18%	6,010,124,970.09	6,151,642,343.81
Net assets per share attributable to equity holders of the Company	5.9451	5.1250	16.00%	4.4009	4.5045

Note: According to the requirement of Article 14 “gains and losses on changes in fair value of financial assets held for trading and financial liabilities held for trading and investment income generated from disposal of financial assets held for trading, financial liabilities held for trading and available-for-sale financial assets, other than effective hedging activities associated with normal business operations of the company” of Dilution Information Disclosure by Companies Offering Securities to the Public No.1 – extraordinary gains or losses (2008), the Company had adjusted the extraordinary gains or losses of 2007.

IV. Rate of Return on net assets and earnings per share in accordance with Preparation Criteria of Information Disclosure by Companies Offering Securities to the Public No. 9 issued by China Securities Regulatory Commission

	Rate of Return on net assets (%)		Earnings per share (RMB)	
	Fully diluted	Weighted average	Fully diluted	Weighted average
Net profit attributable to equity holders of the Company	8.77%	10.24%	0.57	N/A
Net profit after extraordinary gains or losses attributable to equity holders of the Company	6.97%	8.13%	0.45	N/A

III Changes in Share Capital and Shareholders

I. Changes in share capital

(Unit: shares)

	Opening balance		Increase/decrease (+/-)					Closing balance	
			resulting from changes in the reporting period						
	Number of shares	Percentage	Increase in lock- up shares	Restricted shares	Transfer of state- owned shares	Issue of new shares	Sub- total	Number of shares	Percentage
I. Restricted shares	339,500,453	19.90%	176,774	-120,101	-35,570,000	—	-35,513,327	303,987,126	14.74%
of which: State-owned legal person shares	328,573,657	19.26%	—	—	-35,570,000	—	-35,570,000	293,003,657 ⁽¹⁾	14.21%
Shares held by Senior Management	10,926,796	0.64%	176,774	-120,101	—	—	56,673	10,983,469 ⁽²⁾	0.53%
II. Non-restricted shares	1,366,845,488	80.10%	-176,774	120,101	35,570,000	355,700,000	391,213,327	1,758,058,815	85.26%
of which: Renminbi ordinary shares									
(A shares)	809,348,003	47.43%	-176,774	120,101	—	—	-56,673	809,291,330	39.25%
Domestic listed foreign shares									
(B shares)	557,497,485	32.67%	—	—	—	—	—	557,497,485	27.04%
Overseas listed foreign shares									
(H shares)	—	—	—	—	35,570,000	355,700,000	391,270,000	391,270,000	18.97%
III. Total number of shares	1,706,345,941	100.00%	—	—	—	355,700,000	355,700,000	2,062,045,941	100.00%

III Changes in Share Capital and Shareholders

I. Changes in share capital (continued)

- Note:
1. Pursuant to the Notice of the Provisional Administrative Measures for State-owned Shares reduction for Raising Social Security Fund promulgated by the State Council (《國務院關於印發減持國有股籌集社會保障資金管理暫行辦法的通知》), the State-owned Assets Supervision and Administration Commission of the State Council approved the transfer from Shouguang Chenming Holdings Co., Ltd. to the National Social Security Fund Council of the PRC (the “NSSF Council”) such number of A shares held by it in aggregate equivalent to 10% of the number of the offer shares, representing 35,570,000 state-owned legal person shares, which were converted into overseas listed foreign shares (H shares) and listed on the Main Board of The Stock Exchange of Hong Kong Limited upon the issuance of overseas listed foreign shares (H shares) by the Company. The number of A shares held by Shouguang Chenming Holdings Co., Ltd. was reduced to 293,003,657 shares.
 2. During the reporting period, the restricted shares held by the Senior Management changed by 56,673 shares from 10,926,796 shares to 10,983,469 shares. The reasons for such change were as follows:
 - (1) According to “the Practice Guidance for the Company’s shares held by the directors, supervisors and senior management of the listed companies of Shenzhen Stock Exchange” (《深圳證券交易所上市公司董事、監事和高級管理人員所持本公司股份管理業務操作指南》), the shares held by the existing Directors, Supervisors and Senior Management would be unlocked up on the basis of the percentage of 25% of the shares held at the beginning of each year. For the 27,301 shares held by the Senior Management, the nature of the shareholdings would be changed from “restricted shares held by the senior management” to “non-restricted RMB ordinary shares (A shares)”. The Senior Management of the Company did not dispose any shares of the Company.
 - (2) During the reporting period, the half year lock-up period for the resigned Directors and Senior Management of the Company was expired. Therefore, the nature of the 92,800 shares, used to be held by the Senior Management, was changed from restricted shares held by the senior management to the non-restricted RMB ordinary shares (A shares).
 - (3) During the reporting period, the unlocked non-restricted shares held by Dong Jianwen, the resigning deputy general manager, were locked up again as his resignation had been effective for less than 6 months. The shares held by Meng Feng, the new deputy general manager, were locked up, therefore the number of lock-up shares held by Senior Management increased by 176,774 shares.

III Changes in Share Capital and Shareholders

II. Offering of shares and the listing

- As approved by the approval document No. [2008] 290 on Approval of the Issue of Overseas Listed Foreign Shares by Shandong Chenming Paper Holdings Ltd. from the CSRC, and the approval from the Stock Exchange of Hong Kong Limited (the “Hong Kong Stock Exchange”), the Company issued overseas listed foreign shares (H shares) through global offering. The offer price of this global offering was HK\$9.00 per H share, and the Company offered 355,700,000 H shares for the global offering, of which, 35,570,000 H shares were offered in the Hong Kong public offering and the remaining 320,130,000 H shares were offered in the international offering. 35,570,000 state-owned legal person shares were transferred to NSSF Council due to the reduction of shareholding of state-owned shares by the Company’s relevant state-owned corporate shareholders, and were converted into overseas listed foreign shares (H shares). A total of 391,270,000 H shares were listed on the main board of the Hong Kong Stock Exchange on 18 June 2008. The Company’s English abbreviation is “Chenming Paper” and its stock code is “1812”.
- No staff shares of the Company have been issued.

III. Shareholders’ profiles

1. Change in restricted shares

Names of shareholders	Restricted	Restricted	Restricted	Restricted	Reason for restriction	Date of release from restriction
	shares at the beginning of the year	shares released this year	shares increased this year	shares at the end of the year		
Shouguang Chenming Holdings Company Limited	328,573,657	35,570,000	0	293,003,657	Commitments during the reform of conversion	29 March 2010
Shares held by Senior Management of the Company	10,926,796	120,101	176,774	10,983,469	Lock-up of shares held by senior management of the Company	Released according to relevant rules of the ShenZhen Stock Exchange
Total	339,500,453	35,690,101	176,774	303,987,126	—	—

Note: For “Restricted shares released this year” of Shouguang Chenming Holdings Company Limited, please refer to the descriptions in Note 2 of Part I in this section.

III Changes in Share Capital and Shareholders

III. Shareholders' profiles (continued)

2. Top ten shareholders and the top ten shareholders of non-restricted shares

Unit: shares

Total number of shareholders The total number of shareholders was 153,980, of which, 116,525 were holders of A shares, 36,629 were holders of B shares and 826 were holders of H shares

Shareholdings of the top ten shareholders

Name of shareholders	Nature of shareholders	Percentage of shareholding	Total number of shares held	Number of restricted shares held	Number of shares pledged or locked-up
HKSCC Nominees Limited	Overseas non-state-owned legal person (foreign shareholder)	18.89%	389,783,500	0	Unknown
Shouguang Chenming Holdings Company Limited	State-owned legal person	14.21%	293,003,657	293,003,657	None
Agricultural Bank of China - 中郵核心成長股票型證券投資基金	Domestic non-state-owned legal person	1.67%	34,499,190	0	Unknown
Agricultural Bank of China - 中郵核心優選股票型證券投資基金	Domestic non-state-owned legal person	1.62%	33,494,942	0	Unknown
Bank of China - 華夏行業精選股票型證券投資基金(LOF)	Domestic non-state-owned legal person	1.27%	26,107,478	0	Unknown
China Construction Bank - 鵬華價值優勢股票型證券投資基金	Domestic non-state-owned legal person	1.20%	24,731,696	0	Unknown
Industrial and Commercial Bank of China - 諾安股票證券投資基金	Domestic non-state-owned legal person	1.19%	24,578,106	0	Unknown

III Changes in Share Capital and Shareholders

III. Shareholders' profiles (continued)

2. Top ten shareholders and the top ten shareholders of non-restricted shares (continued)

Name of shareholders	Nature of shareholders	Percentage of shareholding	Total number of shares held	Number of restricted shares held	Number of shares pledged or locked-up
China Construction Bank - 華夏紅利混合型開放式證券投資基金	Domestic non-state-owned legal person	0.99%	20,415,255	0	Unknown
Joincare Pharmaceutical Group Industry Co., Ltd	Domestic non-state-owned legal person	0.92%	18,900,000	0	Unknown
KEYWISE GREATER CHINA OPPORTUNITIES MASTER FUND	Overseas legal person	0.85%	17,476,904	0	Unknown

Shareholding of the top ten shareholders of non-restricted shares

Name of shareholders	Number of non-restricted shares held	Class of shares
HKSCC Nominees Limited	389,783,500	H share
Agricultural Bank of China - 中郵核心成長股票型證券投資基金	34,499,190	A share
Agricultural Bank of China - 中郵核心優選股票型證券投資基金	33,494,942	A share
Bank of China - 華夏行業精選股票型證券投資基金(LOF)	26,107,478	A share
China Construction Bank - 鵬華價值優勢股票型證券投資基金	24,731,696	A share
Industrial and Commercial Bank of China - 諾安股票證券投資基金	24,578,106	A share
China Construction Bank - 華夏紅利混合型開放式證券投資基金	20,415,255	A share
Joincare Pharmaceutical Group Industry Co., Ltd	18,900,000	A share
KEYWISE GREATER CHINA OPPORTUNITIES MASTER FUND	17,476,904	B share
PLATINUM ASIA FUND	16,234,459	B share

III Changes in Share Capital and Shareholders

III. Shareholders' profiles (continued)

2. Top ten shareholders and the top ten shareholders of non-restricted shares (continued)

Connected relationship or concert-party relationship among the above shareholders

Among the top ten shareholders of the Company, Shouguang Chenming Holdings Company Limited, a state-owned legal person shareholder, is not connected with any of the other shareholders, nor is it a party acting in concert with any of them as defined in Administrative Measures for Information Disclosure of the Changes in Shareholdings of Listed Companies (《上市公司持股變動信息披露管理辦法》); among which, Agricultural Bank of China — 中郵核心成長股票型證券投資基金 and Agricultural Bank of China — 中郵核心優選股票型證券投資基金 are the sub-funds of 中郵創業基金管理有限公司. Bank of China — 華夏行業精選股票型證券投資基金(LOF) and China Construction Bank — 華夏紅利混合型開放式證券投資基金 are the sub-funds of 華夏基金管理有限公司. Save for the above, the Company is not aware that any other shareholders of outstanding shares as aforesaid are connected with others or whether any of these shareholders falls within the meaning of parties acting in concert as defined in Administrative Measures for Information Disclosure of Changes in Shareholdings of Listed Companies (《上市公司持股變動信息披露管理辦法》).

3. Profile of controlling shareholders and beneficial controllers

- (1) The Company's controlling shareholders and beneficial controllers remained unchanged during the reporting period.
- (2) The controlling shareholder of the Company, Shouguang Chenming Holdings Company Limited (hereinafter referred to as "Chenming Holdings"), was established on 30 December 2005 with registered capital of RMB1.685 billion. Its legal representative is Chen Hongguo. Scope of business is investment in paper-making, electricity, heat and forestry projects. At the end of the reporting period, it held 293,003,657 state-owned legal person shares, representing 14.21% of the total share capital of the Company. During the reporting period, 35,570,000 state-owned shares were converted to overseas listed foreign shares (H share) and transferred to NSSF Council due to the reduction of shareholding of state-owned shares by the Company in connection with the issuance of overseas listed foreign shares (H share), the remaining shares held by it were neither pledged or locked-up. During the reporting period, Shandong San Wei Oil Group Company Limited ("Shandong Sanwei"), a shareholder of Chenming Holdings, transferred 10.86% equity interests in Chenming Holdings held by it to Shouguang Henglian Enterprise Investment Co. Ltd.; upon completion of transfer, Shandong Sanwei no longer held any equity interests in Chenming Holdings. State-owned Assets Supervision and Administration Commission of Shouguang City continued to hold 75.73% equity interests in Chenming Holdings. The beneficial controllers of the Company remained unchanged.

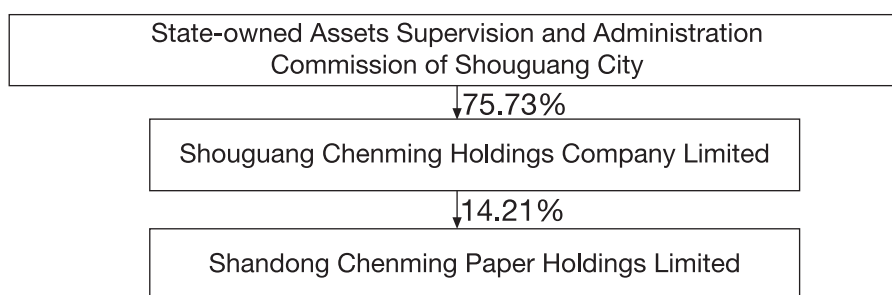
III Changes in Share Capital and Shareholders

III. Shareholders' profiles (continued)

3. Profile of controlling shareholders and beneficial controllers (continued)

(3) State-owned Assets Supervision and Administration Commission of Shouguang City is the controlling shareholder of Chenming Holdings, holding 75.73% equity interests in Chenming Holdings. Person in charge of the unit is Zhang Yuhua. Scope of business is administration and supervision of state-owned assets, properties and titles belonging to Shouguang City.

(4) Chart illustrating the relationship between the Company and the beneficial controllers



III Changes in Share Capital and Shareholders

III. Shareholders' profiles (continued)

4. The Company's substantial shareholders' and other persons' interest in shares or debentures

As at 31 December 2008, the following shareholders (other than the directors, supervisors or chief executives of the Company) had interests or short positions in the Company's shares and underlying shares as shown in the share register maintained by the Company in accordance with Section 336 of the Securities and Futures Ordinance ("SFO") (Chapter 571 of the Laws of Hong Kong):

Name	Number of shares held (share)	Approximate shareholding as a percentage of (%)	
		Total share capital	Class of shares
Shouguang Chenming Holdings Company Limited	293,003,657 A shares (L)	14.21	26.32
JPMorgan Chase & Co.	55,527,500 H shares (L)	2.69	14.19
	50,527,500 H shares (P)	2.45	12.91
Schroder Investment Management (Hong Kong) Limited	39,119,500 H shares (L)	1.90	9.99
NSSF Council	35,570,000 H shares (L)	1.73	9.09
Invesco Ltd.	31,527,000 H shares (L)	1.53	8.06
Keywise Capital Management (HK) Limited	23,634,000 H shares (L)	1.15	6.04

(L) – Long position

(S) – Short position

(P) – Lending pool

Save as disclosed above, as at 31 December 2008, no other person had interests or short positions in the Company's shares or underlying shares as recorded in the register maintained under section 336 of the SFO.

5. Purchase, sale and redemption of shares

Save for the listing of H shares of the Company on the main board of the Hong Kong Stock Exchange on 18 June 2008, the Group did not purchase, sell or redeem any listing outstanding securities of the Company during the reporting period.

IV Directors, Supervisors and Senior Management and the Staff

I. Changes in shareholdings and remunerations of the Directors, Supervisors and Senior Management

Name	Position	Sex	Age	Terms in office	Shares held at the beginning of the year (share)	Shares held at the end of the year (share)	Change in number of shares (share)	Reasons for change	Total remuneration received from the Company during the reporting period (in ten thousands RMB)
I. Executive Directors									
Chen Hongguo	Chairman	M	44	April 2007 - April 2010	6,334,527	6,334,527	0	—	144.68
Yin Tongyuan	Vice-chairman and general manager	M	51	April 2007 - April 2010	3,231,520	3,231,520	0	—	96.12
Li Feng	Director, sales director	M	36	April 2007 - April 2010	471,818	471,818	0	—	59.40
Hou Huancai	Director	M	47	April 2007 - April 2010	628,915	628,915	0	—	54.00
Zhou Shaohua	Director	M	47	April 2007 - April 2010	125,307	123,007	-2,300	Note 3	27.00
Xing Fangtong	Director	M	43	April 2007 - April 2009	355,561	355,561	0	—	19.84
Wu Bingyu	Director	M	43	April 2007 - April 2009	428,107	428,107	0	—	27.65
II. Non-executive Directors									
Gan Zhihe	Director	M	64	April 2007 - April 2010	0	0	0	—	4.00
Zhao Wei	Director	M	49	April 2007 - April 2010	0	0	0	—	4.00
Cao Chunyu	Director	M	45	April 2007 - April 2010	0	0	0	—	4.00
III. Independent non-executive Directors									
Diao Yuntao	Independent Director	M	44	April 2007 - April 2010	0	0	0	—	4.00
Wang Zihua	Independent Director	M	50	April 2007 - April 2010	0	0	0	—	4.00
Zhou Chengjuan	Independent Director	F	45	April 2007 - April 2010	0	0	0	—	4.00
Wang Yumei	Independent Director	F	46	April 2007 - April 2010	0	0	0	—	4.00
Lau Ying Kit	Independent Director	M	34	April 2007 - April 2010	0	0	0	—	10.00

IV Directors, Supervisors and Senior Management and the Staff

I. Changes in shareholdings and remunerations of the Directors, Supervisors and Senior Management (continued)

Name	Position	Sex	Age	Terms in office	Shares held at the beginning of the year	Shares held at the end of the year	Change in number of shares	Reasons for change	Total remuneration received from the Company during the reporting period (in ten thousands RMB)
IV. Supervisors									
Gao Junjie	Chairman of Supervisory Committee	M	38	April 2007 - April 2010	39,606	39,606	0	—	7.42
Wang Ju	Supervisor	F	43	April 2007 - April 2010	0	0	0	—	13.45
Yang Hongqin	Supervisor	F	41	April 2007 - April 2010	0	0	0	—	6.94
Zhao Shujun	Supervisor	M	35	April 2007 - April 2010	0	0	0	—	6.47
Liu Wenzheng	Supervisor	M	37	April 2007 - April 2010	0	0	0	—	0.00

IV Directors, Supervisors and Senior Management and the Staff

I. Changes in shareholdings and remunerations of the Directors, Supervisors and Senior Management (continued)

Name	Position	Sex	Age	Terms in office	Shares held at the beginning of the year	Shares held at the end of the year	Change in number of shares	Reasons for change	Total remuneration received from the Company during the reporting period (in ten thousands RMB)
V. Senior Management									
Wang Baoliang	Deputy general manager	M	35	April 2007 - April 2010	209,200	209,200	0	—	28.08
Geng Guanglin	Deputy general manager	M	35	April 2007 - April 2010	437,433	437,433	0	—	45.90
Ren Wei	Deputy general manager	M	47	April 2007 - April 2010	109,200	109,200	0	—	21.60
Li Xueqin	Deputy general manager	F	43	April 2007 - April 2010	429,348	429,348	0	—	25.92
Hao Yun	Deputy general manager, secretary to the Board of Directors	M	46	April 2007 - April 2010	708,441	708,441	0	—	27.00
Wang Zaiguo	Deputy general manager	M	46	April 2007 - April 2010	195,600	195,600	0	—	21.60
Wang Shihong	Deputy general manager	M	45	April 2007 - April 2010	0	0	0	—	18.00
Fang Lijun	Deputy general manager	M	39	April 2007 - April 2010	436,851	436,851	0	—	25.24
Meng Feng	Deputy general manager	M	37	April 2008 - April 2010	185,700	185,700	0	—	27.00
Han Chunlai	Deputy general manager	M	45	April 2008 - April 2010	0	0	0	—	21.60
Xia Guangchun	Deputy general manager	M	44	April 2007 - April 2009	70,700	70,700	0	—	18.73
Liu Junwu	Chief financial officer	M	47	April 2007 - April 2009	0	0	0	—	17.28
Total	—	—	—	—	14,397,834	14,395,534	-2,300	—	798.92

IV Directors, Supervisors and Senior Management and the Staff

I. Changes in shareholdings and remunerations of the Directors, Supervisors and Senior Management (continued)

Note:

1. The 2001 annual general meeting of the Company approved the resolution to establish a Share Option Incentive Scheme for the Senior Management and resolved to adopt share option incentives for the Senior Management of the Company. The Company had purchased its own A shares for some of its Directors and operating management in prior years, details of which were disclosed in the 2004 and 2006 annual reports. There were no share option incentive events during the year.
2. None of the Directors, Supervisors and Senior Management of the Company had received any remunerations from shareholder or other related entities.
3. During the reporting period, Mr. Zhou Shaohua, an executive Director of the Company, sold part of the outstanding A shares held by him in the secondary market after sales restrictions were released.

II. Major career histories of Directors, Supervisors and Senior Management and their positions

1. Brief Biographies of Directors

(1) Brief biographies of executive Directors

Mr. Chen Hongguo, who joined the Company in 1987, had held different positions including chief officer of manufacturing section, chief officer of branch factory, deputy general manager, executive Director of the Company and the chairman of Wuhan Chenming Hanyang Paper Co., Ltd., etc. He is currently the Chairman of the Company and the chairman and general manager of Chenming Holdings. Mr. Chen Hongguo is the spouse of Ms. Li Xueqin, a deputy general manager of the Company.

Mr. Yin Tongyuan, who joined the Company in 1982, had held different positions including the chief officer of manufacturing section, director of technology department, deputy factory chief and standing deputy factory chief. He is presently the party committee secretary, vice-chairman and general manager of the Company and a director of Chenming Holdings.

Mr. Li Feng, who joined the Company in 1992, had held different positions including the chief officer of manufacturing section, assistant to the general manager, deputy general manager of Shandong Chenming Paper Group Qihe Paperboard Co., Ltd., deputy general manager, vice-chairman and chairman of Wuhan Chenming Hanyang Paper Co., Ltd. He is currently the executive Director and the sales director of the Company. Mr. Li Feng is the brother of Ms. Li Xueqin, a deputy general manager of the Company.

IV Directors, Supervisors and Senior Management and the Staff

II. Major career histories of Directors, Supervisors and Senior Management and their positions (continued)

1. Brief Biographies of Directors (continued)

(1) Brief biographies of executive Directors (continued)

Mr. Hou Huancai, who joined the Company in 1983, had held different positions including the chief officer of manufacturing section, chief of branch factory, chairman of Jilin Chenming Paper Co., Ltd., chairman of Shandong Chenming Paper Group Qihe Paperboard Co., Ltd. and Jiangxi Chenming Paper Co., Ltd. and the chairman of the 1st and 2nd Supervisory Committee of the Company. He is currently an executive Director of the Company and the chairman of Jilin Chenming Paper Co., Ltd.

Mr. Zhou Shaohua, who joined the Company in 1997, had held different positions of the standing deputy general manager, chief engineer, vice-chairman of Wuhan Chenming Hanyang Paper Co. Ltd. and the chairman of Jiangxi Chenming Paper Co., Ltd. He is currently an executive Director of the Company and the party committee secretary of Zhanjiang Chenming Paper Pulp Co., Ltd.

Mr. Xing Fangtong, who joined the Company in 1984, had held different positions including the machines supervisor, chief officer of manufacturing section and general manager and chairman of Chibi Chenming Paper Co., Ltd. He is currently the executive Director of the Company. On 8 April 2009, the Twelfth Meeting of the Fifth Session of the Board approved the resolution for Xing Fangtong's resignation from executive Director of the Company.

Mr. Wu Bingyu, who joined the Company in 1989, had held different positions including the supervisor of organization department, officer of the party office, leader of the party section, assistant to the general manager and party committee vice secretary of Wuhan Chenming Hanyang Paper Co. Ltd. and the chairman of Jilin Chenming Paper Co., Ltd. He is currently the executive Director of the Company. On 8 April 2009, the Twelfth Meeting of the Fifth Session of the Board approved the resolution for Wu Bingyu's resignation from executive Director of the Company.

IV Directors, Supervisors and Senior Management and the Staff

II. Major career histories of Directors, Supervisors and Senior Management and their positions (continued)

1. Brief Biographies of Directors (continued)

(2) Brief biographies of non-executive Directors of the Company

Mr. Gan Zhihe had held positions of head of Technical Development Department of National Construction Material Bureau, Principal of China Construction Material Institute, vice chief of Technical Equipment Department of National Commission of Economics and Commerce, director of Investment and Planning Department of National Commission of Economics and Commerce, vice chief secretary of National Commission of Economics and Commerce, and vice chief secretary of National Development and Reformation Committee, etc. He is also an independent director of Xinjiang Tianshan Cement Co., Ltd. and is currently a non-executive Director of the Company.

Mr. Zhao Wei had held positions of director of Paper Manufacturing Department of Minister of Light Industry and deputy director of the paper making industry management office of China Light Industry Association (中國輕工總會造紙工業管理辦公室), and is currently vice president and general secretary of the China Paper Association, independent non-executive director of Guangdong Guanhao High-Tech Co., Ltd. and Qunxing Paper Holdings Co. Ltd., a Hong Kong listed company. He is currently a non-executive Director of the Company.

Mr. Cao Chunyu is currently the vice president of China National Pulp & Paper Research Institute, deputy general manager of China Paper Production Development Company and a member of the Academic Committee of China Technical Association of Paper Industry. He also serves as an independent director of Mudanjiang Hengfeng Paper Co., Ltd. and a non-executive Director of the Company.

(3) Brief biographies of independent non-executive Directors

Mr. Diao Yuntao previously held positions of vice executive officer of Accounting Department of Financial Bureau of Shandong Province, executive officer of Local Taxation Bureau office of Shandong Province and president of Shandong Province Qilu CPAs. He is currently the vice chairman of Wanlong Asia CPAs and independent director of Guangdong Golden Horse Tourism Group Stock Co., Ltd. Mr. Diao became an independent non-executive Director of the Company in April 2003.

Mr. Wang Zhihua had held the positions of tutor for Accounting of Shandong Economic College, director and secretary of Institute of Economics, Shandong Electricity Academe. Mr. Wang is currently the deputy chief economist and general manager of capital operation department of Luneng Group Co., Ltd., and concurrently serves as a director of Shandong Luneng Taishan Cable Co., Ltd., Guangdong Golden Horse Tourism Group Stock Co., Ltd. and Tianjin Guangyu Development Co., Ltd., as well as an independent director of Wuzhou Minovo Co., Ltd. He became an independent non-executive Director of the Company in April 2003.

IV Directors, Supervisors and Senior Management and the Staff

II. Major career histories of Directors, Supervisors and Senior Management and their positions (continued)

1. Brief Biographies of Directors (continued)

(3) Brief biographies of independent non-executive Directors (continued)

Ms. Zhou Chengjuan was assigned to the School of Finance Taxation & Public Administration of Shandong University of Finance in 1987, and is now deputy head of Institute of Public Finance and Taxation of Shandong University of Finance. She became an independent non-executive Director of the Company in April 2003.

Ms. Wang Yumei had held the positions of committee member of the 6th and 7th People's Political Consultative Committee of Haidian District, Beijing City and a committee member of the Committee for Social and Legal Affairs. Ms. Wang is currently the vice president of the department of insurance of the Central University of Finance and Economics, a standing director of the Labor Science Education Branch of the China Association for Labor Studies and a committee member of the Beijing City Economic Committee of the China National Democratic Construction Association, etc. She became an independent non-executive Director of the Company in April 2007.

Mr. Lau Ying Kit was the chief financial officer and company secretary of two listed companies, and is now the chief financial officer and company secretary of C Y Foundation Group Limited (a Hong Kong listed company) and an independent non-executive director of Kingdom Holdings Limited (a Hong Kong listed company). Mr. Lau became an independent non-executive Director of the Company in April 2007.

2. Brief biographies of Supervisors of the Company

Mr. Gao Junjie, who joined the Company in 1994, had held the positions of the chief officer of the legal section, chief officer of auditing department and chief officer of capital operations department, etc. He is now the chairman of supervisory committee, assistant to general manager, supervisor of Chenming Holdings and supervisor of Shouguang Henglian Enterprise Investment Co. Ltd.

Ms. Wang Ju, who joined the Company in 1987, had held the positions of deputy chief officer and chief officer of manufacturing section, deputy manager and general manager of branch company, assistant to the general manager and deputy general manager of Chenming Holdings. She is now a Supervisor of the Company and the vice president of the workers' union.

IV Directors, Supervisors and Senior Management and the Staff

II. Major career histories of Directors, Supervisors and Senior Management and their positions (continued)

2. Brief biographies of Supervisors of the Company (continued)

Ms. Yang Hongqin, who joined the Company in 1987, held the positions of the deputy chief and chief officer of quality control section, the chief of after sale services department and manager of property management company. She presently serves as a Supervisor of the Company and assistant to general manager of Shandong Chenming Power Supply Holdings. Co., Ltd.

Mr. Zhao Shujun, who joined the Company in 1997, had held the positions of the deputy chief of the party office, deputy chief of the training department and the deputy chief of the human resources department, etc. He is now a Supervisor of the Company and the deputy chief of the party group department. On 8 April 2009, the Ninth Meeting of the Fifth Session of the Supervisory Committee approved the resolution for Zhao Shujun's resignation from Supervisor of the Company.

Mr. Liu Wenzheng, who joined the Company in 1993, had held the positions of the chief officer of financial department of Shandong Chenming Paper Group Qihe Paperboard Co., Ltd. and the deputy chief officer and chief officer of audit department etc. He is currently a Supervisor of the Company. The Ninth Meeting of the Fifth Session of the Supervisory Committee approved the resolution for Liu Wenzheng's resignation from Supervisor of the Company.

3. Brief biographies of Senior Management of the Company

Mr. Wang Baoliang held the positions of secretary, deputy chief, deputy chief of Bureau of Investigation, deputy chief of the Office and deputy secretary-general of the committee office of Shouguang City, etc. He joined the Company in October 2003, and currently serves as deputy general manager of the Company and director of Chenming Holdings.

Mr. Geng Guanglin, who joined the Company in 1992, had held the positions of chief of manufacturing section, deputy general manager of Chibi Chenming Paper Co., Ltd, the chairman of Wuhan Chenming Hanyang Paper Holdings Co., Ltd. and chairman of Jilin Chenming Paper Co., Ltd.. He is now a deputy general manager of the Company.

Mr. Ren Wei held the positions of credit teller, deputy chief of credit section, deputy manager of international business department, chief of operation department, assistant to president, deputy president and president of Industrial and Commercial Bank, Shouguang City Branch etc. He joined the Company in July 2004 and currently serves as a deputy general manager of the Company.

IV Directors, Supervisors and Senior Management and the Staff

II. Major career histories of Directors, Supervisors and Senior Management and their positions (continued)

3. Brief biographies of Senior Management of the Company (continued)

Ms. Li Xueqin, who joined the Company in 1987, had held the positions of the chief of audit department, the vice chairman of the Supervisory Committee, etc.. Ms. Li has been a deputy general manager of the Company and a director of Chenming Holdings since March 2003. Ms. Li Xueqin is the spouse of Mr. Chen Hongguo, chairman of the Company.

Mr. Hao Yun, who joined the Company in 1984, had held the positions of secretary of the communist youth league of the Company, chief of the labor & personnel department, chief of shares and securities office and assistant to the general manager, etc. He is currently a deputy general manager of the Company and secretary to the Board.

Mr. Wang Zaiguo, who joined the Company in 1987, had held the positions of the deputy chief of office, assistant to the general manager, chief of logistics department of our Company, manager of hotel, deputy general manager of Chenming Holdings, Supervisor of the Company, etc. He is now a deputy general manager of the Company and the chairman of Zhanjiang Chenming Arboriculture Co., Ltd.

Mr. Wang Shihong had held the positions of deputy secretary of China National Development and Planning Committee, general manager of administration department of Fuxing Pulp Co., Ltd., head of Office of Party Committee and assistant to the general manager of China Gaoxin Investment Group Corp. He became a deputy general manager of the Company in March 2006.

Mr. Fang Lijun, who joined the Company in 1991, had been the manager and the assistant to the general manager of the Beijing branch office of the Company and the general manager of the sales office etc.. He currently serves as a deputy general manager of the Company.

Mr. Meng Feng, who joined the Company in 1992, had held the positions of deputy general manager of the Company, general manager of Jiangxi Chenming Paper Co., Ltd., chairman of printing paper company and chairman of news press paper company, etc. He is currently a deputy general manager of the Company and a director of Chenming Holdings.

Mr. Han Chunlai, who joined the Company in 1983, had held the positions of a manager of branch supplying company and the chief representative of the sales management section. He is currently a deputy general manager of the Company and concurrently serves as manager of paperboard products in sales office.

IV Directors, Supervisors and Senior Management and the Staff

II. Major career histories of Directors, Supervisors and Senior Management and their positions (continued)

3. Brief biographies of Senior Management of the Company (continued)

Mr. Liu Junwu, who joined the Company in 2002, had held the positions of financial controller of Jilin Paper Holdings Company Limited, chief accountant of Shandong Chenming Paper Group Qihe Paperboard Co., Ltd., chief of the financial department of the Company, assistant to the general manager and financial controller of the Company. On 8 April 2009, the Twelfth Meeting of the Fifth Session of the Board approved the resolution for Liu Junwu's resignation from chief financial officer of the Company.

Mr. Xia Guangchun, who joined the Company in 1989, had held the positions of deputy general manager of Wuhan Chenming Hanyang Paper Co. Ltd., general manager of Shandong Chenming Power Supply Holdings. Co., Ltd., party committee secretary of Jilin Chenming Paper Co., Ltd and deputy general manager of the Company. On 8 April 2009, the Twelfth Meeting of the Fifth Session of the Board approved the resolution for Xia Guangchun's resignation from deputy general manager of the Company.

IV Directors, Supervisors and Senior Management and the Staff

III. Securities interests held by Directors, Supervisors and Senior Management under the SFO of Hong Kong

As at 31 December 2008, interests of the Company or its associated corporations (within the meaning of the Part XV of SFO) held by each of the Directors, Supervisors and Senior Management of the Company under section 352 of the SFO are set out as follows:

The Company

Name	Position	Number of shares (A shares) held at the end of the reporting period (shares)
Directors		
Chen Hongguo (Note 1)	Chairman	6,334,527
Yin Tongyuan	Executive Director and general manager	3,231,520
Li Feng	Executive Director	471,818
Hou Huancai	Executive Director	628,915
Zhou Shaohua	Executive Director	123,007
Xing Fangtong	Executive Director	355,561
Wu Bingyu	Executive Director	428,107
Gan Zhihe	Non-executive Director	—
Zhao Wei	Non-executive Director	—
Cao Chunyu	Non-executive Director	—
Diao Yuntao	Independent non-executive Director	—
Wang Zhihua	Independent non-executive Director	—
Zhou Chengjuan	Independent non-executive Director	—
Wang Yumei	Independent non-executive Director	—
Lau Ying Kit	Independent non-executive Director	—
Supervisors		
Gao Junjie	Supervisor	39,606
Wang Ju	Supervisor	—
Yang Hongqin	Supervisor	—
Zhao Shujun	Supervisor	—
Liu Wenzheng	Supervisor	—

IV Directors, Supervisors and Senior Management and the Staff

III. Securities interests held by Directors, Supervisors and Senior Management under the SFO of Hong Kong (continued)

Associated corporations

Name	Position	Name of associated corporations	Number of shares held at the beginning of the reporting period (shares)	Change during the period +/-	Number of shares held at the end of the reporting period (shares)
Chen Hongguo (Note 2)	Chairman	Shouguang Chenming Holdings Company Limited	48,000,000	183,000,000	231,000,000
Li Feng	Executive Director	Qihe Chenming Waste Collection Co., Ltd.	10,000	—	10,000

Note 1: Save for the 6,334,527 A shares held personally, Chen Hongguo is deemed to be interested in the 429,348 A shares held by his spouse, Li Xueqin.

Note 2: Chen Hongguo and his spouse, Li Xueqin, collectively hold 43% equity interests in Shouguang Henglian Enterprise Investment Co. Ltd., (hereinafter referred to as “Shouguang Henglian”), as a result, Shouguang Henglian is deemed to be controlled by Chen Hongguo. As such, the 231,000,000 shares in Chenming Holdings (approximately 13.71% of the total share capital of Chenming Holdings) held by Shouguang Henglian is also deemed to be held by Chen Hongguo.

Save as disclosed above, as at 31 December 2008, none of each of the Directors, Supervisors or chief executives of the Company had any interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations which were required to be filed in the register of the Company required to be maintained pursuant to section 352 of the SFO or which were required to be notified to the Company and the Hong Kong Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers as contained in Appendix 10 to the Rules Governing the Listing of Securities on the Hong Kong Stock Exchange (hereinafter referred to as the “Hong Kong Listing Rules”).

As at 31 December 2008, none of each of the Directors, Supervisors or chief executives or their respective spouses or children under the age of 18 held or exercised any rights to subscribe for the share capital or debentures of the Company or its associated corporations.

IV Directors, Supervisors and Senior Management and the Staff

IV. Service contracts with Directors and Supervisors

None of the Directors or Supervisors had entered into service contracts with the Company which is not determinable by the Company within one year without payment of compensation other than statutory compensation.

V. Contractual interests of Directors and Supervisors

None of the Directors or Supervisors directly or indirectly held any beneficial interests in the material contracts entered into or performed by the Company during the year ended 31 December 2008.

VI. Purchase of shares or interests in debentures

At no time during the year was the Company or any of its subsidiaries a party to any arrangement to enable the Directors or Supervisors of the Company to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate.

VII. Annual remunerations of Directors, Supervisors and Senior Management

1. The remunerations of directors, Supervisors and Senior Management are determined by the remuneration committee of the Board of the Company, which will submit the same to the Board for approval and execution.
2. Factors determining the remunerations of the Directors and Senior Management include: actual profitability of the Company, position held, workload undertaken and interests created by the individual. Based on the principles of personnel stability and combination of incentives and restrictions, annual remuneration policy categorized by position is adopted on Directors and Senior Management.

Fixed annual remuneration policy is adopted on Supervisors. The annual remunerations of Supervisors assuming specific managerial duties in the Company are determined by the meetings of the management of the Company based on the specific managerial duties assumed by them.

3. As approved on the 2006 annual general meeting, the Company will pay each of the independent non-executive Directors and non-executive Directors of the Company annual allowance of RMB40,000 – RMB100,000 (after tax). The travel expenses for attending board meetings and shareholders' meeting and fees incurred reasonably in the performance of their duties under the Articles of the Associations by independent non-executive Directors and non-executive Directors are reimbursed as expensed.
4. For the total remunerations received from the Company by Directors, Supervisors and Senior Management in 2008, please refer to Part I of this section.

IV Directors, Supervisors and Senior Management and the Staff

VIII. Pre-emptive rights

In accordance with the Articles of Associations and the PRC laws, there are no rules requiring the Company to grant existing shareholders pre-emptive rights on newly issued shares of the Company in proportion to their shareholdings.

IX. Change of Directors, Supervisors and Senior Management

1. On 11 April 2008, upon the approval of the seventh meeting of the fifth session of the Board, Mr. Meng Feng and Mr. Han Chunlai were appointed as deputy general managers of the Company. For details, please refer to the relevant announcements published on China Securities Journal, Hong Kong Commercial Daily and <http://www.cninfo.com.cn> on 15 April 2008.
2. On 18 July 2008, upon the approval of the second extraordinary meeting of the fifth session of the Board, Mr. Dong Jianwen resigned from his duties as deputy general manager due to personal reasons. For details, please refer to the relevant announcements published on China Securities Journal, Hong Kong Commercial Daily, <http://www.cninfo.com.cn> and Hong Kong Stock Exchange's website (<http://www.hkex.com.hk>) on 19 July 2008.

X. Personnel of the Company and remuneration policy

At the end of the reporting period, the Group had 17,163 employees in aggregate, including 12,467 production staff, 524 sales staff, 1,120 technical staff, 288 financial staff, 908 administrative staff and 1,856 other staff. By level of education, there were 711 employees with bachelor's degree or above, 2,051 employees with college degree, 4,254 employees with technical secondary school education and 10,147 employees with high school, technical school education and levels below technical secondary school education.

The Company had obligations for 0 ex-employees or retired employees, including employees of subsidiaries. The remuneration of the employees of the Company includes their salaries, bonuses and other fringe benefits. Subject to the relevant laws and regulations of the PRC, the Company adopts different standards of remuneration for different employees, which are determined based on their performance, experience, position, etc. Details of the remuneration of employees of the Group in 2008 are set out in Note 9 to the financial statements prepared in accordance with the International Financial Reporting Standards.

Meanwhile, employees of the Group in the PRC participate in state-managed retirement benefit schemes operated by local governments. The Group is required to contribute a specified percentage of the employees' payroll costs to the retirement benefit scheme to fund the benefits. Details of the employee pension benefits provided by the Group are set out on Note 9 of the financial statements prepared in accordance with the International Financial Reporting Standards.

V Corporate Governance Report

I. Disclosures as required by China Securities Regulatory Commission

(I) Corporate Governance

Under the requirement of Company Law (《公司法》), Securities Law (《證券法》), Code of Corporate Governance for Listed Companies (《上市公司治理準則》), listing rules of Shenzhen Stock Exchange (《深圳證券交易所股票上市規則》), Hong Kong Listing Rules and the related requirements as required by China Securities Regulatory Commission, the Company further established and optimized its legal person governance structure in the reporting period. The Company operated in accordance with the practices stipulated in Procedural Rules of Shareholders Meetings (《股東大會議事規則》), Procedural Rules of Board Meetings (《董事會議事規則》), Procedural Rules of Supervisory Committee Meetings (《監事會議事規則》) and Information Disclosure Criteria (《信息披露管理制度》). The corporate governance of the Company was in compliance with the requirements of Code of Corporate Governance for Listed Companies (《上市公司治理準則》).

In 2007, the Company seriously conducted special corporate governance activities in light of its actual situation in strict compliance with the requirements and integrated arrangements relating to special corporate governance activities of listed companies of China Securities Regulatory Commission, China Securities Regulatory Commission Shandong Bureau, and Shenzhen Stock Exchange, as well as the laws and regulations such as Company Law (《公司法》) and Securities Law (《證券法》), the Articles of Association of the Company and the requirements of internal systems such as the Procedural Rules of Shareholders Meetings (《股東大會議事規則》), Procedural Rules of Board Meetings (《董事會議事規則》), Procedural Rules of Supervisory Committee Meetings (《監事會議事規則》). The activities were completed in three stages including self investigation, public inquiry and rectification. The governance standard of the Company was fully reviewed, summarized and enhanced. The Company made timely rectification based on the issues discovered in self investigation and the consolidated appraisal and rectification suggestions on corporate governance from China Securities Regulatory Commission and China Securities Regulatory Commission Shandong Bureau. The Company timely revised and improved the Connected Transaction Criteria (《關聯交易管理制度》), Information Disclosure Criteria (《信息披露管理制度》), General Manager Working Criteria (《總經理工作細則》), Internal Control Criteria (《內部控制制度》), Independent Director Administration Criteria (《獨立董事管理辦法》), Secretary of Board Working Criteria (《董事會秘書工作細則》), and Reception and Promotion Criteria (《接待和推廣工作制度》). All of these regulations were examined and approved at the second meeting of the fifth session of the Board.

V Corporate Governance Report

I. Disclosures as required by China Securities Regulatory Commission (continued)

(I) Corporate Governance (continued)

In 2008, according to the requirements and integrated arrangements of China Securities Regulatory Commission Announcement [2008] No. 27 and the Notice Regarding the Furthering of Self-Inspection Procedures of Works Related to the Enhancement of Special Governance Matters in Listed Companies (《關於做好加強上市公司治理專項活動自查階段有關工作通知》),《關於做好加強上市公司治理專項活動自查階段有關工作通知》, Notice Regarding Further Regulation of Behavior Relating to Preventing of Recurrence of Embezzling of Funds in Listed Companies by Substantial Shareholders (Lu Zheng Jian Gong Si Zi [2008] No.41)《關於進一步規範相關行為防止大股東佔用上市公司資金問題復發的通知》(魯證監公司字[2008] 41號) and Implementation Proposal for the Special Campaign in Shandong Jurisdiction for Prevention of Embezzling of Funds in Listed Companies by Substantial Shareholders and Related Parties (Lu Zheng Jian Gong Si Zi [2008] No.42)《山東區防止大股東及關聯方佔用上市公司資金行為專項活動實施方案》(魯證監公司字[2008] 42號) issued by China Securities Regulatory Commission Shandong Bureau, the Company continued to conduct special corporate governance activities based on the achievements of special corporate governance activities in 2007 and conducted self investigation and rectification in light of the existing issues relating to corporate governance. On 18 July 2008, the second extraordinary meeting of the fifth session of the Board considered and approved its rectification report on corporate governance and the resolutions regarding to the establishment of the Special System to Take Precautions against Controlling Shareholders and Related Parties from Embezzling the Company's Fund《防範控股股東及關聯方佔用公司資金專項制度》. On 19 July 2008, the related resolution announcement was published on China Securities Journal, Hong Kong Commercial Daily, www.cninfo.com.cn and the Hong Kong Stock Exchange's website (<http://www.hkex.com.hk>). The full text of rectification report on corporate governance and the Special System to Take Precautions against Controlling Shareholders and Related Parties from Embezzling the Company's Fund《防範控股股東及關聯方佔用公司資金專項制度》was published on www.cninfo.com.cn and the Hong Kong Stock Exchange's website (<http://www.hkex.com.hk>).

V Corporate Governance Report

I. Disclosures as required by China Securities Regulatory Commission (continued)

(II) Performance of the independent non-executive Directors

In the reporting period, each of the independent non-executive Directors continued to suggest constructive opinion on the material matters relating to operations and management and internal control of the Company. They issued their independent opinion on related matter pursuant to related requirements, thus raising the science and objectiveness of Board decisions. Attendance of independent non-executive Directors at Board meetings in 2008 is as follows:

Name of independent non-executive Directors	Number of Board meetings requiring Attendance			
	Attendance in person	Attendance by proxy	Absence	
Liu Yingjie	9	9	0	0
Wang Yumei	9	9	0	0
Diao Yuntao	9	9	0	0
Wang Zhihua	9	9	0	0
Zhou Chengjuan	9	9	0	0

In the reporting period, independent non-executive Directors of the Company issued their independent opinions on the connected transactions pursuant to the related laws and regulations, they raised no objection opinion on the proposals of Board meetings or other issues.

(III) Particulars about the separation of businesses, personnel, assets, organizations, and finance from the controlling shareholder

1. In terms of business: The Company was completely independent from the controlling shareholder, and had its independent and complete business operation capability.
2. In terms of personnel: The labour, personnel and salary management were completely separated from the controlling shareholder.
3. In terms of assets: There was only shareholding relationship between the Company and Chenming Holdings. The assets of the Company were completely separated from those of the controlling shareholder.
4. In terms of organization: The Company had a mature and independent organization structure, which was established according to the legal processes and the business practice of the Company. It was completely separated from that of the controlling shareholder.
5. In terms of finance: The Company had its own accounting department, accounting system, financial management system, and bank accounts. The controlling shareholder never interfered in the financial activities of the Company.

V Corporate Governance Report

I. Disclosures as required by China Securities Regulatory Commission (continued)

(IV) Internal Control of the Company

1. Internal control overview

The Company established the procedural rules for shareholders' meetings, board meetings, and the Supervisory Committee meetings to ensure their decision-making, execution, and supervision duties to be carried out effectively. Meanwhile, the Company also established the Strategic Committee, Nomination Committee, Audit Committee and Remuneration and Assessment Committee of the Board. In accordance with their respective working criteria, they assumed the functions of discussing the material matters and decision making, raising the science and professionalism of Board decisions.

Internal administration departments were established to monitor the set-up, improvement and implementation of internal control systems. Audit Committee reviewed and monitored the material connected transactions.

The Company established a complete internal control system covering production management, financial management, connected transactions, external guarantee, use of proceeds, and material investment of the Company and its subsidiaries.

2. Control over major activities of the Company

(1) Administration of and control over controlling subsidiaries

The Company managed its controlling subsidiaries according to the related laws and regulations and relevant listing rules of the Shenzhen Stock Exchange and the Hong Kong Stock Exchange. According to the requirements of Company Law, subsidiaries established their respective board of directors and supervisory committee and lawfully conducted management and supervision duties. Sound operation and financial management systems were established according to the practices of the Company's business operations. By exercising its rights as a shareholder, the Company controlled the director and key management nomination process and decision-making process of the subsidiaries. As a result, the Company was assured that its subsidiaries were under firm control and the decisions and systems of the Company were effectively, promptly and consistently implemented within its subsidiaries. So all the tasks within the Company and its subsidiaries were consistently dealt with.

V Corporate Governance Report

I. Disclosures as required by China Securities Regulatory Commission (continued)

(IV) Internal Control of the Company (continued)

2. Control over major activities of the Company (continued)

(1) Administration of and control over controlling subsidiaries (continued)

According to the related requirements of Shenzhen Stock Exchange Guidelines on Internal Controls of Listed Companies (《深圳證券交易所上市公司內部控制指引》), the Company set up and improved the related systems such as Internal Control System, Measures on Administration of Subsidiaries and Measures on Administration of Expatriate Senior Management based on the strategic development, the requirement of the management and the characteristics of various subsidiaries, and persuaded the subsidiaries to set up corresponding operation plans, risk management processes and required the subsidiaries to set up the system of shareholders' meeting, board meetings and supervisory committee meetings modeling on their parent company and optimize their corporate governance structure. The Company seriously implemented the material matters reporting and approval system to strengthen its control over its subsidiaries.

(2) Administration of and control over connected transactions

The Articles of Association of the Company has provided clear rules for the authorities of the Board and Shareholders' Meeting to examine connected transactions, the auditing procedure, and waiving of voting by related Directors and shareholders. According to Shenzhen Stock Exchange Guidelines on Internal Controls of Listed Companies (《深圳證券交易所上市公司內部控制指引》), the Company prepared its Administration on Connected Transactions, which set out the regulations regarding classification, identification, contract execution and disclosure of connected transactions. The Company also set up the Special System to Take Precautions against Controlling Shareholders and Related Parties from Embezzling the Company's Fund (《防範控股股東及關聯方佔用公司資金專項制度》). None of capital, assets, or other resources of the Company has been appropriated or transferred by the controlling shareholder and its related persons. All connected transactions were conducted under the principle of faithfulness, fairness, voluntary, and open and their information was disclosed according to the disclosure requirements and published in the annual report of the Company. No action was conducted which was harmful to the benefits of the Company and the shareholders. Overall, the connected transactions of the Company were in compliance with Shenzhen Stock Exchange Guidelines on Internal Controls of Listed Companies (《深圳證券交易所上市公司內部控制指引》) and the related laws and regulations.

V Corporate Governance Report

I. Disclosures as required by China Securities Regulatory Commission (continued)

(IV) Internal Control of the Company (continued)

2. Control over major activities of the Company (continued)

(3) Administration of and control over external guarantee

The authority of external guarantee was stipulated by the Articles of Association and the Company had implemented the requirements relating to aggregate amount of external guarantees according to the Rules Governing Listing of Stocks on Shenzhen Stock Exchange. Meanwhile the Company had set up “The Working Procedures of Financing and Guarantee”. Except for guarantees provided to the subsidiaries, the Company made no external guarantees. Overall, external guarantees of the Company were in compliance with Shenzhen Stock Exchange Guidelines on Internal Controls of Listed Companies (《深圳證券交易所上市公司內部控制指引》) and the related laws and regulations.

(4) Administration of and control over using of financing proceeds

The Company had set up Administration Criteria of Financing Proceeds to govern the use, approval, deposit, change of use, report and supervision of financing proceeds and liabilities. Financing proceeds were used according to their intended usage. The Company disclosed the information about the use of financing proceeds in compliance with related requirements.

(5) Administration of and control over capital

The Company had set up Capital Administration Criteria, Financing and Guarantee Procedures, Reporting Rules of Material Financial Issues, and Administrative Rules of Account Receivable, which set up strict procedures for authorization and approval of receipts and payments of monetary capital, separated the incompatible positions in the process of monetary capital operation and established a checking system in the related organization and staff. The Company set up procedures such as those for approval of receipts and payments of monetary capital and strictly implemented verification and investigation of receipts and payments of monetary capital.

(6) Administration of and control over material investments

Material investment operations were conducted under principles of lawfulness, cautiousness, safety and effectiveness. The Articles of Association has clearly set out the authorities of shareholders’ meeting and the Board on approval of major investment operations. The Company has been focusing on its main businesses and made no material investment other than the main businesses so far.

V Corporate Governance Report

I. Disclosures as required by China Securities Regulatory Commission (continued)

(IV) Internal Control of the Company (continued)

2. Control over major activities of the Company (continued)

(7) Administration of and control over finance

In accordance with the laws and regulations such as Company Law, Accounting Law, and Accounting Standards for Business Enterprises and their supplementary requirements, the Company prepared its Financial Management Rules, which set out the procedures and rules for major financial decisions, standardized the procedures for accounting evidence, books and reports, defined the responsibilities of accounting staff and set up the evidence flow. Transactions were implemented with evidence timely prepared and delivered to the accounting department and filing department for record and filing. Meanwhile, the records were compared with the corresponding accounting entries to build up a sound internal control system of accounting in the form of computerization. The Company introduced ERP system as the common platform for the management techniques and coordinating of the internal administration. The platform effectively standardized corporate and foundation information and business operations, increased the management efficiency and timely provided the management of the Company and the Board with related information. The financial system of the Company is sound and complete and in compliance with the requirements of related laws and regulations.

(8) Administration of and control over information disclosure

The Company prepared the Information Disclosure Criteria, Internal Reporting of Material Information, Investor Relationship Management Criteria, and Investor Reception and Promotion Criteria, which set out the extent, reporting, examination, disclosure, and confidentiality of material information. China Securities Journal, Hong Kong Commercial Daily, www.cninfo.com.cn and Hong Kong Stock Exchange website were the designated information disclosure media of the Company, through which the information of the Company was first disclosed. The Company also timely released its public information through its own website to communicate with the investors. Reception of visitors and online road shows were lawfully conducted to ensure open, just and fair information disclosure.

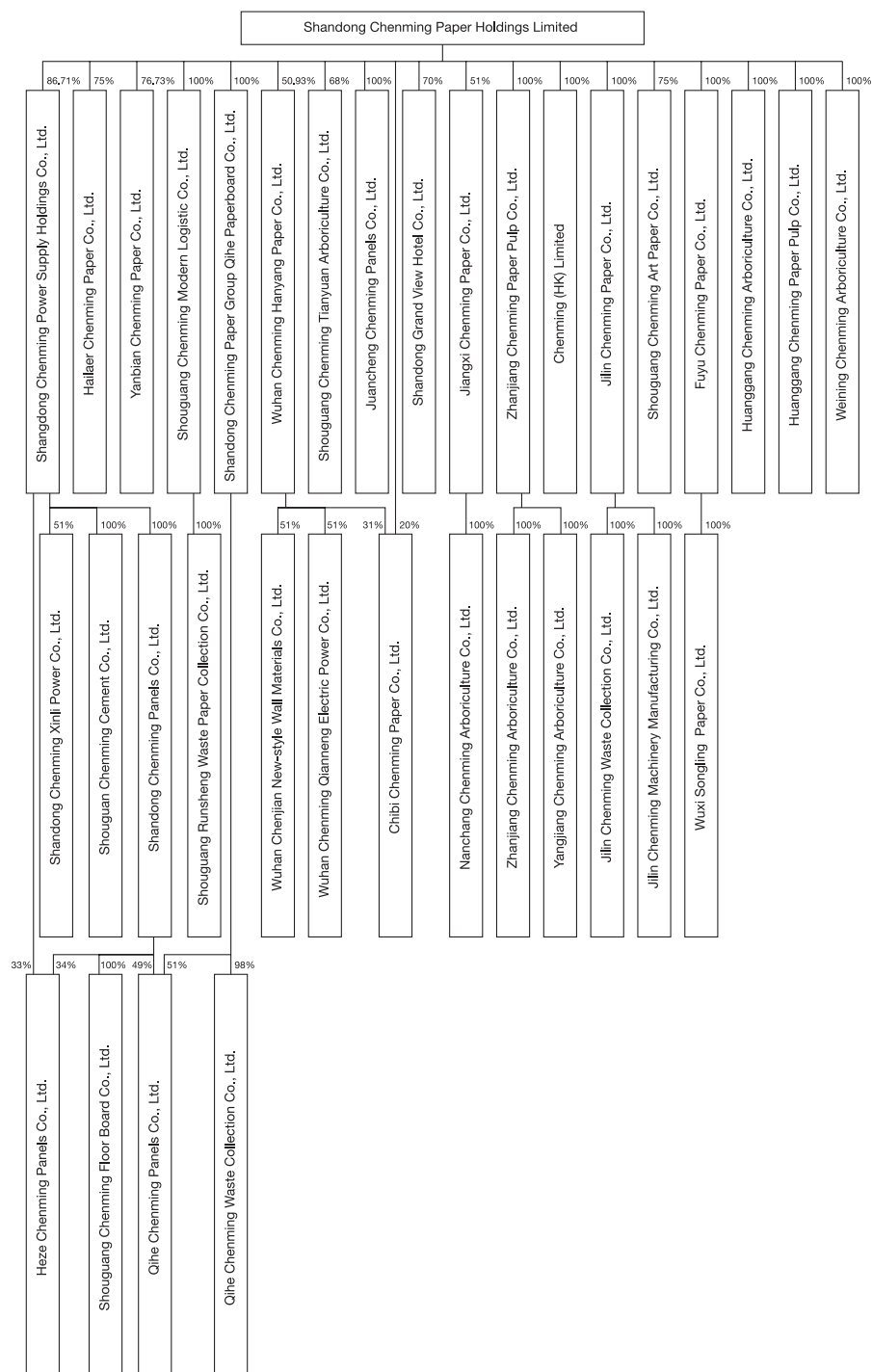
V Corporate Governance Report

I. Disclosures as required by China Securities Regulatory Commission (continued)

(IV) Internal Control of the Company (continued)

2. Control over major activities of the Company (continued)

(9) Shareholding structure of the subsidiaries of the Company



V Corporate Governance Report

I. Disclosures as required by China Securities Regulatory Commission (continued)

(IV) Internal Control of the Company (continued)

3. Implementation of internal control system

The Company performed inspection and monitoring operation on implementation of internal control system. The planning department was in charge of inspecting and monitoring the internal control system and made amendments from time to time to ensure effective implementation of the internal control system and normal production and operating activities. The Company took a top-down approach in the annual inspection of its subsidiaries to assess the compliance of the financial system and financial audit of the subsidiaries. The audit department of the Company performed random audit on the financial position the Company and its subsidiaries.

4. Overall assessment on the internal control system

The Board is of opinion that the internal control system of the Company and its measures were comprehensive and reasonable and practically effective. The internal control system was consistent with the actual situation of the Company and was implemented seriously and effectively. It proved to be effective as illustrated by its practices from many years without significant fault.

After the special corporate governance activities in 2008, the internal control system became more comprehensive. Directors, Supervisors and the Senior Management of the Company became more aware of the importance of corporate governance and standard operation, thus laying a foundation for continuous improvement on corporate governance.

5. Supervisors and independent non-executive Directors of the Company made the following self-evaluation comments on the internal controls of the Company:

The internal control measures of the Company are in compliance with the requirements of the relevant regulations and the securities regulatory authorities, while are also appropriate taking into account of the prevailing practical needs of the Company. The internal control measures of the Company provided better results in controlling of all the processes and integral parts of company management. The “Self-evaluation Report on Internal Controls” adopted by the Company objectively reflected the actual circumstances of internal control within the Company and formed a comprehensive overview on the internal controls of the Company.

V Corporate Governance Report

I. Disclosures as required by China Securities Regulatory Commission (continued)

(v) Assessment and incentive mechanism for the Senior Management in the reporting period

The Senior Management of the Company is assessed monthly and annually. Monthly assessments were focused on the completion status of major tasks and working performance. It was carried out monthly by way of cross assessment and supervision among the related departments. Results of monthly assessments provided the basis for the annual assessment. The annual assessments were carried out by the Remuneration and Assessment Committee with reference to the results of monthly assessments and performances all over the year.

II. Disclosures as required by the Hong Kong Listing Rules

(I) In Compliance with the Code on Corporate Governance Practices

The Company maintained high standards of corporate governance through various internal controls. The Board reviewed the corporate governance practices of the Company from time to time to enhance the corporate governance standards of the Company.

The Company had fully complied with all the principles and code provisions of the Code on Corporate Governance Practices set out as Appendix 14 to the Hong Kong Listing Rules during the reporting period.

(II) Securities transactions by Directors

The Directors of the Company confirmed that the Company had adopted the Model Code for Securities Transactions by Directors of Listed Companies as set out in Appendix 10 to the Hong Kong Listing Rules. Having made adequate enquiries with all Directors and Supervisors of the Company, the Company was not aware of any information that reasonably suggested that the Directors and Supervisors had not complied with the requirements as stipulated in this code during the reporting period.

V Corporate Governance Report

II. Disclosures as required by the Hong Kong Listing Rules (continued)

(III) Board of directors

The board of directors of the Company are elected at the shareholders' meeting and held accountable to the shareholders' meeting, and shall exercise the following functions and powers: (1) to be responsible for convening shareholders' general meeting and to report on its work to the shareholders' meeting; (2) to carry out the resolutions of shareholders' meetings; (3) to decide on the business plans and investment proposals of the Company; (4) to formulate the proposed annual financial budget and final accounts of the Company; (5) to formulate the plan for profit distribution and the plan making up losses of the Company; (6) to formulate plans for the increase or reduction in the registered capital of the Company and for the issue and listing of Company's debentures or other securities; (7) to draft plans for material acquisition and repurchase of the Company's own shares; (8) to draft plans for the merger, division or dissolution or the change of formation of the Company; (9) to decide on external investment, acquisition and disposal of assets, pledge of assets, matter in relation to external guarantee, entrusted wealth management, connected transactions, etc. within the scope of mandate of the shareholders' meeting; (10) to decide on the establishment of the Company's internal management organization; (11) to employ or dismiss the manager or secretary to the board of directors of the Company; to employ or dismiss the Senior Management, such as the deputy general manager(s) and personnel in charge of financial affairs, as proposed by the general manager; and to decide on their remuneration and rewards and punishments; (12) to formulate the basic management system of the Company; (13) to formulate proposals for amending the Articles of Association; (14) to administrate matter related to information disclosure of the Company; (15) to propose to the shareholders' meeting for the engagement or replacement of accounting firm performing audit for the Company; (16) to review work reports from managers of the Company and to inspect on their work; and (17) to exercise the functions and powers as conferred upon by the Articles of Associations or the shareholders' meeting.

During the reporting period, the Board comprised seven executive Directors: Chen Hongguo (Chairman), Yin Tongyuan, Li Feng, Hou Huancai, Zhou Shaohua, Xing Fangtong, Wu Bingyu; three non-executive Directors: Gan Zhihe, Zhao Wei, Cao Chunyu; and five independent non-executive Directors: Diao Yuntao, Wang Zhihua, Zhou Chengjuan, Wang Yumei, Lau Ying Kit. Please refer to section IV of the Report for their brief biographies.

The Board is responsible for leading and monitoring the Company, and is on a whole responsible for the administration and supervision of company businesses to facilitate its success. Directors of the Company shall act objectively and make decisions in the interests of the Company. The operating management of the Company held regular meetings with the board of directors to discuss the ordinary business operations and performance of the Company, and carried out the relevant decisions of the board of directors.

V Corporate Governance Report

II. Disclosures as required by the Hong Kong Listing Rules (continued)

(III) Board of directors (continued)

During the reporting period, the Board held 9 meetings, 7 of which were regular meetings and 2 extraordinary meetings. All 15 Directors attended 9 Board meetings.

Name	Position	Attendance of the relevant meetings (attention required/attended)				Remuneration and assessment committee meetings
		Board meetings	Audit committee meetings	Nomination committee meetings		
I. Executive Directors						
Chen Hongguo	Chairman	9/9	Not applicable	1/1	1/1	
Yin Tongyuan	Vice chairman, general manager	9/9	Not applicable	1/1	1/1	
Li Feng	Director, sales director	9/9	Not applicable	Not applicable	Not applicable	
Hou Huancai	Director	9/9	Not applicable	Not applicable	Not applicable	
Zhou Shaohua	Director	9/9	Not applicable	Not applicable	Not applicable	
Xing Fangtong	Director	9/9	Not applicable	Not applicable	Not applicable	
Wu Bingyu	Director	9/9	Not applicable	Not applicable	Not applicable	
II. Non-executive Directors						
Gan Zhihe	Director	9/9	Not applicable	Not applicable	Not applicable	
Zhao Wei	Director	9/9	Not applicable	Not applicable	Not applicable	
Cao Chunyu	Director	9/9	2/2	Not applicable	Not applicable	

V Corporate Governance Report

II. Disclosures as required by the Hong Kong Listing Rules (continued)

(III) Board of Directors (continued)

Name	Position	Attendance of the relevant meetings (attention required/attended)				Remuneration and assessment committee meetings
		Board meetings	Audit committee meetings	Nomination committee meetings		
III.	Independent non-executive Directors					
	Diao Yuntao	Independent Director	9/9	2/2	1/1	1/1
	Wang Zihua	Independent Director	9/9	2/2	1/1	1/1
	Zhou Chengjuan	Independent Director	9/9	2/2	Not applicable	1/1
	Wang Yumei	Independent Director	9/9	Not applicable	1/1	Not applicable
	Lau Ying Kit	Independent Director	9/9	2/2	Not applicable	Not applicable

Save for those disclosed in the brief profile of Directors of the Company in the Report, none of the members of the Board had any financial, business, family relations or material connections with each other.

The Board held seven regular meetings during the year, each by giving a 14-day notice in advance to ensure that all Directors could participate in discussions of matters in the agenda. Reasonable prior notification was given for the other meetings of the Board to ensure all Directors could take time to attend.

All Directors had access to opinions and services of the secretary to the Board to ensure the procedures governing the Board and all applicable regulations and rules were complied with.

V Corporate Governance Report

II. Disclosures as required by the Hong Kong Listing Rules (continued)

(IV) Chairman and general manager

The chairman of the Company is Mr. Chen Hongguo and Mr. Yin Tongyuan is the general manager. Please refer to section IV of the Report for their brief biographies. During the year, there was clear delineation of duties between operation administration and company businesses functions of the Board, where power and authorizations were evenly allocated without concentration of power on any individual member.

The division of responsibilities between the chairman and general manager is well defined and duly set out in writing. According to the Articles of Association of the Company, the chairman shall exercise the following powers: (1) presiding over shareholders' meetings, and convening and presiding over Board meetings; (2) supervising and inspecting the implementation of the resolutions of the Board; (3) signing the shares, the securities and bonds issued by the Company; (4) signing important documents of the Board and other documents which are required to be signed by legal representative of the Company; (5) performing the powers of a legal representative; (6) nominating candidates for general manager for the Board; (7) exercising the special right to operate the Company in accordance with the laws and acting for the benefits of the Company in the event of emergency situation as a result of act of God or natural disaster, and reporting to the Board meetings and shareholders' meeting afterwards; and (8) exercising other powers authorized by the Board.

The general manager shall exercise the following powers: (1) in charge of the operation and management of the Company, and organizing the implementation of the resolutions of the Board; (2) organizing the implementation of the Company's annual business plans and investment plans; (3) drafting plans for the establishment of the internal organizational structure of the Company; (4) drafting the basic management system of the Company; (5) formulating specific rules and regulations for the Company; (6) proposing the appointment or dismissal of the deputy general manager and chief financial officer; (7) appointing or dismissing management personnel other than those required to be appointed or dismissed by the Board; (8) proposing the wages, welfare, rewards, and penalties of staff and to decide the appointment or dismissal of staff of the Company; (9) proposing the convening of extraordinary meeting of the Board; and (10) exercising other powers conferred by the Articles of Association of the Company and the Board.

V Corporate Governance Report

II. Disclosures as required by the Hong Kong Listing Rules (continued)

(V) Independent non-executive Directors

There are five independent non-executive Directors in the Board, which is compliance with the minimum requirement of the number of independent non-executive directors set out in the Hong Kong Listing Rules. Diao Yuntao and Lau Ying Kit, the independent non-executive Directors of the Company, have appropriate accounting or related financial management expertise, which is compliance with the requirement of Rule 3.10 of the Hong Kong Listing Rules. Please refer to section IV of the Report for their brief biographies. The Company has received from each of the independent non-executive Directors a confirmation of independence for the year pursuant to Rule 3.13 of the Hong Kong Listing Rules and considered all of the independent non-executive Directors to be independent during the year.

(VI) Terms of Directors

According to the Articles of Association of the Company, all Directors, including non-executive Directors, are elected at shareholders' meetings with a term of three years from April 2007 to April 2010. They may be re-elected for another term.

(VII) Directors' responsibility for the financial statements

The Directors acknowledged their responsibility to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company. The Directors believed that the Company had adopted and applied consistently appropriate accounting policies in preparing the financial statements in compliance with all related accounting standards.

(VIII) Audit committee

The audit committee of the Company comprises of four independent non-executive Directors and a non-executive Director. Its primary duties are serving as a communication media between internal and external audit and the related review and supervision. The chief member of the audit committee is Diao Yungtao, an independent non-executive Director, and other members are Lau Ying Kit, Zhou Chengjuan, Wang Zhihua and Cao Chunyu. Diao Yuntao has appropriate professional qualifications or appropriate accounting or related financial management expertise, which is compliance with the requirement of the Hong Kong Listing Rules.

V Corporate Governance Report

II. Disclosures as required by the Hong Kong Listing Rules (continued)

(VIII) Audit committee (continued)

The primary duties of the audit committee of the Company are: (1) proposing the appointment or dismissal of the external auditors; (2) supervising the internal control system of the Company and its implementation; (3) serving as a communication media between internal and external audit; (4) auditing the financial information of the Company and its disclosures; (5) reviewing the internal control system of the Company and audit the significant connected transactions; and (6) dealing with other matters as delegated by the Board. The audit committee discussed with the management of the Company the accounting standards and practices adopted by the Group and discussed and reviewed this report, including the review of the financial statements of the Group for the year ended 31 December 2008 prepared in accordance with Accounting Standards for Business Enterprises and International Financial Reporting Standards respectively.

The works performed by the audit committee in the reporting period are detailed in the Directors' Report of the Report.

(IX) Remuneration and assessment committee

The Company set up a remuneration and assessment committee which comprised five Directors, including Diao Yungtao, the chief committee member, and other members, namely Chen Hongguo, Yin Tongyuan, Wang Zhihua and Zhou Chengjuan. Three members, including the chief member, are independent non-executive Directors, which is in compliance with Code of Corporate Governance Practice. The remuneration and assessment committee is primarily responsible for formulating the criteria of appraisal of the Directors and managers and conducting the appraisal, and studying and formulating the remuneration policy and package of the Directors and the Senior Management of the Company. The remuneration and assessment committee is accountable to the Board.

The primary duties of the remuneration and assessment committee of the Company are: (1) formulating the remuneration plan or package based on the major scope of work, duties and importance of the Directors and the management and the remuneration level of other counterparts; (2) formulating the remuneration plan or package which mainly includes but not limited to standards, procedures and a system for performance appraisals as well as major plans and a system for rewards and sanctions; (3) examine the performance of the Directors, excluding the independent non-executive Directors, and the Senior Management and conduct annual performance appraisals for them; (4) supervising the implementation of the remuneration policy of the Company; and (5) dealing with other matters as delegated by the Board.

The works performed by the remuneration and assessment committee in the reporting period are detailed in the Directors' Report of the Report.

V Corporate Governance Report

II. Disclosures as required by the Hong Kong Listing Rules (continued)

(X) Nomination committee

The Company set up a nomination committee which comprised five Directors, including Wang Zhiwa, the chief committee member, and other members, namely Chen Hongguo, Yin Tongyuan, Diao Yuntao and Wang Yumei. Three members, including the chief member, are independent non-executive Directors, which is compliance with Code of Corporate Governance Practice. The nomination committee is primarily responsible for selecting the candidates for directors and the management of the Company, determinating the selection criteria and procedure and making recommendations. The primary duties of the nomination committee are (1) advising the Board on the size and composition of the Board in light of the company's operating activities, asset scale and shareholding structure; (2) studying the selection criteria and procedure for Directors and the management and advising the Board on the same; (3) extensively identifying qualified candidates for Directors and the management; (4) examining candidates for Director and the management and advising on the same; (5) examining other Senior Management staff pending referral to the Board for decision on their employment and advising on the same; (6) dealing with other matters as delegated by the Board.

During the reporting period, the nomination committee studied the needs of the Company for new Directors and managerial personnel and identified suitable candidates for Director and managerial positions through various channels (including from the Group internally and from the human resources market). Upon acceptance of nomination by the nominated person, the nomination committee performed qualification review on preliminary candidates by holding meetings, review criteria include the academic qualifications, relevant experience and specialized skills of the preliminary candidates. One month prior to election of new Directors, nomination committee submitted recommendations and relevant materials of the directorial candidates to the Board; prior to engaging new Senior Management, the nomination committee submitted recommendations and relevant materials of the new Senior Management personnel to the Board.

The works performed by the nomination committee in the reporting period are detailed in the Directors' Report of the Report.

V Corporate Governance Report

II. Disclosures as required by the Hong Kong Listing Rules (continued)

(XI) Strategic committee

The Company set up a strategic committee which comprised seven Directors, including Chen Hongguo, the chief committee member, and other members, namely, Yin Tongyuan, Xing Fangtong, Wu Bingyu, Lau Ying Kit, Wang Yumei and Wang Zhihua. The strategic committee is primarily responsible for studying the long term strategic development and major investments of the Company and making recommendations.

The primary duties of the strategic committee are (1) conducting research and submitting proposals regarding the long term development strategic plan; (2) conducting research and submitting proposals regarding the financing plans for major investments which require approval from the Board as stipulated in the Articles of Association of the Company; (3) conducting research and submitting proposals regarding major capital operations and assets operation projects which require approval from the Board as stipulated in the Articles of Association of the Company; (4) conducting research and submitting proposals regarding other material matters that may affect the development of the Company; (5) carrying out examination on the implementation of the above matters; (6) dealing with other matters as delegated by the Board.

(XII) Remuneration for the auditors

The financial statements for 2008 prepared in accordance with Accounting Standards for Business Enterprises and International Financial Reporting Standards respectively by the Group were audited by Deloitte Touche Tohmatsu Certified Public Accountants Ltd and Deloitte Touche Tohmatsu. In 2008, the Company paid a total of RMB4,800,000 financial statements auditing and review fee to the auditors, of which, RMB4,200,000 was paid for auditing services rendered for the annual financial statements in 2008, and RMB600,000 was paid for review of the interim financial statements in 2008. The audit fees for the engagement of Deloitte Touche Tomatsu incurred during the Company's first issuance of H shares on the Hong Kong Stock Exchange in June 2008 was RMB7,000,000.

There was no change of auditors of the Company in the last three years.

V Corporate Governance Report

II. Disclosures as required by the Hong Kong Listing Rules (continued)

(XIII) Shareholders and shareholders' meeting are detailed in the section summarizing Shareholders' meeting in this Report.

(XIV) Supervisors and the Supervisory committee

The Supervisory Committee is accountable to the shareholders. It monitors the financial position of the Company and the performance of the Directors, managers and Senior Management of the Company as to whether they are in accordance with relevant requirements of the laws and regulations to protect the lawful rights of the Company and the shareholders. The Supervisory Committee comprises three shareholder representatives and two staff representatives. The shareholder representatives shall be elected and removed at a shareholders' meeting and the staff representatives shall be elected and removed democratically by the staff of the Company.

The works performed by the Supervisory Committee in the reporting period are detailed in the Supervisory Committee' Report of the Report.

VI. Particulars about the Shareholders' Meeting

I. Shareholders' annual meeting

The shareholders' annual meeting 2007 was held on 29 June 2008. Five resolutions regarding directors' reports, supervisory committee's report and independent non-executive directors' report of the Company for 2007, 2007 financial statements, profit distribution plan for 2007, proposal on appointing of certified public accountants were passed at the meeting. Related resolution announcements were published on China Securities Journal, Hong Kong Commercial Daily, <http://www.cninfo.com.cn> and Hong Kong Stock Exchange website (<http://www.hkex.com.hk>) on 1 July 2008.

II. Shareholders' extraordinary meetings

The shareholders' first extraordinary meeting was held on 11 April 2008. Three resolutions, among other things, regarding extension of the expiry date of the related matters on H shares issue, guarantee for the banking facilities granted to the subsidiaries of the Company and revision to the Articles of Association (draft) of the Company, related resolution announcements were published on China Securities Journal, Hong Kong Commercial Daily and <http://www.cninfo.com.cn> on 12 April 2008.

VII. Chairman's Statement

Dear valued shareholders,

On behalf of the Board, I present to you the annual results for 2008. During the year, the Group experienced rapid development in the first half year and the impacts of the financial crisis in the fourth quarter. Throughout 2008, the Group achieved satisfactory results.

Operating results

In 2008, the Group realized production of 3.17 million tonnes of paper products, representing a growth of 300,000 tonnes, or 10.45%, over 2007. Revenue under the Accounting Standards for Business Enterprises was RMB15,530 million, representing an increase of RMB365 million, or 2.41%, over 2007. Profit before tax was RMB1,555 million, up RMB66 million or 4.43% compared with 2007. Net profit attributable to the equity holders of the Company was RMB1,075 million, representing a growth of RMB108 million, or 11.13%, over 2007. In accordance with the International Financial Reporting Standards, revenue amounted to RMB15,431 million, representing an increase of RMB552 million over 2007 or a year-on-year increase of 3.71%. Profit before tax was RMB1,591 million, representing an increase of RMB67 million over 2007 or a year-on-year increase of 4.43%. Net profit attributable to equity holders of the Company was RMB1,102 million, representing an increase of RMB108 million over 2007 or a year-on-year increase of 10.89%.

Corporate governance

In 2008, according to the requirements and integrated arrangements of China Securities Regulatory Commission Announcement [2008] No. 27 (中國證券監督管理委員會公告[2008]27號文) and the Notice Regarding the Furthering of Self-Inspection Procedures of Works Related to the Enhancement of Special Governance Matters in Listed Companies (《關於做好加強上市公司治理專項活動自查階段有關工作通知》), Notice Regarding Further Regulation of Behavior Relating to Preventing of Recurrence of Embezzling of Funds in Listed Companies by Substantial Shareholders (Lu Zheng Jian Gong Si Zi [2008] No.41) (《關於進一步規範相關行為防止大股東佔用上市公司資金問題復發的通知》(魯證監公司字「2008」41號)) and Implementation Proposal for the Special Campaign in Shandong Jurisdiction for Prevention of Embezzling of Funds in Listed Companies by Substantial Shareholders and Related Parties (Lu Zheng Jian Gong Si Zi [2008] No.42) (《山東區防止大股東及關聯方佔用上市公司資金行為專項活動實施方案》(魯證監公司字「2008」42號)) issued by the Securities Regulatory Commission of Shandong Bureau, together with the principles and code provisions of the Code on Corporate Governance Practices set out in Appendix 14 to the Hong Kong Listing Rules, the Company consolidated upon the foundation of the special projects in connection with strengthening of corporate governance in 2007 to further implement special projects and promote corporate governance of the listed company. Meanwhile, we continued to conduct self-inspections and corrections on issued surrounding corporate governance; this ever-improving structure in corporate governance had laid down a solid foundation for our achievement of sound operating results.

VII. Chairman's Statement

Dividends distribution

Consistent with our long-term goal of pursuing the maximization of corporate values, the Group had always placed much emphasis on shareholders' benefits and returns. In view of the favorable operating results realized in 2008 and after considering the financial positions and cash flow conditions of the Group as a whole, the Board recommended a distribution budget for 2008 as follows: based on total share capital of 2,062,045,941 shares as of 31 December 2008, to distribute cash bonuses of RMB0.5 (tax included for A shares) per 10 shares to all shareholders, aggregating to RMB103,102,297.05 (tax included) of cash bonuses in this distribution, which would account for 10.59% of the net profit attributable to equity holders of the Company as set out in the combined financial statements prepared in accordance with Accounting Standards for Business Enterprises in 2008 after deducting statutory reserves. After such profit distribution, undistributed profit would be rolled over for distribution in subsequent years. As always, the Group will continue to stay focused in its long-term development and maximize returns for shareholders by delivering even better results.

Future development

As the extent and scope of influence under the global financial crisis is still highly uncertain, this will directly affect the pace of economic growth in China, and therefore make it difficult for the Company to accurately judge the development prospects of the papermaking industry. Nevertheless, as the papermaking industry in China is still undergoing a general direction of growth, the Board is of the opinion that: after the trough experienced in the fourth quarter of 2008, papermaking industry will begin to stabilize; while the price for upstream raw materials will remain low for a certain period, the price for paper products will be able to maintain a reasonable balanced point of profitability; following the implementation of the new environmental protection policies and renewed efforts in implementing policies related to the papermaking industry, small-to-medium papermaking enterprises will face expansion limitation, challenges in economy of scale and heavier costs for environmental protection in their future development, which will lead to higher degree of industry concentration that is beneficial to enterprises with larger structural scale. The Group will adhere strictly to its prescribed development strategies in an orderly manner, highlights of which are as follows:

Eliminate the bottleneck in provision of raw materials which is restricting the Group's development, through which to enhance our ability in controlling production costs. By focusing on construction of Zhanjiang Chenming pulp project and its ancillary raw timber base, coupled with the acceleration of the construction of Hubei forestry project base, an industrial chain of "forestry-pulp-paper integration" can be established; through this, we can elude the limitation imposed by upstream resources to solidify the Group's capability of achieving sustainable development.

VII. Chairman's Statement

Concentrate on research and development as well as production of high-end paper products to stake out market shares in both PRC and international high-end markets. Utilizing the Group's existing national-level technological research and development centers and post-doctoral technological research workstations, our production innovation and research and development capabilities are well-positioned for the development of new high-end paper products. More capital injections in such products will be continued to expand production capability; in the meantime, construction of several papermaking production lines with high technology utilization will be underway. As a result, the production size and product class of the Company can be further improved, aiding the Company in its bid to step up and become one of the forerunners in the league of international papermaking companies in the foreseeable future.

Remain focused on environmental protection constructions under the objective of "energy saving, reduced emission and harmonious development". With the conceptual belief that environmental protection takes the first great leap in corporate development, the Group strives to realize the goal of "energy saving, reduced emission and harmonious development". Underpinned by ascended national environmental protection standards and stronger regulatory efforts, the Group will carry out recycle economy on a full scale that promotes exchange and reuse of waste materials and maximization of resource utilization. In addition, construction of environmental protection projects will be speeded up to guarantee the Company's compliance with the relevant standards regulating waste emission.

Leverage on the Group's advantageous capital operations to actualize low-cost expansion. In view of the current stage of integration in the papermaking industry of China, we actively identify suitable targets for merger and acquisition under the premise that the expansion is in line with the Group's development strategies and beneficial to a rational allocation of production bases, with the ultimate aim of realizing low-cost expansion that can exploit the advantages embedded in the capital operations of the Group.

In the coming year, the Company and the Board will endeavor to establish a more complete corporate governance structure with better operation efficiency and transparency by following the future development strategy of the Group. Benefiting from the state's policies that encourage development of large scale papermaking enterprises, we will remain steadfast in expanding and strengthening the corporation so as to deliver more solid results to pay back our shareholders and the society.

Chen Hongguo

Chairman

8 April 2009

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises

(I) Overall operations during the reporting period

In 2008, the Group experienced rapid development of the domestic economy during the first half year, and suffered the slowdown of economy resulted from the global financial crisis, which presented the Company and the whole papermaking industry an austere test in the 2008. During the first half of 2008, market supply and demand for paper products underwent a gradual change as a result of effective implementation of the national energy saving and environmental emission reduction policies, and the macroeconomic policies such as phasing out of obsolete capacity in the papermaking industry under the “Eleventh Five-Year Plan” by way of accelerated closure of companies not up to standard environmentally and of obsolete capacity. Since the second half of 2007, the price of the Company’s products had seen rises of various degrees driven by many factors such as the surge in raw materials costs. Meanwhile, the phenomenon of the Beijing Olympic Games boosted the swift development of the macroeconomic environment to the speedway of growth, as a result of the high positive correlation between the papermaking industry and the macroeconomy, the whole papermaking industry was positioned in a benevolent environment of growth that had seen prices of paper and pulp maintained at generally higher positions, as reflected from the significant increase in paper demands. To a lesser extent, the papermaking industry was also one of the benefactors of the appreciation of Renminbi, because the appreciation of Renminbi made the import of pulp, waste paper and paper making equipment by domestic corporations less expensive, which turned into lowering of production costs and finance expenses as well as higher profitability. Under the influence of the above macroeconomic factors, the Company enjoyed substantial growth in its economic benefits in the first half year of 2008, which served as a solid base for the operations of the whole year.

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(I) Overall operations during the reporting period (continued)

In the second half of 2008, the subprime crisis in the United States turned into a global financial crisis, and its further deterioration severely impacted the global economy. China's economy retreated in its pace of growth, directly led to the slump in paper demands both domestically and overseas, as more clearly shown in the post-Olympic Games period. Against the backdrop of demand constriction and slow-moving inventories, the price of most paper products in China suffered significant downward correction. Although the cost of raw materials recorded significant period-on-period drops in October to an extent exceeding the period-on-period drop in paper prices, the decline in costs did not sufficiently reflect in the fourth quarter results due to the approximately two-month inventory period of raw materials. The management of the Company had taken effective measures to tackle the challenges in the second half year: in respect of product structure, the Company reinforced its efforts in research and development of new products to optimize product offerings; in terms of sales, flexible sales strategies were used to lower inventory level and build-up a policy to avoid business risks; for supply of raw materials, through considering the actual state of affairs in the Company, production limitations were imposed on certain pulp production lines on a targeted basis; while procurement of principal raw materials were strictly based on the principle of "tendering for lump sum purchases and quality to price comparison for small lot purchases" under the Group's central administration in order to minimize procurement costs.

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(I) Overall operations during the reporting period (continued)

1. Overview of production and operation

During 2008, the Company completed machine-made paper production of 3.17 million tonnes, representing a growth of 300,000 tonnes compared with 2007, or a growth of 10.45%; revenue realized from principal operations amounted to RMB15,530 million, up RMB365 million or 2.41% over 2007. Costs of principal operations were RMB12,557 million, increased by RMB482 million or 3.99% over 2007. Realized operating profit and net profit attributable to equity holders of the Company were RMB1,293 million and RMB1,075 million respectively, showing respective growths of 0.62% and 11.13%.

The growths were mainly attributable to: the 98,000-tonne annual capacity waste paper deinking project, the 120,000-tonne annual capacity art paper project and the Jilin 300-tonne daily chemical pulp production line came into operation successively during the reporting period, while the proprietary 300,000-tonne per annum super art paper project and the Jilin 180,000-tonne light weight coated paper project commenced operation in 2007 achieved benchmark during the reporting period, thereby expanding the production size of the Company. In spite of the financial crisis which resulted in lower sales prices in the fourth quarter, sales price for the year on an integrated basis was higher than 2007; on the other hand, unit production costs were driven up by inflated raw material prices, however, was countered by the decrease of 87,000 tonnes in sales volume to record slightly increased but substantially unchanged cost of revenue. The reduction in interest expenses and asset losses and the acquisition of minority interests in subsidiaries had resulted in increases in operating profit and net profit.

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(I) Overall operations during the reporting period (continued)

2. Progress of the Zhanjiang Chenming pulp project

- (1) As undertaken in the offering prospectus, 91% of the proceeds from H share offering were used in the Zhanjiang Chenming pulp project in Guangdong Province. As at 31 December 2008, RMB500 million was injected into the project while the rest of the amount was deposited in a bank account for the project to ensure safety of the funds.
- (2) The construction area of the woodlands for papermaking materials reached 600,000 mu already, of which 260,000 mu of woodlands for papermaking materials had obtained legal forestry rights certificates (林權證) at the end of 2008.
- (3) The site formation work of the Zhanjiang Chenming pulp project was 70% complete.
- (4) On the site of the Zhanjiang Chenming pulp project, the ancillary fencing work, catchment and drainage work design and the tendering works were under progress and would soon commence in all areas.
- (5) Actively worked with domestic ancillary equipment providers and installation service providers through idea exchange, detailed discussions and preparation in connection with the proposal and plan in tendering of the project by stages
- (6) Procurement of main imported equipment. As affected by the global financial crisis, the price of steel materials experienced a significant decline. To maximize the benefits under the construction of the Zhanjiang Chenming pulp project and ensure the investment returns of shareholders, the project company believed it necessary to further lower the relevant terms in pricing of the related main equipment supply contracts. The import price of the main equipment are currently under negotiation, and the project company will determine the construction progress of the main equipment in view of the international economic environment and pay the import equipment prepayments as stipulated in the contracts, in order to proceed with the construction of the Zhanjiang Chenming pulp project in an active and steady manner.

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(I) Overall operations during the reporting period (continued)

3. Management and innovation

- (1) The Company had made it a policy to convene joint-meetings for production, sales and management in 2008, which called management of the Company, responsible personnel in relevant departments and officials above chief representative level of each sales administrative area to attend the joint-meetings. During the meetings, the economic operations of each type and model of machines was seriously analyzed to identify and raise issues, while each of such issues would be discussed to formulate corrective measures. For the weaker links of management in the Company and each subsidiary that were identified, the Group would establish dedicated committees in the areas of technology, environmental protection, energy saving and equipment, allocation, costs, electricity and safety, etc. Professionally structured vertical management was enhanced to help the Company and all subsidiaries identify and solve issues in the course of operation to allow effective and better level of governance throughout the Company.
- (2) During the reporting period, the national-level technology centers and post-doctoral technological research workstations were utilized to scrupulously improve upon our abilities to innovate and create. Also, the corporate collaborations with advanced international corporations such as Arjo Wiggins of France and Sappi of South Africa immersed us in an engaging atmosphere of research and development and innovation, under which we produced a series of high added-value new products that would be suitable for marketing and sales; these products had optimized our product structure and increased our market competitiveness, thereby building ourselves as an international brand name in both PRC and overseas markets. The “High Yield Pulping and Chemical Pulping Technological Research” (高得率制漿及化學制漿技術研究) of the Company was granted construction work job qualification by Yuandu Scholars (鳶都學者) of Weifang City. Our study subject “The Practical Key Techniques Study in Mixed Wide Leaves for Bleaching in a Chemithermomechanical Pulping Process” (混合闊葉材漂白化學熱磨機械漿生產應用關鍵技術研究) was listed as a national scientific support project under the “Eleventh Five-Year Plan”, the results of the study improved the quality of pulping using mixed wide leaves through bleaching in chemithermomechanical pulping process. In response to market demands, newly development products such as environmental-friendly high-end low basis weight coated paper, environmental-friendly high-end copperplate paper and environmental-friendly high-end white paperboard were introduced to further enrich our product mix and allow more channels of profit generation.

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(I) Overall operations during the reporting period (continued)

3. Management and innovation (continued)

In connection with energy saving and emission reduction, the Company maximized recycling and reuse to the largest extent by implementing a scientific method of water usage categorized by quality, quantity, process and techniques in our production system. Papermaking water was reused at a rate above 90%. During the reporting period, a 30,000 cubic daily capacity intermediate water reuse project was put into use, all the processed waste water would be returned to use in production to reduce overall pollutants and waste emission by 40%. Building upon the recycling of methane, electricity plant ash-slag and papermaking mud produced in the processing of waste water with anaerobic gas, the “double alkali method” of desulphurization was used for the modification of three coal powder kilns to reduce production of sulfur dioxide by 7,000 tonnes annually and process white sludge recovered from papermaking alkali by 17,000 tonnes. The 130t/h circulating sulphurized bed boiler for waste substances equipped with a 12MW single stage extraction turbine electricity generation module was put into operation for mixed usage of solid waste substances, including bark, wood bits, sawdust, ink sludge and mud, producing a win-win situation with both economic benefits and environmental benefits.

During the reporting period, the Company was listed on the main board of Hong Kong Stock Exchange and became the first company in China listed with A, B and H shares;

The Company was named by the People's Government of Shandong Province as the “Leading Enterprise of Foreign Economic and Trade in Shandong Province” (山東省外經貿先進企業);

The Company's aldehyde-free fiberboard was given the “Technological Advancement Award for China's Fiberboard Industry” (中國纖維板行業技術進步獎);

The Company won the accolades of “Pioneering Energy Saving Enterprise in Shandong Province” (山東省節能先進企業) and “Leading Unit in Earthquake Relief in Weifang City” (濰坊市抗震救災先進單位);

The Company was honored with the titles of “Excellent Paper Making Enterprise in China for the Year 2008” (2008中國造紙年度優秀企業) and “Model Company of Labor Protection Integrity” (勞動保障誠信示範單位);

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(I) Overall operations during the reporting period (continued)

3. Management and innovation (continued)

The People's Government of Shandong Province heralded the Company as "Leading Tax-paying Enterprise in Shandong Province" (山東省納稅先進企業);

The Company was ranked 165 in the Top 500 China Manufacturing Enterprises (中國製造企業500強) published by China Enterprise Confederation and China Enterprise Director Association, retaining its highest position among papermaking industrial players.

(II) Principal operations of the Company and analysis on their operations

1 Principal operations by industry and product

Unit: RMB in ten thousands

By industry or product	Sales revenue	Cost of sales	Gross profit margin (%)	Principal operations by industry		
				Year-on-year increase / decrease in sales revenue (%)	Year-on-year increase / decrease in cost of sales (%)	Year-on-year increase / decrease in gross profit margin (%)
Machine made paper	1,457,392.10	1,181,495.56	18.93%	5.18%	7.02%	-1.39%
Electricity and steam	23,555.16	19,948.53	15.31%	-3.92%	8.67%	-9.81%
Construction materials	51,259.42	44,427.32	13.33%	-41.08%	-38.92%	-3.06%
Chemicals for papermaking	8,863.99	3,697.06	58.29%	-3.66%	-19.44%	8.17%
Hotel industry	2,414.89	835.63	65.40%			
Others	9,473.78	5,272.13	44.35%	-7.18%	-32.05%	20.36%
Total	1,552,959.34	1,255,676.23	19.14%	2.41%	3.99%	-1.23%

By product	Sales revenue	Cost of sales	Gross profit margin (%)	Principal operations by product		
				Year-on-year increase / decrease in sales revenue (%)	Year-on-year increase / decrease in cost of sales (%)	Year-on-year increase / decrease in gross profit margin (%)
Light weight coated paper	175,859.59	146,586.20	16.65%	-6.94%	-4.64%	-2.01%
Duplex press paper	206,039.86	158,442.89	23.10%	-0.56%	-2.11%	1.21%
Writing paper	38,933.62	30,774.44	20.96%	53.72%	57.92%	-2.1%
Copperplate paper	261,118.84	197,660.47	24.30%	12.96%	11.41%	1.05%
News press paper	213,287.29	172,542.40	19.10%	7.64%	7.74%	-0.08%
Paperboard	83,347.88	79,816.12	4.24%	-9.10%	4.03%	-12.09%
White paperboard	215,858.53	174,874.58	18.99%	-8.20%	-9.42%	1.09%

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(II) Principal operations of the Company and analysis on their operations (continued)

2 Breakdown of revenue form paper products of principal operations by geographical segment

Unit: RMB in ten thousands

Geographical segment	Sales revenue	Year-on-year increase / decrease in sales revenue (%)
PRC	1,263,291.65	9.37%
United States	4,965.80	-80.14%
Hong Kong	20,712.97	-31.70%
Japan	14,667.01	-56.11%
South Africa	23,646.04	-19.17%
Other overseas countries	130,108.63	15.63%
Total	1,457,392.10	5.18%

(III) Analysis and explanation on major year-on-year changes in composition of assets of the Company during the reporting period

Unit: RMB

Items	2008		2007		Difference
	At the end of the period	As percentage of total assets in 2008	At the end of the period	As percentage of total assets in 2007	
Bank balances and cash	2,853,418,128.07	10.85%	740,621,843.91	3.36%	7.49%
Bills receivable	974,009,788.24	3.70%	1,676,684,054.95	7.62%	-3.92%
Inventories	3,397,792,930.38	12.92%	1,744,492,612.36	7.93%	4.99%
Fixed assets	14,213,441,758.08	54.04%	13,243,156,039.93	60.17%	-6.13%
Construction in progress	431,379,272.50	1.64%	904,753,634.02	4.11%	-2.47%
Intangible assets	1,277,076,588.53	4.86%	822,301,826.32	3.74%	1.12%
Consumable biological assets	301,212,691.14	1.15%	92,159,871.29	0.42%	0.73%

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(III) Analysis and explanation on major year-on-year changes in composition of assets of the Company during the reporting period (continued)

1. Explanation on the main reasons leading to the changes

- (1) Bank balances and cash: the Company issued H shares in June 2008 with a total of RMB2,728 million in proceeds and interests, increasing bank balances and cash.
- (2) Bills receivable: mainly due to the Group conducted sales on credit more frequently, requiring distributors to repay within a credit period instead of settling by bills receivable, which caused a drop in the balance of bills receivable.
- (3) Inventories: under the impact of the financial crisis, the market price for paper products dropped during the year with substantially lowered demands, which was caused by lower sales volume in all four quarters.
- (4) Fixed assets: (1) constructions in progress including 120,000-tonne art paper project, Shandong Grand View Hotel construction and 98,000-tonne waste paper de-inking project were transferred to fixed assets, increasing amount in fixed assets; and (2) subsidiary Fuyu Chenming Paper Co., Ltd. (富裕晨鳴紙業有限責任公司) acquired all the fixed assets in Heilongjiang Sida Paper Company Limited (黑龍江斯達紙業有限公司) and Heilongjiang Paper Factory (黑龍江造紙廠) during the year, also led to increase in fixed assets.
- (5) Construction in progress: constructions in progress such as 120,000-tonne art paper project, Shandong Grand View Hotel construction and 98,000-tonne waste paper de-inking project were transferred to fixed assets, which increased fixed assets and reduced construction in progress.
- (6) Intangible assets: primarily due to subsidiary Zhanjiang Chenming Paper Pulp Co., Ltd. starting preparation for construction works that resulted in increase of land use rights.
- (7) Consumable biological assets: mainly attributable to the purchase, nurturing and fair value change in forestry of subsidiaries Zhanjiang Chenming Arboriculture Co., Ltd., Yangjiang Chenming Arboriculture Co., Ltd., Nanchang Chenming Arboriculture Co., Ltd. and Huanggang Chenming Arboriculture Co., Ltd..

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(III) Analysis and explanation on major year-on-year changes in composition of assets of the Company during the reporting period (continued)

2. Nature of measurement adopted for the major assets of the Company:

Historical cost method is normally used for measurement in preparing the financial statements of the Company, except the below asset items were carried at fair value:

- (1) Financial assets carried at fair value through profit or loss for the current period
- (2) Consumable biological assets (please refer to Note 17 of financial statements items prepared in accordance with Accounting Standards for Business Enterprises)
- (3) Changes on and effects of changes in major assets carried at fair value:

Unit: RMB in ten thousands

Statement items	Item	Method of obtaining fair value	Balance as of 31 December 2008	Balance as of 31 December 2007	Effect on profit or loss for the year
Financial assets held for trading	Derivative financial instruments	Quotations from financial institutions	0	5,955,480.00	1,738,200.00
Consumable biological assets	Consumable timber assets	Note (1)	301,212,691.14	92,159,871.29	918,451.60

The Group adopted the following critical methodology and assumptions when estimating the fair value of financial assets held for trading and consumable biological assets carried at fair value at the balance sheet date:

- (1) Derivative financial instruments: the fair values of forward foreign exchange contracts were determined by the difference between the present value of the price of contractual forward foreign exchange and the spot foreign exchange price at the balance sheet date. The Group used the forward contract settlement exchange rate for same day settlement published by banks on 31 December 2008 as the basis and used the contractual settlement exchange rate for determination of the difference.

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(III) Analysis and explanation on major year-on-year changes in composition of assets of the Company during the reporting period (continued)

2. Nature of measurement adopted for the major assets of the Company: (continued)

- (2) Consumable biological assets: independent valuers determined the market price of timber harvest by the active market quotations in Zhanjiang City and Fujian Province where our biological assets were located. In estimating future cash flow, the independent valuers considered the following factors: 1) the expected nominal market price of the timber harvest; 2) expected timber gains was dependent on the opinion and judgment of biological assets by considering the expected timber reserve level and timber production rate formulated by experts for a limited scope; 3) the expected costs for maintaining and nurturing existing biological assets; and 4) the expected costs of sales (including our estimated harvest costs and transportation costs).

(IV) Analysis and explanation on major year-on-year changes in profit and loss indicators during the reporting period

Unit: RMB in ten thousands

Item	Accrued during this year	Accrued during the previous year	Increase (+) Decrease (-)
Sales revenue	15,529,593,435.77	15,164,742,450.26	2.41%
Costs of sales	12,556,762,340.80	12,074,481,475.02	3.99%
Tax and levies on operations	12,582,354.31	17,854,424.80	-29.53%
Selling and distribution expenses	705,595,565.95	783,289,341.85	-9.92%
General and administrative expenses	561,194,537.62	530,820,858.29	5.72%
Finance expenses	287,136,504.05	392,163,050.56	-26.78%
Losses on impairment of assets	93,125,334.87	102,198,629.26	-8.88%
Gain on change in fair value	2,656,651.60	30,370,880.31	-91.25%
Investment income	-23,081,752.26	-9,461,550.75	-143.95%
Non-operating income	274,366,224.82	232,218,083.67	18.15%
Non-operating expenses	11,798,611.64	27,725,881.15	57.45%
Net profit attributable to shareholders			
of the parent company	1,075,291,741.53	967,636,172.39	11.13%
Gains and losses of minority interests	184,249,712.74	250,905,016.90	-26.57%

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(IV) Analysis and explanation on major year-on-year changes in profit and loss indicators during the reporting period (continued)

Explanation on the main reasons leading to the changes

- (1) Please refer to “1. Overview of production and operation” under “(I) Overall operations during the reporting period” of this section for changes in indicators of sales revenue, costs of sales and net profit attributable to shareholders of the parent company.
- (2) Tax and levies on operations decreased by 29.53% over in 2007, because Chibi Chenming Paper Co., Ltd, a subsidiary of the Company, was changed into a foreign-invested enterprise on 29 June 2007, therefore tax and levies on operations (e.g. city construction tax) were no longer required.
- (3) Selling and distribution expenses fell by 9.92% compared with 2007, mainly because sales volume decreased in 2008 under the impact of the financial crisis, allowing more room for a drop in transportation expenses.
- (4) General and administrative expenses increased by 5.72% over 2007, mainly due to loss from production interruption in certain subsidiaries.
- (5) Finance expenses decreased by 26.78% when compared with 2007, mainly because the Company issued H shares in June 2008, the proceeds collected therefrom increased interests income; the Group also reduced interest expenses by repaying a portion of borrowings with the proceeds from issuance of RMB1,900 million short-term debentures in 2008.; and the convertible bonds were converted into shares in 2007, thus reducing interest expenses in 2008.
- (6) Losses on impairment of assets was reduced by 8.88% compared with 2007, primarily due to the Group's receipt of goods payment from 佛山市順德區星辰紙業有限公司 (Foshan Shunde Xingchen Paper Co., Ltd.) which was recognized as impaired in 2008, therefore, the Group reversed a bad debt fully provided for in 2007; meanwhile, the Group performed impairment tests on inventories in view of the impact of the financial crisis, which had led to increase in losses from impairment of assets.

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(IV) Analysis and explanation on major year-on-year changes in profit and loss indicators during the reporting period (continued)

Explanation on the main reasons leading to the changes (continued)

- (7) Gain on change in fair value dropped by 91.25% compared with 2007, the main reason was forestry assets recorded less gain on change in fair value when compared with 2007 as affected by the financial crisis.
- (8) Investment income decreased by 143.95% over 2007, primarily due to the exacerbation of losses in associated corporations during 2008.
- (9) Non-operating income increased by 18.15% over 2007, primarily attributable to the increase in government grants and negative goodwill arising from purchase of minority interests in 2008.
- (10) Non-operating expenses decreased by 57.45% over 2007, mainly due to the effect of reduction in net loss from disposal of assets during the period.
- (11) Gains and losses attributable to minority interests fell by 26.57% compared with 2007, mainly due to in the acquisition of Shandong Chenming Power Supply Holdings Co., Ltd., a subsidiary of the Company, in 2008, and the decrease in profit of certain non-wholly owned subsidiaries.

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(V) Cash flow generated from operating activities of the Company during the reporting period

Unit: RMB

Item	For the current period	For the corresponding period of the previous year	Increase (+) Decrease (-)
Net cash flow generated from operating activities	1,934,140,803.04	1,324,263,125.01	46.05%
Net cash flow generated from investment activities	-1,503,850,542.15	-977,001,495.03	-53.93%
Net cash flow generated from financing activities	1,661,066,800.52	-512,996,336.43	423.8%

Note: In the cash flow statements prepared by the Company, receipt of outstanding bank acceptance bills are not reflected as cash inflow in "cash received from sales of goods, rendering of services"; similarly, payments made using outstanding bank acceptance bills are not reflected as cash outflow in "cash paid for goods and services" nor "cash paid to acquire fixed assets, intangible assets and other long-term assets" with respect to bills paid in the course of investment activities.

Explanation on the main reasons leading to the changes:

- (1) Net cash flow generated from operating activities increased by 46.05% over 2007, mainly due to increase in income and profit in 2008, as well as the Company's proportionate reduction in settlements by bills and the increase in amount of financial grants received.
- (2) Net cash flow generated from investment activities dropped 53.93% over 2007, mainly due to increase in investments, including the 120,000-tonne art paper project launched during the reporting period, the acquisition of the entire interests in Heilongjiang Sida Paper Company Limited (黑龍江斯達紙業有限公司) and Heilongjiang Paper Factory (黑龍江造紙廠) by our subsidiary Fuyu Chenming Paper Co., Ltd. (富裕晨鳴紙業有限責任公司) during the year, investments in the Zhanjiang pulp project and other technological reform projects.
- (3) Net cash flow generated from financing activities increased 423.8% over 2007, mainly attributable to the Company's issued H shares in June 2008 and increased repayment of borrowings.

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(VI) Operation and results of major subsidiaries of the Company

Unit: RMB in ten thousands

Name of subsidiary	Business nature	Shareholding percentage	Principal products manufactured	Registered capital	Asset size	Net profit
武漢晨鳴陽紙業股份有限公司 (Wuhan Chenming Hanyang Paper Holdings Co., Ltd.)	Papermaking	50.93%	Writing paper, news press paper	21,136.70	239,559.46	18,457.76
山東晨鳴紙業集團齊河板紙有限責任公司 (Shandong Chenming Paper Group Qihe Paperboard Co., Ltd.)	Papermaking	100.00%	Paperboard, corrugated paper	37,620.00	123,822.64	-1,019.48
山東晨鳴熱電股份有限公司 (Shandong Chenming Power Supply Holdings Co., Ltd.)	Electricity and heat	86.71%	Generation and sales of electricity and heat	9,955.31	70,188.45	3,811.73
吉林晨鳴紙業有限責任公司 (Jilin Chenming Paper Co., Ltd.)	Papermaking	100.00%	News press paper, light weight coated paper	150,000.00	243,002.92	-365.60
赤壁晨鳴紙業有限責任公司 (Chibi Chenming Paper Co., Ltd.)	Papermaking	35.79%	Duplex press paper	17,741.94	50,477.37	6,448.03
江西晨鳴紙業有限責任公司 (Jiangxi Chenming Paper Co., Ltd.)	Papermaking	51.00%	Coated paper	USD172 million	338,680.79	13,049.21
延邊晨鳴紙業有限公司 (Yanbian Chenming Paper Co., Ltd.)	Pulping	76.73%	Pulp and chemicals	8,163.30	32,843.27	1,328.05

VIII. Directors' Report

I. Management discussion and analysis under Accounting Standards for Business Enterprises (continued)

(VII) Explanation on single subsidiaries with net profit (or investment gains) accounting for over 5% of the net profit of the Company

Unit: RMB in ten thousands

Name of company	Revenue from principal operations	Profit from principal operations	Net profit	Net profit attributable to the Company according to shareholding percentage	As a percentage of net profit of the Company
武漢晨鳴漢陽紙業股份有限公司 (Wuhan Chenming Hanyang Paper Holdings Co., Ltd.)	184,965.69	36,177.1	18,457.76	9,400.54	8.74%
江西晨鳴紙業有限責任公司 (Jiangxi Chenming Paper Co., Ltd.)	183,839.13	31,170.39	13,049.21	6,655.1	6.19%

II. Management discussion and analysis under International Financial Reporting Standards

The following financial data is extracted from the audited financial statements of the Company prepared in accordance with International Financial Reporting Standards. The following discussion and analysis should be read in conjunction with the financial statements of the Company set out in this report and the notes thereto.

Revenue from operations

Unit: RMB '000

By sector or by product	2008		2007	
	Revenue from principal operations	As a percentage of revenue from operations (%)	Revenue from principal operations	As a percentage of revenue from operations (%)
Sales of paper products	14,561,339.00	94.37	13,837,756.00	93.00
Sales of electricity and steam	235,552.00	1.53	68,996.00	0.46
Sales of construction materials	512,594.00	3.32	869,910.00	5.85
Sales of chemical products	88,640.00	0.57	92,004.00	0.62
Others	32,785.00	0.21	10,209.00	0.07
Total	15,430,910.00	100.00	14,878,875.00	100.00

VIII. Directors' Report

II. Management discussion and analysis under International Financial Reporting Standards (continued)

Unit: RMB '000

Geographical segment	2008		2007	
	Revenue from operations	As a percentage of revenue from operations (%)	Revenue from operations	As a percentage of revenue from operations (%)
PRC	13,502,030.00	87.50	12,573,625.00	84.51
United States	49,658.00	0.32	250,063.00	1.68
Hong Kong	207,130.00	1.34	303,261.00	2.04
Japan	146,670.00	0.95	334,189.00	2.24
South Africa	236,460.00	1.54	292,530.00	1.97
Other overseas areas	1,288,962.00	8.35	1,125,207.00	7.56
Total	15,430,910.00	100.00	14,878,875	100.00

Revenue from operations for 2008 was RMB15,431 million, representing an increase of RMB552 million or 3.71% over 2007. Under the impact of various factors including the financial crisis, exports business declined moderately compared with 2007; among which revenue from exports to Hong Kong dropped 31.70% from 2007 to RMB207 million; revenue from exports to United States fell 80.14% compared with 2007 to stand at RMB50 million; revenue from exports to Japan amounted to RMB147 million, down 56.11% over 2007; exports to South Africa reached RMB236 million to record a drop of 19.17% compared with 2007. Revenue from exports to other overseas areas was RMB1,289 million, representing an increase of 14.55% over 2007, mainly contributed by exports to areas such as Singapore and the Middle East.

Revenue from sales of paper products amounted to RMB14,561 million, representing growth of 5.23% over 2007; the growth was primarily due to a substantial surge in average product price for the year on integrated basis over 2007, despite the influence of unfavorable market conditions and the drop in product price during the fourth quarter of 2008 as a result of the financial crisis.

Revenue from sales of electricity and steam amounted to RMB236 million, surged 241.40% over 2007, mainly due to the fact that sales of certain electricity and steam were accounted for as raw materials in 2007 and therefore reflected in other gains.

Revenue from sales of construction materials amounted to RMB513 million, a plunge of 41.08% compared with 2007, mainly due to reduction in revenue as a result of unfavorable market conditions that led to lower sales volume of fiberboard in 2008 compared with 2007.

VIII. Directors' Report

II. Management discussion and analysis under International Financial Reporting Standards (continued)

Revenue from sales of chemical products operations amounted to RMB89 million, down 3.66% compared with 2007, mainly due to lower sales volume of chemicals in 2008 compared with that of 2007 as affected by factors such as market conditions, which resulted in lower revenue.

Cost of sales and gross profit

Cost of sales as a percentage of revenue from operations

Unit: RMB '000

By sector or by product	2008		2007	
	Cost of sales	As a percentage of revenue from operations (%)	Cost of sales	As a percentage of revenue from operations (%)
Sales of paper products	11,780,147.00	80.90%	11,005,949.00	79.54%
Sales of electricity and Steam	199,485.00	84.69%	58,925.00	85.40%
Sales of construction materials	444,273.00	86.67%	727,364.00	83.61%
Sales of chemical products	36,971.00	41.71%	45,891.00	49.88%
Others	12,035.00	36.71%	7,495.00	73.42%
Total	12,472,911.00	80.83%	11,845,624.00	79.61%

Gross profit and gross profit margin

By industry or by product	2008		2007	
	Gross profit	Gross profit margin	Gross profit	Gross profit margin
Sales of paper products	2,781,192.00	19.10%	2,831,807.00	20.46%
Sales of electricity and steam	36,067.00	15.31%	10,071.00	14.60%
Sales of construction materials	68,321.00	13.33%	142,546.00	16.39%
Sales of chemical products	51,669.00	58.29%	46,113.00	50.12%
Others	20,750.00	63.29%	2,714.00	26.58%
Total	2,957,999.00	19.17%	3,033,251.00	20.39%

VIII. Directors' Report

II. Management discussion and analysis under International Financial Reporting Standards (continued)

Cost of sales of the Group in 2008 reached RMB12,473 million, increased by 5.30% over 2007. Gross profit dropped 2.48% compared with 2007 to RMB2,958 million, principally because costs of sales in the first to third quarters of 2008 rose due to higher price of raw materials and slower sales. The Group recorded relatively low gross profit margin in the fourth quarter mainly due to the financial crisis, which contributed to the drop in overall gross profit margin of 1.22% in 2008 compared with 2007 while the gross profit margin in 2008 is 19.17%.

Cost of sales of paper products was RMB11,780 million, representing a growth of 7.03% over 2007, mainly due to the higher cost of sales resulted from increased price of raw materials and weaker sales volume between the first and third quarters of 2008.

Cost of sales of the electricity and steam amounted to RMB199 million, increased by 238.54% over 2007, mainly because certain electricity and steam were accounted for as sales of raw materials in 2007, and were therefore reflected in other gains.

Cost of sales of the construction materials amounted to RMB444 million, decreased by 38.92% over 2007, mainly due to the decrease in sales volume of fiberboard in 2008 under the influence of market conditions and the corresponding drop in costs of sales.

Cost of sales of the chemical products was RMB37 million, decreased by 19.44% over 2007, mainly due to lower costs from weak sales of chemicals in 2008 as affected by market conditions.

Other income

Other income of the Group for 2008 amounted to RMB501 million, increased by 8.26% over 2007, mainly due to: (1) proceeds of RMB2,728 million from issuance of H shares of the Company in 2008, which increased interests income; and (2) government grants received in 2008 exceeded that of 2007 by RMB35 million.

Share of results of associates

In 2008, the Group's share of results of associates was -RMB23.2 million, representing a decrease of 144.21% compared with 2007, mainly due to the exacerbation of losses in associates in 2008.

VIII. Directors' Report

II. Management discussion and analysis under International Financial Reporting Standards (continued)

Distribution expenses

Distribution expenses in 2008 was RMB706 million, representing a drop of 9.92% over 2007, principally affected by the financial crisis which caused sales volume in the fourth quarter of 2008 to drop and in turn substantially lowered transportation expenses.

Administrative expenses

Administrative expenses in 2008 amounted to RMB543 million, representing a decrease of 16.92% over 2007, mainly due to more efforts put in by the Group in its collection of goods payments, where the already provided for impairment receivables due from 佛山市順德區星辰紙業有限公司 (Foshan Shunde Xingchen Paper Co., Ltd.) were recovered in 2008, this led to the reversal of fully provided bad debts and reduced administrative expenses; meanwhile, under the impact of the financial crisis, the loss from production interruption in certain subsidiaries led to an increases in administrative expenses.

Gain on change in fair value of derivative financial instruments

In 2008, gains from derivative financial instruments decreased by RMB4.217 million in 2007 to RMB1.738 million, mainly due to the future pooling foreign exchange contracts, which were dominated in USD, entered into by Jiangxi Chenming, a subsidiary of the Company, with Changbei branch of China Construction Bank and Changbei branch of Bank of China respectively on 18 October 2007. Such financial assets had gain on change in fair value of RMB1.738 million in 2008, representing a decrease of RMB4.217 million compared with 2007.

Gain on change in fair value less estimated point-of-sale cost of biological assets

Gain on change in fair value less estimated point-of-sale cost of biological assets in 2008 was RMB918,000, decreased by RMB23.497 million from 2007, mainly due to the change in fair value of forestry assets of the Company.

Impairment loss on property, plant and equipment

In 2008, impairment loss on property, plant and equipment was RMB8.563 million, mainly due to 襄樊晨鳴銅版紙有限公司 (Xiangfan Chenming Copperplate Pater Co., Ltd) cancelled its registration in 2008, therefore its fixed assets with net worth of RMB6.766 million was fully provided for impairment.

Allowance for inventory

In 2008, allowance for inventory increased by RMB127 million compared with 2007, mainly because under the impact of the financial crisis, the Group provided allowance for drop in inventory price by stating at the lower of net realizable value and cost.

VIII. Directors' Report

II. Management discussion and analysis under International Financial Reporting Standards (continued)

Finance costs

Finance costs amounted to RMB463 million in 2008, decreased by 16.75% compared with 2007, mainly due to invigoration of the Group's capital operations to issue short-term debentures and repay certain portions of short-term borrowings, at the same time the Company redeemed all the convertible bonds of the Company in advance on 14 May 2007, leading to lower interest expenses in 2008 compared with 2007.

Income tax expenses

The Group recorded income tax expenses of RMB296 million in 2008, representing an increase of 9.23% over 2007, mainly due to higher profit of the Company in 2008 over that of 2007, causing income tax to increase.

Profit attributable to minority interests

Profit attributable to minority interests amounted to RMB193 million in 2008, representing a decrease of 25.47% over 2007, mainly due to (1) reduction in realized net profit of certain non-wholly owned subsidiaries of the Company in 2008, reducing profit attributable to minority interests; and (2) the Company's acquisition of 35.71% minority interests in subsidiary Shandong Chenming Power Supply Holdings Co., Ltd. during the year, the effects of which reduced profit attributable to minority interests.

Profit attributable to equity holders of the Company and profit margin

Profit of the Group attributable to the equity holders of the Company was RMB1,102 million for 2008, representing an increase of 10.89% over 2007; while profit margin was 7.14%, grew 0.46% compared with 6.68% in the corresponding period of 2007. The changes were mainly due to: (1) acquisition of minority interests in Shandong Chenming Power Supply Holdings Co., Ltd. by the Company increased revenue, while profit attributable to equity holders of the Company also increased due to the additional shareholding interests; (2) the Company strengthened its efforts in recovery of goods payments and received payments of impaired receivables from 佛山市順德區星辰紙業有限公司 (Foshan Shunde Xingchen Paper Co., Ltd.) to reverse bad debts already provided in full, hence increased profit attributable to the equity holders of the Company; and (3) invigoration of the Company's capital operations to issue short-term debentures and repay certain portions of short-term borrowings, so as to reduce interest expenses and increase net profit.

VIII. Directors' Report

II. Management discussion and analysis under International Financial Reporting Standards (continued)

Liquidity

In 2008, the cash flows from operating activities, the cash flows from investing activities and the cash flows from financing activities of the Company were RMB 1,934 million, -RMB 1,543 million and RMB 1,700 million respectively, increased by 22.87%, - 38.41% and 371.95% from 2007. The main reasons were:

- (1) The increase in the cash flows from operating activities was mainly due to increased income and profit in 2008, decreased settlement ratio of bill receivable and increased financial subsidies of the Company.
- (2) The decrease in the cash flows from investing activities was mainly due to : the launch of the 120,000 tonnes art paper project during the reporting period by the Company, the acquisition of Heilongjiang Xida Paper Company Limited (黑龍江斯達紙業有限公司) and Heilongjiang Paper Plant (黑龍江造紙廠) by Fuyu Chenming Paper Co., Ltd. (富裕晨鳴紙業有限責任公司), a subsidiary of the Company, in 2008, the Zhanjiang pulp project and an increase in technological transformation investment projects.
- (3) The increase in the cash flows from financing activities was mainly due to receipt of the proceeds from the issuance of H shares in June 2008, changes in borrowings and short-term financing debentures.

Significant seasonal effect on the capital requirements of the Company

In 2008, there was no significant seasonal effect on the capital requirements of the Company.

Principal sources of funding

In 2008, the principal sources of funding of the Company mainly derived from the revenue from production operations, bank loans, issuance of the short-term financing debentures and financing activities of new H shares offering in the Hong Kong capital market.

VIII. Directors' Report

II. Management discussion and analysis under International Financial Reporting Standards (continued)

Bank borrowings and interest rate of borrowings of the Company during the reporting Period

As at 31 December 2008, the Group's new bank borrowings were increased by RMB 6,002 million (excluding RMB 1,900 million raised from this issuance of the short-term financing debentures), and the repayment of loans amounted to RMB 7,547 million (excluding RMB 500 million of the repayment of loans for the period). The borrowing was bearing interest from 3.6% to 7.7%.

Gearing ratio of the Company

As at 31 December 2008, the gearing ratio of the Group was 32.5% (including minority interests), dropped by 7.8% compared with the ratio of 40.3% in 2007, mainly due to the fact that the Company increased the capital by the way of H shares issue in June 2008, and the Company repaid part of the loans in 2008, thus the loans from bank dropped. Meanwhile, it was also because of an increase in equity attributable to equity holders of the Company. The formula adopted by the Group in calculating gearing ratio was as follows: gearing ratio = total borrowings/total assets (Total borrowings refers to borrowings due within one year, borrowings due after one year and short-term debentures).

Secured assets of the Company at the end of the reporting period

As at 31 December 2008, the secured assets of the Group included: International Finance Corporation ("IFC"), Deutsche Bank AG ("DEG") and China Construction Bank Nanchang Changbei Branch entered into an loan agreement with Jiangxi Chenming Paper Co., Ltd, a subsidiary of the Company, pursuant to which, secured loans of USD 40,000,000.00, USD 9,411,765.00 and USD 17,500,000.00 were provided to Jiangxi Chenming Paper Co., Ltd respectively. The collateral was the fixed assets and land use rights of Jiangxi Chenming Paper Co., Ltd. As at 31 December 2008, the net book value of the collateral with regard to fixed assets was RMB 1,144,235,273.50 and that with regard to the land use rights (intangible assets) was RMB 74,653,598.66.

Contingent liabilities of the Company

As at 31 December 2008, there were no contingent liabilities of the Group.

The financial risk management is the responsibility of the Group's treasury function at our head office. One of the major objectives of the Group's treasury policies is to manage its exposure to fluctuations in interest rates and foreign currency exchange rates.

VIII. Directors' Report

II. Management discussion and analysis under International Financial Reporting Standards (continued)

Risk of fluctuations in foreign exchange rate and any relevant hedging

As at 31 December 2008, the exchange gain of the Group was RMB 157 million mainly due to: the exchange gain from the foreign currency borrowings and accounts payable resulting from appreciation of RMB.

The business operations of the Group were conducted mainly in the PRC with revenues and expenses denominated in RMB. Some of the Group's cash and bank deposits, including proceeds from global offering, were denominated in Hong Kong Dollars, US Dollars, Euro or RMB. Any exchange rate fluctuations of foreign currencies against RMB could have an impact on the financial position of the Group.

During the year ended 31 December 2008 under review, the Group had used derivative financial instruments denominated in US dollar for hedging purposes. However, the Group will continue to monitor the exposure of proceeds from global offering to foreign exchange fluctuations.

Property, plant and equipment

Details of movements in property, plant and equipment during the year ended 31 December 2008 are set out in Note 14 to the financial statements prepared in accordance with the International Financial Reporting Standards contained herein.

Fixed Assets

During the listing of the Company's H shares on the main board of the Hong Kong Stock Exchange in June 2008, valuation was conducted on the property interests held by the Group. However, those property interests were still carried at historical costs less accumulated depreciation and accumulated impairment loss (if any) on the balance sheet.

By reference to the property valuation set out in Appendix IV to the prospectus of the Company dated 4 June 2008 (the "Prospectus"), a revaluation surplus of approximately RMB903.7 million was recorded in respect of the property interests of the Group as at 31 March 2008. Were the property stated at that valuation, the depreciation and amortisation charges per year would have increased by approximately RMB22.5 million.

VIII. Directors' Report

II. Management discussion and analysis under International Financial Reporting Standards (continued)

Material contracts

During the reporting period, the Company or any of its subsidiaries did not enter into any material contracts with the controlling shareholder or its subsidiaries.

Reserve

According to the relevant requirements imposed by the State Ministry of Finance and Articles of Association, the distributable profit shall be the lower of the distributable profit as calculated in accordance with Accounting Standards for Business Enterprises and that calculated in accordance with International Financial Reporting Standards. The net profit attributable to shareholders realized in 2008 according to the Accounting Standards for Business Enterprises was RMB973,557,811.58, and net profit attributable to shareholders realized in 2008 according the International Financial Reporting Standards was RMB1,000,553,922.04; accordingly, the net profit distributable to shareholders realized during this year was RMB973,557,811.58.

Details of changes in the reserves for this year and details of the distributable reserves of the Company as at 31 December 2008 are set out in the consolidated statement of changes in equity and Note 12 to the financial statements prepared in accordance with the International Financial Reporting Standards contained herein.

Sufficiency of public float

During the year ended 31 December 2008, the Company maintained sufficient public float.

III. Prospect of the future developments of the Company

1. The development trend of the industry to which the Company belongs and the strategic plans for the Company's future development

The industry to which the Company belongs is the paper making industry, which is a light industry. The paper making industry is an important basic raw materials industry which is closely related to the national economy and social matter development. The paper making industry features capital and skills intensive characteristics with prominent economy of scale. Its growth rate is strongly and positively correlated to that of GDP.

VIII. Directors' Report

III. Prospect of the future developments of the Company (continued)

1. The development trend of the industry to which the Company belongs and the strategic plans for the Company's future development (continued)

As the extent and scope of influence under the global financial crisis is still highly uncertain, this will directly affect the pace of economic growth in China, and therefore make it difficult for the Company to accurately judge the development prospects of the papermaking industry. Nevertheless, as the papermaking industry in China is still undergoing a general direction of growth, the Board is of opinion that: after the trough experienced in the second half of 2008, papermaking industry will begin to stabilize; while the price for upstream raw materials will remain low for a certain period, the price for paper products will be able to maintain a reasonable balanced point of profitability; following the implementation of the new environmental protection policies and renewed efforts in implementing policies related to the papermaking industry, small-to-medium papermaking enterprises will face expansion limitation, challenges in economy of scale and heavier costs for environmental protection in their future development, which will lead to higher degree of industry concentration that is beneficial to enterprises with larger structural scale.

Based the above viewpoints, the Company will stick to its existing strategy already made to operate in an orderly way towards the development, mainly including the following aspects:

(1) Solving the bottleneck of the raw materials which restricts the Company's development and improving the control over product cost

The Company established the Zhanjiang wood pulp project and ancillary raw materials bases as its major development targets. The Company also accelerated the construction of the Hubei forestry project base, establishing the production chain of "forestry-pulp-paper integration" in order to eliminate any restrictions posed by upstream resource industries on the Company and strengthen the sustainable development capacity of the Company.

VIII. Directors' Report

III. Prospect of the future developments of the Company (continued)

1. The development trend of the industry to which the Company belongs and the strategic plans for the Company's future development (continued)

- (2) Dedicated to research and development and production of the advanced paper products and enhancing the Company's share in high-end PRC and international markets.

By relying on the existing national-level technological research and development centres and post-doctoral scientific research work stations, the Company put greater efforts to innovate, research and develop products, develop new advanced paper products, improve existing product quality; strengthen the omni-directional co-operations with the international advanced paper making enterprises, utilizing their advanced management models, production technologies and marketing experiences as much as possible; continue to increase the input in projects, expand production capacity, build paper making production lines with high technical input, further improve the Company 's production scale, product specifications, strive to step into the direction towards becoming a frontrunner in the international paper making industry in the future.

- (3) Paying close attention to environment protection construction, and committed to the goal of "energy saving, reduced emission and harmonious development"

The Company is devoted to its mission of "environmental protection comes first during enterprise's development", and adopts the goal of "energy saving, reduced emission and harmonious development". As the national environmental protection standard is raised and more efforts are made to administration, the Company will emphasize to develop the recycle economy, exchange of wastes, recycle use, enhance the resources utilization ratios to the greatest extent, put greater efforts in the construction of environmental protection project at the same time and guarantee the discharge of wastes in strict compliance with the standard.

VIII. Directors' Report

III. Prospect of the future developments of the Company (continued)

1. The development trend of the industry to which the Company belongs and the strategic plans for the Company's future development (continued)

(4) Continuous improving the Company 's operational efficiency

The Company will further optimize and promote production procedures and production equipment, thereby increasing output and improving production efficiency and products quality; further improve the Company's unifies administrative system, including the unified sales of products and unified procurement of raw materials; continue to optimize the portfolio of financial instruments and lower financial costs.

(5) Taking advantage of capital operation of the Company to realize low-cost expansion

As the Chinese paper industry is in the process of consolidation, the Company may engage in such an acquisition or merger if it fits the expansion strategies of the Company and optimizes the geographic layout of the Company to realize low-cost expansion and take advantage of capital operation of the Company accumulated throughout the years.

2. Consolidating the deep understanding of the Senior Management as to the future development trend, the Senior Management takes the view that, in relation to 2009: although the impact of the financial crisis will sustain, it is foreseen that the atmosphere of the industry will improve gradually in 2009 due to factors such as the reinforced macro-control measures of the State, the promulgation and implementation of encouraging policies and the forced elimination of lagging production capabilities through competition, and the further implementation of energy-saving and emission-reducing policies.

In 2009, Company will mainly launch the following works:

(1) To accelerate the structural adjustment and achieve scientific development

The Company will actively optimize the low value-added and resource-consuming products, eliminate obsolete techniques, equipment and raw materials, and improve technical equipment and product grade. In order to improve the quality and volume of the pulp, the headquarters of the Company, Wuhan Chenming Hanyang Paper Co., Ltd. and Shandong Chenming Paper Group Qihe Paperboard Co., Ltd. will upgrade the oxygen delignification techniques for some pulp production lines. Shouguang Chenming Art Paper Co., Ltd will carry out the project of changing first and second drying to vacuum rolls in light of the web break and low output problems in it dryer section. Jiangxi Chenming Paper Co., Ltd. and Fuyu Chenming Paper Co., Ltd. (富裕晨鳴紙業有限責任公司), two subsidiaries of the Company, will successfully carry out technological upgrade projects in light of their actual situation.

VIII. Directors' Report

III. Prospect of the future developments of the Company (continued)

1. The development trend of the industry to which the Company belongs and the strategic plans for the Company's future development (continued)

(2) To enhance independent innovation

Leveraging on the support and resources of the national-level technology centres and the post-doctoral technological research workstations, we will enhance cooperation with leading international papermaking enterprises as well as conduct collaboration and exchange ideas with PRC and international scientific research institutes. Through actively acquiring, promoting and applying new skills and technologies, we will fully utilize the scientific and technological resources to keep up with the forefront technologies of international research studies, aiming to capture an advanced position when competing for market share. With respect to talents, we will reinforce the establishment of technical teams and encourage innovation; more resources will be mobilized to nurture top-notch technical talents, and solicitation of technical professionals of all kinds will be carried out through all means without any prejudice. By exploiting the technological and research advantages of the Company, we can focus aggressively on the research and development of new products; based on prevailing market demands and after considering the actual state of affairs of the Company, we aim to broaden the Company's sources of revenue by actively developing new products with high added value and high technological content, including: high basis weight copperplate paper, anti-forgery white paper board and restickable business labels.

(3) To enhance energy saving and emission reduction and ability to sustain development

Energy saving, emission reduction and environmental protection are the highlighted items in the corporate development strategies of the Company. Reduction of water resources consumption continue to be the focal point of such work, through developing and promoting new technologies, techniques and equipment for water conservation, we aim to raise our ratio of repeated water utilization. We will also excel to perform well in the project “對製漿生產線原黑液提取工段進行的項目”. Inspection and supervision on the completion of energy saving and emission reduction at each unit will be regularly conducted by the environmental protection department, and practical experiences obtained from implementing such advanced energy saving and emission reduction technologies will be communicated in a timely manner, in order to ensure that these works are carried out in an effective way.

VIII. Directors' Report

III. Prospect of the future developments of the Company (continued)

1. The development trend of the industry to which the Company belongs and the strategic plans for the Company's future development (continued)

(4) To accelerate the forestry-pulp-paper integration

The Company speeds up the progress of the Zhanjiang pulp project by making great efforts in professional management, target management and planning management with careful organization and scientific deployment. The project site construction is in full swing and the "Five Accesses and One Leveling" will be completed as soon as possible in order to carry out wood chip yards, warehouse and plants construction, as well as complete labelling work for the technologies of main imported equipment such as pulping and recovery of black liquor. At the same time, the Company fully communicates with the domestic ancillary equipment suppliers and service providers to complete the tender biddings and plans in the course of the Zhanjiang Chenming pulp project, thereby speeding up the project progress. The Company puts great emphasis on the Zhanjiang Chenming and accelerates the construction of raw timber bases of the forestry subsidiaries in Hubei to build an industry chain of "forestry-pulp-paper integration".

(5) To strengthen corporate brand building to gain market share in the PRC and overseas markets

The Company builds its brand with product quality. The Company is determined to nurture "Chenming" as an internationally well-known brand by enhancing quality awareness across the Group to raise the product quality of the Company to the utmost top level among its counterparts. The Company also strengthens the building of its marketing team through optimization of the salary assessment plan to give incentive to the operating staff to improve their service quality in order to build up "Chenming" as brand of quality service. The Company strives to gain its market share in the PRC market and expands overseas at the same time by seriously studying and making good use of the PRC export policy, exploring export channels to gain its market share in the overseas market.

(6) Standardization of corporate management to fully enhance the operating quality

The Company consistently maintains a philosophy of people-oriented management and further explores and innovates new management models. The Company also strives to enhance its overall management level to quicken its convergence with international practices by making a reference to the management experience of the international leading enterprises.

VIII. Directors' Report

III. Prospect of the future developments of the Company (continued)

3. The risk factors in the course of realization of the future development strategies and operating targets of the Company

The competition of the paper product market becomes intense, exaggerated by the repercussions of the financial crisis in the fourth quarter of 2008, as the production capacity of the paper industry rapidly grows in recent years. The results of the Company will be undermined due to the increased volatility in prices of various paper products and the volatility of the raw material prices. In face of the intense market competition, the Company continues to develop new products with high added value and high technological level. However, the product development process covering from experiment, research, testing, mass production and gaining market recognition is so long that the Company is subject to the risk of product development failure at any time.

4. Future capital requirement, sources of funds and their planned use

The demand for capital of the Company is ever increasing as the Company and its operating scale continuously grows. As the largest paper making company and a company listed with A shares, B shares and H shares, the Company has a good reputation in the financial market and extensive financing sources. The Company will adopt the following effective sources of funds based on its growth and future development strategies:

- (1) Reinforcement for market sales - The Company will increase its sales revenue and put greater efforts in the recovery of receivables to speed up capital turnover, utilize capital potential and take full advantage of its own funds.
- (2) Taking advantage of the credibility and reputation of the Company - The Company will secure bank loans and syndicated loans and strengthen its internal financial control and enhance its capital utilization.
- (3) Optimization of financial structure to reduce finance expenses - The Company intends to issue of medium-term notes of not more than RMB 2,300 million to fund working capital and repay bank loans.
- (4) Reasonable use of proceeds from H shares issue - The Company will contribute capital into the Zhanjiang pulp project on schedule as set out in the prospectus.

VIII. Directors' Report

IV. Investments during the reporting period

1. Use of proceeds during the reporting period

The Company issued 355.7 million H shares in June 2008 with the issue price of HK\$ 9. The total proceeds from the issue were translated into RMB 2,831 million. The net proceeds less the expenses of RMB 103 million were RMB 2,728 million. As of 31 December 2008, RMB 746 million of the proceeds from the issue was used, of which, RMB 245 million was used to fund the working capital and RMB 501 million was used in the Zhanjiang pulp project primarily for land and plants areas construction. As of the end of the reporting period, the use of proceeds in the reporting period was as follows:

Unit: RMB in ten thousands

Project undertaken	Proposed investment	Project changes	Actual investment	Benefits realized	Whether progressing as scheduled	
					Whether progressing as scheduled	Whether progressing as scheduled with estimated benefits
Total proceeds	272,825				Use of total proceeds during the reporting period	74,565
					Accumulated use of total proceeds	75,565
Zhanjiang 700,000-tonne per annum pulp project	248,271	No	50,055	—	—	—
Supplement to working capital	24,554	No	24,510	—	—	—
Total	272,825	—	74,565	—	—	—
Explanation on failure to progress as scheduled and realize benefits (by project)	Nil					
Reasons for modification and modification procedures (by project)	Nil					
Use of unused proceeds and their status	The entire unused portion of the proceeds to be used in the Zhanjiang pulp project as set out in the prospectus was deposited at special deposit bank accounts.					

VIII. Directors' Report

IV. Investments during the reporting period (continued)

2. Other investments during the reporting period

- (1) The 120,000-tonne per annum coated art paper project was financed by self-owned funds and the actual total investment for the project was RMB 783 million. The project commenced operation in July 2008.
- (2) The 98,000-tonne de-ink waste paper project was financed by self-owned funds and the actual total investment for the project was RMB 263 million. The project commenced operation in April 2008.
- (3) The Grand View Hotel project was financed by self-owned funds and the actual total investment for the project was RMB 260 million. The hotel commenced operation in the reporting period.

3. Setting up of subsidiaries during the reporting period

- (1) 黃岡晨鳴林業發展有限責任公司 (Huanggang Chenming Arboriculture Co., Ltd.) - The company contributed capital to set up Huanggang Chenming Arboriculture Co., Ltd. on 23 January 2008. Its registered capital was RMB 10 million and it was fully owned by the Company. Its principal activities were nutrition of forest resources, cultivation, processing and sales of forest, and comprehensive development and utilization of forestry.
- (2) 咸寧晨鳴林業發展有限責任公司 (Xianning Chenming Arboriculture Co., Ltd.) - The Company contributed capital to set up Xianning Chenming Arboriculture Co., Ltd. on 1 September 2008. Its registered capital was RMB 10 million and it was fully owned by the Company. Its principal activities were nutrition of forest resources, cultivation, processing and sales of forest, forest and tree nursery construction, comprehensive development and utilization of forestry, and development and utilization of related ancillary products and related business consultation.
- (3) 黃岡晨鳴漿紙有限公司 (Huangguang Chenming Paper Pulp Co., Ltd.) - The Company contributed capital to set up Huangguang Chenming Paper Pulp Co., Ltd. on 26 September 2008. Its registered capital was RMB 20 million and it was fully owned by the Company. Its principal activities were construction of raw timber base, operation and acquisition of lumber, production of pulp and related products, preparation of production, processing and sales projects.

During the reporting period, for the establishment of indirectly owned subsidiaries by the directly owned subsidiaries of the Company please refer to the financial statements prepared in accordance with Accounting Standards for Business Enterprises and note 7 thereto.

VIII. Directors' Report

V. Auditors of the Company, Deloitte Touche Tohmatsu Certified Public Accountants Ltd. and Deloitte Touche Tohmatsu, issued standard auditors' reports for the year without qualified opinion on the Company

VI. Day-to-day operation of the Board

1. Board meetings and their resolutions

During the reporting period, the Board held nine meetings.

- (1) On 19 January 2008, the fifth session of the Board held its fifth meeting, at which, the principal matters considered included circulation and studying of the documents in respect of the information disclosed in the 2007 annual report, approval of the resolution to write off some bad debt loss of sales branches of the Company, approval of the resolution to increase the shareholding in Shandong Chenming Power Supply Holdings Co., Ltd. by the Company and approval of the resolution to invest in a forestry project company in Hubei by the Company. The related resolution announcement was published on China Securities Journal, Hong Kong Commercial Daily and <http://www.cninfo.com.cn> on 22 January 2008.
- (2) On 24 March 2008, the fifth session of the Board held its sixth meeting, at which, the principal matters considered included approval of the resolution to extend the expiry date of the related matters on H shares issue, approval of the resolution to extend the expiry date of the authorization to the chairman and deputy chairman of the Company to deal with the related matters on H shares issue with full power, approval of the resolution to apply for comprehensive banking credit facilities, approval of the resolution to provide guarantee for comprehensive banking credit facilities granted to the controlling subsidiaries of the Company, approval of the resolution to liquidate certain fixed assets and approval of the resolution to revise the Articles of Association (draft) of the Company and approval of notice of the first extraordinary shareholders' meeting. The related resolution announcement was published on China Securities Journal, Hong Kong Commercial Daily and <http://www.cninfo.com.cn> on 25 March 2008.

VIII. Directors' Report

VI. Day-to-day operation of the Board (continued)

1. Board meetings and their resolutions (continued)

- (3) On 11 April 2008, the fifth session of the Board held its seventh meeting, at which, the principal matters considered included approval of the 2007 Directors' report, approval of the 2007 general manager report, listening to the 2007 independent non-executive Directors' report of the Company, approval of the full text of the 2007 annual report and its summary, approval of the 2007 final accounts of the Company, approval of the profit appropriation plan for 2007 of the Company, listening to the conclusion on 2007 auditing from the accounting firms, approval of the resolution to appoint the auditors of the Company, approval of the resolution to appoint Senior Management of the Company, approval of the resolution to establish System of Work on Annual Report of independent Directors, approval of the resolution to establish Work Flow on Annual Report of the Audit Committee of the Board, approval of the Self Assessment Report on Internal Control of the Company, approval of the resolution to adjust the opening balance of certain items of the 2007 balance sheet of the Company and approval of the remuneration scheme on the Directors and Senior Management of the remuneration committee of the Board. The related resolution announcement was published on China Securities Journal, Hong Kong Commercial Daily and <http://www.cninfo.com.cn> on 15 April 2008.
- (4) On 29 May 2008, the fifth session of the Board held its eighth meeting, which was a procedural meeting held as stipulated by the related requirements of the listing rules of Hong Kong as part of the arrangement of issue of H shares of the Company. The main purposes of the meeting was to further confirm the related matters of issue and listing of H shares of the Company as approved at the first extraordinary shareholders' meeting in 2007, the first extraordinary shareholders' meeting in 2008, the twentieth meeting of the fourth session of the Board, the twentieth-first meeting of the fourth session of the Board and the sixth meeting of the fifth session of the Board and to make arrangements for the future actions on the listing of H shares. The related resolution announcement was published on China Securities Journal, Hong Kong Commercial Daily and <http://www.cninfo.com.cn> on 31 May 2008.
- (5) On 6 June 2008, the fifth session of the Board held its ninth meeting, at which, among other things, the notice of the 2007 annual general meeting was approved. The related resolution announcement was published on China Securities Journal, Hong Kong Commercial Daily and <http://www.cninfo.com.cn> on 7 June 2008.

VIII. Directors' Report

VI. Day-to-day operation of the Board (continued)

1. Board meetings and their resolutions (continued)

- (6) On 18 July 2008, the fifth session of the Board held its second extraordinary meeting, at which, the principal matters considered included circulation and studying of seven documents such as Opinion on Improvement of the Quality of Listed Company (《關於提高上市公司質量的意見》), Amendment VI to Criminal Law of the PRC and China Securities Regulatory Commission (the "CSRC") Announcement [2008] No.27, approval of the rectification report on corporate governance, approval of the resolution to establish the Special System to Take Precautions against Controlling Shareholders and Related Parties from Embezzling the Company's Fund (《防範控股股東及關聯方占用公司資金專項制度》) and approval of change of Senior Management of the Company. The related resolution announcement was published on China Securities Journal, Hong Kong Commercial Daily, <http://www.cninfo.com.cn> and Hong Kong Stock Exchange website (<http://www.hkex.com.hk>) on 19 July 2008.
- (7) On 1 August 2008, the fifth session of the Board held its third extraordinary meeting, at which, the principal matters considered included approval of the resolution to acquire assets by Fuyu Chenming Paper Co., Ltd. (富裕晨鳴紙業有限責任公司), a wholly-owned subsidiary of the Company. The related resolution announcement was published on China Securities Journal, Hong Kong Commercial Daily, <http://www.cninfo.com.cn> and Hong Kong Stock Exchange website (<http://www.hkex.com.hk>) on 4 August 2008.
- (8) On 28 August 2008, the fifth session of the Board held its tenth meeting, at which, the full text of 2008 interim report of the Company and its summary, and the resolutions to provide entrusted loans to subsidiaries by the Company, to obtain bank loans by the Company, to contribute capital for the establishment of Huanggang Chenming Paper Pulp Co., Ltd. (黃岡晨鳴漿紙有限公司) and to contribute capital for the establishment of Arjo Wiggins Chenming Specialty Paper Co., Ltd. (阿爾諾維根斯晨鳴特種紙有限公司) were approved. The related resolution announcement was published on China Securities Journal, Hong Kong Commercial Daily, <http://www.cninfo.com.cn> and Hong Kong Stock Exchange website (<http://www.hkex.com.hk>) on 29 August 2008.
- (9) On 30 October 2008, the fifth session of the Board held its eleventh meeting, at which, the full text of 2008 third quarterly report of the Company and its summary, and the resolutions to provide entrusted loans by the Company to its wholly-owned subsidiaries or controlling subsidiaries, and to contribute capital by the Company to increase the registered capital of Jilin Chenming Paper Co., Ltd. were approved. The related resolution announcement was published on China Securities Journal, Hong Kong Commercial Daily, <http://www.cninfo.com.cn> and Hong Kong Stock Exchange website (<http://www.hkex.com.hk>) on 31 October 2008.

VIII. Directors' Report

VI. Day-to-day operation of the Board (continued)

2. Implementation of resolutions of shareholders' meetings by the Board

The Board discharged its duties diligently as authorized by shareholders' meetings and the Articles of Association. It completed the principal tasks under the authorization of shareholders' meetings as follows:

- (1) the Board dealing with the matters with respect to issue of H shares with full power under the authorization granted at the first extraordinary shareholders' meeting in 2008 dated 11 April 2008

During the reporting period, the Board actively worked for the Hong Kong public offering of the global offering of H shares under the authorization of shareholders' meetings. It was completed in the period from 4 to 10 June 2008. The final issue price of H shares was determined at HK\$ 9.00 with a issue of 355,700,000 H shares by the Company, as approved by the Stock Exchange, and 35,570,000 overseas listed foreign shares (H shares) converted from state-owned shares and transferred to the National Social Security Fund Council of the PRC resulting from disposal of state-owned shares by the relevant shareholder. A total of 391,270,000 H shares were listed on the main board of Stock Exchange on 17 June 2008. The short name of the Company was Chenming Paper and its stock code was 1812. The related announcement was published on China Securities Journal, Hong Kong Commercial Daily, <http://www.cninfo.com.cn> and the Hong Kong Stock Exchange website on 17 June 2008.

- (2) Implementation of the profit appropriation plan for 2007

The 2007 annual general meeting resolved the 2007 profit appropriation plan of the Company: based on the total share capital of 1,706,345,941 shares as at the end of 2007, a cash bonus of RMB 1.60 (including tax) per 10 shares was to be paid to all shareholders and the total cash bonus in this distribution was RMB 273,015,350.56 (including tax), which represented 30.79% of the net profit attributable to the shareholders of the Company as set out in the 2007 combined financial statements and 37.43% of the net profit attributable to the equity holders of the parent company less statutory surplus reserve respectively. The balance of RMB 2,303,634,998.82 after the profit appropriation was retained for future distribution.

The 2007 bonus payment announcement was published by the Company on China Securities Journal, Hong Kong Commercial Daily, <http://www.cninfo.com.cn> and Hong Kong Stock Exchange website (<http://www.hkex.com.hk>) on 2 July 2008. The 2007 profit appropriation plan was implemented with 8 July 2008 as the book closure date of A shares and B shares.

VIII. Directors' Report

VI. Day-to-day operation of the Board (continued)

3. Discharge of duties by the audit committee of the Board

The audit committee of the Board discharged of its duties with diligence in accordance with the related requirements of the China Securities Regulatory Commission and the Shenzhen Stock Exchange and the work instructions of the audit committee of the Board as follows:

- (1) The audit committee completed the following major tasks during 2008:

it conducted pre-audit communication with external auditing institution engaged by the Company in respect of the 2007 financial report auditing on pre-auditing work, reviewed the 2007 auditing report and financial report and submitted such reports to the Board of the Company;

it reviewed the 2008 interim financial statements for the six months ended 30 June 2008, which was passed to the Board for approval.

- (2) Auditing work conducted on the 2008 financial report of the Company were as follows:

It reviewed the 2008 auditing plan and the related information of the Company with the auditing certified public accountants and the finance department of the Company prior to the on site audit and negotiated and determined the schedule of an audit of the 2008 financial statements of the Company with Deloitte Touche Tohmatsu Certified Public Accountants Ltd.;

it reviewed the draft of financial statements of the Company prior to an annual on site audit performed by the auditing certified public accountants and issued its approval to audit;

it kept in close contact with the auditors upon the annual on site audit and issued a letter to the auditors to urge the submission of the auditors' report on schedule;

it reviewed the financial statements of the Company again upon the issue of draft opinion on the annual audit by the auditing certified public accountants, and considered the financial statements of the Company true, accurate and complete to reflect the overall position of the Company;

at the second meeting of the audit committee in 2009, the auditors' report on the annual audit issued by the certified public accountants was approved and then was passed to the Board, and the audit fee for the year ended 31 December 2009 payable to the PRC and international auditors was approved and Deloitte Touche Tohmatsu Certified Public Accountants Ltd. was proposed to be re-appointed as the PRC auditors and Deloitte Touche Tohmatsu as the international auditors;

it reviewed the report on internal audit and internal control of the Company for the year ended 31 December 2008.

VIII. Directors' Report

VI. Day-to-day operation of the Board (continued)

4. Discharge of duties by the nomination committee of the Board

In the reporting period, the nomination committee held a meeting, at which, the principal matters considered included a discussion about appointment of Meng Feng and Han Chunlai as deputy general manager of the Company, which then was passed to the seventh meeting of the fifth session of the Board for approval.

5. Discharge of duties by the remuneration committee of the Board

The remuneration and assessment committee of the Company were primarily responsible for formulating the remuneration and assessment for the Directors and the Senior Management of the Company and formulating and examining the remuneration package of the Directors and the Senior Management of the Company, and accountable to the Board. In the reporting period, the remuneration and assessment committee formulated the 2007 remuneration package of the Directors and the Senior Management of the Company, which then was passed to the Board for approval, based on the production and operation conditions of 2007 and assessment of the Directors and the Senior Management of the Company. The 2008 remuneration proposal for Directors and Senior Management of the Company was formulated in view of the production and operation of the Company as well as the appraisal on Directors and Senior Management, and was submitted to the Board.

VII. The proposed profit distribution plan of 2008

According to the relevant requirements imposed by the State Ministry of Finance and Articles of Association, the distributable profit shall be the lower of the distributable profit as calculated in accordance with Accounting Standards for Business Enterprises and that calculated in accordance with International Financial Reporting Standards. The net profit attributable to shareholders realized in 2008 according to the Accounting Standards for Business Enterprises was RMB973,557,811.58, and net profit attributable to shareholders realized in 2008 according the International Financial Reporting Standards was RMB1,000,553,922.04; accordingly, the amount of distributable profit for this year was RMB973,557,811.58.

Based on the total share capital of 2,062,045,941 shares as at the end of 2008, a cash bonus of RMB0.5 (tax included for A shares) per 10 shares was to be paid to all shareholders and the total cash bonus in this distribution was RMB103,102,297.05 (tax included), which accounted for 10.59% of the net profit attributable to equity holders of the Company as set out in the combined financial statements of the Company prepared in accordance with Accounting Standards for Business Enterprises in 2008 after deducting appropriation to statutory reserves. The undistributed profit would be rolled over for distribution in subsequent years.

VIII. Directors' Report

VIII. The cash bonus of the Company in the last three years

Unit: RMB

Cash bonus year	Cash bonus	Net profit attributable to shareholders of the parent company for the cash bonus year	Ratio of cash bonus to net profit attributable to shareholders of the parent company	Remarks
2005	163,880,245.56	479,207,870.83	34.20%	—
2006	204,761,512.92	616,598,966.61	33.21%	—
2007	273,015,350.56	967,636,172.39	28.21%	31.35% of the net distributable profit attributable to shareholders realized in 2007

IX. Major suppliers and customers

The purchase from the largest supplier of the Group for 2008 was RMB 336 million, which accounted for 2.44% of the total purchase of the Group for the year and the total purchase from the five largest suppliers was RMB 1,403 million, which accounted for 10.17% of the total purchases of the Group for the year. None of the Directors, Supervisors and their respective associates, or, so far as the Directors were aware, shareholders who owned more than 5% of the Company's issued share capital had any interest in any of the five largest suppliers of the Group.

The sales to the largest customer of the Group for 2008 was RMB 193 million, which accounted for 1.24% of the total sales of the Group for the year and the total sales from the five largest customers was RMB 768 million, which accounted for 4.94% of the total sales of the Group for the year. None of the Directors, Supervisors and their respective associates, or, so far as the Directors were aware, shareholders who owned more than 5% of the Company's issued share capital had any interest in any of the five largest customers of the Group.

VIII. Directors' Report

X. Independent non-executive Directors' opinion on the regulatory compliance of properties with defective title of the Group

During the course of H shares issue in 2008, an valuation of the properties of the Group was carried out, the result of which showed that the Group still held certain parcels of land (including woodlands) and real estate ("Properties with Title Defects") which had not yet obtained the related title certificates. Apart from some properties that have obtained the related title certificates or the letters certifying the application for title certificates being processed from the local land administration authorities, despite the Group's continuous efforts, the title certificates of certain properties are still being processed until the latest practicable time prior to this report due to local land administration policies and administrative procedures taking much more time than expected.

1. With regard to the above circumstances, the Group primarily implemented the following remedies:
 - (1) The management for day-to-day operation of the Group attached great importance to the regulatory compliance of the related Properties with Title Defects by specifically setting up a corresponding focus working group, which was headed by the general manager of the Company. The heads of the related functional departments (including capital operation department and the finance department) of the Group and the related management of the controlling subsidiaries of the Group actively reported to and communicated with the local government functional authorities to strive for the government's coordination in resolving the issue.
 - (2) Currently, the compliance matters of the land of the related Properties with Title Defects have obtained the letters certifying the application for title certificates being processed from the local land administration authorities: The self-owned land of the Group for production use is currently completing land supply procedures in compliance with the related laws. The titles of the land are well defined without disputes which can lead to application for land use right certificates after the land use rights are legally granted. Other land for non-production use is currently completing related ownership transfer procedures and/or the title certificates application procedures which are free from legal obstacles. The Group will legally apply for title certificates of the related lands and properties in a timely manner in accordance with the related requirements of the title certificate application procedures.

VIII. Directors' Report

X. Independent non-executive Directors' opinion on the regulatory compliance of properties with defective title of the Group (continued)

2. Through the above-mentioned work, the related government departments gained an understanding of the Group's (including the controlling subsidiaries, same below) Properties with Title Defects while providing active assistance and guidance in the light of the historical reasons which led to title defects. Meanwhile, after the examination of the focus working group of the Company, the Company confirmed that the Properties with Title Defects did not provoke material ownership disputes and the related government departments had not imposed any administrative penalties on the Group with regard to the related Properties with Title Defects issue.

According to Hylands Law Firm, the advisor on PRC law of the Company, despite the Properties with Title Defects, the Group is unlikely liable to related administrative penalties.

3. In order to further rectify non-compliance relating to the Properties with Title Defects of the Group and practically protect the legal interests of the shareholders of the Group, Shouguang Chenming Holdings Col., Ltd. (hereinafter referred to as "Chenming Holdings"), the controlling shareholder of the Company, issued the related supplementary indemnity letter again as requested by the Company.
 - (1) With regard to the Properties with Title Defects owned by the Group, should the Group decide to transfer the ownership of or dispose of the property but no other buyers are available, Chenming Holdings will legally purchase the transferred Properties with Title Defects with reference to the related asset valuation results.
 - (2) Before the Company legally dispose of or transfer the ownership of that property, should any economic losses (including but not limited to compensations, fines and removal costs, etc.) be incurred to the Group arising from the Properties with Title Defects, such economic losses will be born by Chenming Holdings accordingly.

Hylands Law Firm, the advisor on PRC law of the Company, confirms that the related indemnity letter issued by Chenming Holdings is legally effective.

VIII. Directors' Report

X. Independent non-executive Directors' opinion on the regulatory compliance of properties with defective title of the Group (continued)

To summarize the above, as the independent non-executive Directors of the Company, we are of the view that:

1. The Company's management has actively strived to obtain the title certificates for the Properties with Title Defects and have made great achievements. Also, the Company will continue to work hard in rectifying non-compliance of the properties that remain title defective in accordance with the related laws and regulations.
2. The Properties with Title Defects do not provoke material ownership disputes and do not pose tangible impacts on the production and operation of the Company and the Company as going concern. The related government departments have so far not imposed any administrative penalties on the Company with regard to the related Properties with Title Defects. Also, according to Hylands Law Firm, the advisor on PRC law of the Company, the Group is unlikely liable to related administrative penalties due to the matters relating to the Properties with Title Defects.
3. The related indemnity letter issued by Chenming Holdings can effectively prevent the Group from bearing any legal risks and economic losses arising from the Properties with Title Defects, thus protecting the interests of the Company and its shareholders.

Independent non-executive Directors

Diao Yuntao

Wang Zhihua

Zhou Chengjuan

Wang Yumei

Lau Ying Kit

8 April 2009

IX. Supervisory Committee's Report

I. Performance of duties

In the reporting period, all the Supervisors, who are accountable to the shareholders, performed their duties in accordance with Company Law, the Articles of Association, and Procedural Rules for Supervisory Committee's Meetings, and under the principle of diligence. They monitored whether the business activities were lawfully operated, and supervised the financial management and connected transactions of the Company. In the reporting period, they examined and supervised the subsidiaries and branch companies in terms of accounting, raw materials purchase, sales of goods, and connected transactions to provide strong protection for the lawful operation and healthy development of the Company.

II. Meetings of the Supervisory Committee

1. The fourth meeting of the fifth session of the Supervisory Committee was held on 19 January 2008. The resolution regarding to writing off part of bad debts of sales branches of Shandong Chenming Paper Holdings Limited was considered and passed at the meeting. The related resolution announcement was published on China Securities Journal, Hong Kong Commercial Daily and <http://www.cninfo.com.cn> on 22 January 2008.
2. The fifth meeting of the fifth session of the Supervisory Committee was held on 11 April 2008. Resolutions regarding to 2007 financial report, 2007 financial statements of the Company, Supervisory Committee' report for 2007, the 2007 annual report, and adjustments of opening balance on 2007 balance sheet was considered and passed at the meeting. The related resolution announcement was published on China Securities Journal, Hong Kong Commercial Daily and <http://www.cninfo.com.cn> on 9 May 2008.
3. The sixth meeting of the fifth session of the Supervisory Committee was held on 27 April 2008. The 2008 first quarter report of the Company and its original text were considered and passed at the meeting.
4. The seventh meeting of the fifth session of the Supervisory Committee was held on 28 August 2008. The 2008 interim report of the Company and its summary were considered and passed at the meeting.
5. The eighth meeting of the fifth session of the Supervisory Committee was held on 30 October 2008. The 2008 third quarter report of the Company and its original text were considered and passed at the meeting.

IX. Supervisory Committee's Report

III. Independent opinion of the Supervisory Committee

1. Operation According to the law

- (1) In the reporting period, the Company conducted its businesses according to Company Law, Securities Law, Articles of Association of the Company and the related national laws and regulations. Information disclosures were conducted under the principles of truthfulness, completeness, accuracy, and timeliness. No false or misleading information was released.
- (2) The Board undertook all of the rights and responsibilities set out by Company Law, Securities Law, and Articles of Association of the Company, and fully implemented the resolutions passed by the shareholders' meetings and Board meetings. The decision making processes were lawful with timely consideration and approval of the production targets, sustainable development measures, operation according to the law and standardization operation. A comprehensive internal control system was established to ensure a healthy development of the Company. The management of the Company was able to perform their duties as stipulated in the Articles of Association of the Company and executed the resolutions of the Board. No contravention of laws or regulations or the Articles of Association nor acts detrimental to the interests of the Company were found.

2. Financial position inspection

The financial statements of the Company were audited by Deloitte Touche Tohmatsu Certified Public Accountants Ltd. and Deloitte Touche Tohmatsu, which issued standard auditors' reports with unqualified opinion on them upon auditing. In the opinion of the Supervisory Committee, the auditors' report gave a true and fair view of the financial conditions and operating results of the Company.

3. Use of proceeds

The actual use of the proceeds from the latest fund raising activity was consistent to their intended use.

4. Significant purchase or sales of assets

The consideration for the purchase of assets by the Company was fair and reasonable and no insider trades and connected transactions, which were detrimental to the interests of any shareholders or resulted in loss of assets of the Company, were found.

5. Connected transactions

The connected transactions were entered into at arm's length and were not detrimental to the interests of the Company and the shareholders.

X. Material Matters

I. There was no material litigation or arbitration of the Company during the reporting period.

II. Liquidation of controlling subsidiaries in the reporting period

Xiangfan Chenming Copperplate Paper Co., Ltd. (“Xiangfan Chenming”), an indirect controlling subsidiary of the Company, was incorporated in 1998 with registered capital of RMB32.2580 million. The Company took 20% of the total capital of Xiangfan Chenming through injection of intangible assets of RMB6.452 million. Wuhan Chenming Hanyang Paper Co., Ltd., a company held by the Company as to 50.93%, took 31% the total capital of Xiangfan Chenming through investment in kind and cash of RMB10 million. Hubei Hanyang Paper Mill took 19% of the total capital of Xiangfan Chenming through capitalization of debts of RMB6.129 million. Xiangfan Bailan Group Co., Ltd. took 30% of the total capital of Xiangfan Chenming through investment in kind of RMB9.677 million. Xiangfan Chenming suffered from out-of-date equipment and a single product mix with a production capacity of less than 20,000 tonnes and it should be eliminated according to the national industrial policies. At present, Xiangfan Chenming has stopped production and entered into the liquidation process as approved at its shareholders’ meeting.

During the reporting period, the liquidation process was completed. For details, please refer to PRC Auditors’ Report and Financial Statements and Note VII thereto Prepared in Accordance with Accounting Standards for Business Enterprises in this Report.

X. Material Matters

III. Significant purchase or sales of assets and merger and acquisition in the reporting period

1. The fifth meeting of the fifth session of the Board considered and approved the resolution to further increase the shareholding in Shandong Chenming Power Supply Holdings Co., Ltd. (“Chenming Power”) by the Company. In the reporting period, the Company completed the related shareholding increase. The Company purchased 2,378,000 state-owned shares, representing 2.39% of the registered share capital, and 33,175,000 collective shares, representing 33.32% of the registered share capital, of Chenming Power, from the State-owned Assets Supervision and Administration Commission of Shouguang City and the People’s Government of Shouguang City respectively. The consideration for the shares was determined based on the net assets of Chenming Power. The shares of Chenming Power held by the Company were increased to 91,326,061 shares and the shareholding in Chenming Power of the Company was increased to 86.71% from 51%. The increase in shareholding constituted no change to the business of the Company on going concern and to the management of the Company. Under Rule 10.1.3 (V) of the Listing Rules of the Shenzhen Stock Exchange, this constituted connected transaction for which independent Directors had expressed their independent opinion and the Company disclosed information related to this connected transaction. For details, please refer to the relevant announcements published on China Securities Journal, Hong Kong Commercial Daily and <http://www.cninfo.com.cn> on 22 January 2008.
2. On 1 August 2008, the third extraordinary meeting of the fifth session of the Board considered and approved the related resolution regarding to the related assets acquisition of Fuyu Chenming Paper Co., Ltd. (“Fuyu Chenming”), a wholly-owned subsidiary of the Company. According to the net assets value and auction price of the relevant assets acquired, the assets acquisition involved a total amount of RMB208.02 million. At the beginning of August 2008, the management executed the relevant agreements for acquisition of such assets in full compliance with the mandate granted by and amount estimated by the Board. For details, please refer to the relevant announcements published on China Securities Journal, Hong Kong Commercial Daily and <http://www.cninfo.com.cn> on 2 August 2008.

X. Material Matters

IV. Major connected transactions

1. For material connected transactions of the Group during the reporting period under the relevant rules of the Shenzhen Stock Exchange, please refer to the relevant information set out in Part III “1” of this section. Save for such connected transactions, the Group had no other material connected transactions.
2. **Continuing connected transactions as defined under the listing rules of the Hong Kong Stock Exchange**

For the year ended 31 December 2008, the following non-exempt continuing connected transactions were subject to reporting requirements under the Hong Kong Listing Rules of the Stock Exchange. Such transactions were conducted in the ordinary course of business of the Group and on commercial terms fair and reasonable to shareholders.

Sale of paper products by Jiangxi Chenming to Sappi and/or its associates

On 3 December 2004, Jiangxi Chenming Paper Co., Ltd. (“Jiangxi Chenming”), the Company, Moorim Paper Co., Ltd. (“Moorim Paper”) and Sappi China Holdings BV (“Sappi China”) entered into a Sales and Distribution Agreement.

Jiangxi Chenming is owned as to 51% by us, 34% by Sappi whose beneficial owners are all Independent Third Parties to the Company, 7.5% by Moorim Paper and 7.5% by IFC. The principal businesses of Sappi and Moorim Paper are making and sales of various paper products. According to Rule 14A.11 of the Hong Kong Listing Rules, Sappi is a connected person of us. Based on information currently available, Sappi China Holdings BV (“Sappi China”) is an associate of Sappi and therefore the sales of products by Jiangxi Chenming to either Sappi or Sappi China (the “Sappi Sales”) in its ordinary and usual course of business will constitute continuing connected transactions under the Hong Kong Listing Rules. Pursuant to the Sales and Distribution Agreement entered into by the parties, Jiangxi Chenming engaged three sole distributors in China, South Korea and overseas markets respectively to reduce distribution costs. Such arrangements will shorten the distribution cycle and assist Jiangxi Chenming in more efficient and effective distribution work in its expansion into overseas markets, and therefore strengthen its market position within the paper making industry. During the reporting period, Sappi recorded total sales of RMB157.2 million, accounting for 1.02% of the total sales of the Group for the year.

Details of the above non-exempt continuing connected transaction are set out in the section headed “Connected Transactions” in the Prospectus of the Company.

X. Material Matters

IV. Major connected transactions (continued)

The independent non-executive Directors of the Company reviewed the connected transactions of the Group and confirmed that:

- the transactions were conducted in the ordinary course of business of the Group;
- the transactions were carried out on normal commercial terms; and
- the transactions were carried out on the terms of the related agreements and the terms were fair and reasonable and in the interests of the shareholders as a whole.

The auditors of the Company reviewed the connected transactions and confirmed to the Board that:

- the transactions were approved by the Board;
- the transactions were carried out based on the pricing policy of the Company;
- the transactions were carried out on the terms of the related agreements; and
- the amounts of the transactions were not more than the annual cap amounts as approved by Hong Kong Stock Exchange.

X. Material Matters

V. Significant contracts and their performance

1. External guarantees

- (1) During the reporting period, the Company did not provide any guarantee to external parties (excluding the guarantees provided to its subsidiaries) and provide any guarantees against the rules and regulations.

As at 31 December, 2008, the Company provided guarantees to its subsidiaries amounting to RMB784,094,400, representing 6.4% of the net assets attributable the shareholders of the parent company.

Name of the subsidiaries	The amounts being guaranteed (RMB in ten thousand)
Jiangxi Chenming Paper Co., Ltd.	34,500.00
Jilin Chenming Paper Co., Ltd.	26,879.52
Wuhan Chenming Hanyang Paper Co. Ltd.	4,341.73
Zhanjiang Chenming Paper Pulp Co., Ltd.	10,683.46
Heze Chenming Panels Co., Ltd.	2,004.73
Total	78,409.44

- (2) The first extraordinary shareholders' meeting for 2008 approved a resolution regarding to provision of guarantee for banking facilities granted to its subsidiaries. The Company provides guarantee for banking facilities granted to its subsidiaries in 2007, which will expire successively. In order to ensure the normal production and management of each of its subsidiaries, the Company intends to continue to provide guarantee for RMB comprehensive banking facilities granted to the related subsidiaries in 2008, with the total value of RMB 2.25 billion under guarantee and effect of one year therefrom. The related announcement was published on China Securities Journal, Hong Kong Commercial Daily and www.cninfo.com.cn on 12 April 2008.

2. Entrusted loans

During the reporting period, in order to save financial expenses, increase incomes, and regulate funds exchanged between the Company and its subsidiaries at the same time, the Company granted entrusted loans from banks of RMB1,790 million to Jiangxi Chenming Paper Co., Ltd, Wuhan Chenming Hanyang Paper Co., Ltd and Heze Chenming Panels Co., Ltd subsidiaries of the Company, for their use.

During the reporting period, save for the above entrusted loans to the controlling subsidiaries, the Company had no other entrusted wealth management matters or those incurred in prior periods extending into the reporting period.

X. Material Matters

V. Significant contracts and their performance (continued)

3. Other significant contracts

- (1) During the reporting period, Zhanjiang Chenming Paper Pulp Co., Ltd., a subsidiary of the Company, entered into Zhanjiang Pulp Project Syndicated Loan Contract (《湛江木漿專案銀團貸款合同》) and Syndicated Loan Mortgage Contract (《銀團貸款抵押合同》) with a syndicate of banks, which included China Development Bank, Zhanjiang branch of Agricultural Bank of China, Zhanjiang branch of Industrial and Commercial Bank of China Limited, Zhanjiang branch of China Construction Bank Corporation, Qingdao Branch of China Merchants Bank Co., Ltd., and Shenzhen Branch of China CITIC Bank Corporation Limited. The syndicated loan was intended to finance the project of Zhanjiang Chenming Paper Pulp. In the meantime, the Company entered into Syndicated Loan Guarantee Contract (《銀團貸款保證合同》) with a syndicate of banks, pursuant to which, the Company provided joint responsibility guarantees to a syndicate of banks for Zhanjiang Chenming for the insolvent part of the debts except for the future asset pledged as collateral. The details of the loan agreement were published in China Securities Journal, Hong Kong Commercial Daily and the website of CHINF (www.cninfo.com.cn) on 22 January 2008.
- (2) During the reporting period, the Company intended to build the Zhanjiang 700,000-tonne pulp project as soon as possible. Therefore, Zhanjiang Chenming Paper Pulp Co., Ltd (湛江晨鳴漿紙有限公司), a wholly-owned subsidiary of the Company, and MetsoFiberKarlstadAB, MetsoPaperValkeakoskiOy, MetsoPaper (China) Co., Ltd, MetsoPaperSundsvallAB.MetsoPowerOy (all of them were relevant subsidiaries of Meizhuo Papermaking Machinery Co., Ltd. (美卓造紙機械有限公司)) entered into procurement contracts for pulp board machines, alkali retrieval stoves, cook and stream apparatus, wash, select and bleach apparatus, wood-cutting apparatus respectively on 13 August 2008. The contracts involve in the total cost equivalent to 194 million euro and come into force from the date on which both parties sign, with effective period from August 2008 to October 2010. The details of the loan agreement were published in China Securities Journal, Hong Kong Commercial Daily, the website of CHINF (www.cninfo.com.cn) and Hong Kong Stock Exchange website (<http://www.hkex.com.hk>) on 21 August 2008.

X. Material Matters

VI. Commitments by holders of non-tradable shares during the reform of conversion

1. Commitments during the reform of Conversion

The Company completed the reform of Conversion on 29 March 2006. State-owned Assets Supervision and Administration Commission of Shouguang City, the controlling shareholder, and other holders of non-tradable shares transferred some of their shares to all of the shareholders of tradable A Shares in the proportion of 2.6 shares for every 10 tradable A Shares. During the reporting period, the controlling shareholder of the Company changed to Shougoang Cheming Holdings Co., Ltd. from State-owned Assets Supervision and Administration Commission of Shouguang City. Shougoang Cheming Holdings Co., Ltd. promises it will fulfill the following commitments made by the original controlling shareholder, State-owned Assets Supervision and Administration Commission of Shouguang City, during the reform of Conversion:

- (1) According the audited financial reports (standard and without qualified opinion) of the Company for 2005-2007, if the compound annual growth rate of the Company's net profit for 2005 to 2007 is less than 20%, then it shall be determined the register day for the top-up matching price share right (i.e. the tenth trading day of disclosing the 2007 annual report) after the fifth trading day of disclosing the 2007 annual report and disclosed the top-up matching price announcement and complete the implementation of top-up matching price on the first trading day after the top-up matching price share right register day. Chenming Holdings will transfer, without consideration, 5% of the total number of tradable A Shares on share right register day to implement the scheme to holders of tradable A Shares with no restricted conditions registered after the close of register day to top-up matching-price share right. (If this scheme is implemented between stock right register day to the top-up matching price share right register day, there is a change in capital due to bonus issue and transfer to capital surplus, it shall adjust number of shares for this top-up matching price arrangement.)
- (2) Shares held by Chenming Holdings shall not be listed and traded within 48 months from the date of the reform of Conversion.
- (3) After this reform scheme of Conversion has been approved to implement, Chenming Holdings proposed the bonus distribution at the shareholders' meetings of the Company for 2005, 2006 and 2007, proposing profit allocation proportion not lower than 30% of those of realized distributable profit in those years (i.e. net profit for those years set out in the income statement net of amount transferred to statutory common reserve fund and statutory public welfare reserve) and guarantee to vote for this proposal when proposed at the shareholders' meeting.

X. Material Matters

VI. Commitments by holders of non-tradable shares during the reform of conversion (continued)

2. Undertakings and their performance during the reporting period

The financial reports of the Company for the three years ended from 2005 to 2007 were audited by Deloitte Touche Tohmatsu Certified Public Accountants Ltd., while it issued auditors' reports of 德師京(審報字(06)第173號·德師報(審)第PB006號·德師報(審)字(08)第P0262號 respectively, all of them were of unqualified opinion. The net profit of Company under Accounting Standards for Business Enterprises amounted to RMB 503,721,298.14, RMB 602,433,342.24, RMB 602,967,195.37 and RMB 967,636,172.39 in 2004, 2005, 2006 and 2007 respectively.

The Company's compound annual growth rate of net profit from 2005 to 2007 amounted to 24.31% (i.e. higher than 20%) and did not trigger the performance condition of top-up price matching shares, thus Chenming Holdings was not required to further increase the matching price.

18,653,854 shares were kept under the custody of the Shenzhen branch of China Securities Depository and Clearing Corporation temporarily to be used for top-up price matching in the undertakings. The temporary custody of these shares was released during the reporting period and the nature of such shares remained restricted state-owned legal person shares.

For the end of the reporting period, Chenming Holdings, the controlling shareholders of the Company has fulfilled all the commitments which made during the reform of Conversion, except the commitment of "Shares held by Shouguang Chenming Holdings Co., Ltd. shall not be listed and traded within 48 months from the date of reform of Conversion".

VII. The accounting firm engaged by the Company during the reporting period

At the seventh meeting of the fifth session of the Board, the Company approved the resolution to engage an accounting firm (Deloitte Touche Tohmatsu Certified Public Accountants Ltd.) as auditing agency for the 2008 financial information of the Company to provide auditing service for one year, at the auditor's fee of RMB4,800,000. Meanwhile, the Company bears traveling expenses of personnel from such accounting firm, which was approved at the 2007 general shareholders' meeting of the Company. This accounting firm has been acting continuously as auditing agency for the Company for 5 years since 2004.

X. Material Matters

VIII. During the reporting period, the Board and the Directors of the Company were not fined by China Securities Regulatory Commission nor condemned by any stock exchange.

IX. Launch various channels to communicate and strengthen investor's relation management

During the reporting period, the Board of the Company not only promptly disclosed sufficient information in strict compliance with the relevant regulations, but also launched various channels to actively manage investor's relations, and strengthen the direct communications with investors, news media and the public, thereby fully introducing and displaying the outstanding image of the Company, as well as our advantages over other players, our continuous improving results and unlimited development prospects which lead investors to further understand the investment value of the Company in depth. Our disclosure of information was comprehensively assessed by the Shenzhen Stock Exchange as "good" for seven years in succession (2001-2007).

In 2008, the receiving organization under the Company' general headquarters handled more than 100 visits for individual investor surveys and studies. The Company fully utilized investor's special telephone lines, strengthened the telephone communication with shareholders, and answered queries from each shareholder patiently. By way of exchanges through the network, an investor's relation forum was set up on the Company's websites where six personnel were arranged to be responsible for answering questions of various aspects from investors.

X. Material Matters

IX. Launch various channels to communicate and strengthen investor's relation management (continued)

Reception of activities including research, communication and interviews

Time of reception	Place of reception	Manner of reception	Received parties	Main contents of conversation and information provided
January 2008	Shouguang, Shandong	Investigation and research on site	Researchers of Changjiang River Securities, Beijing office of Gao Ling Capital and Eastern securities	Recent development of the industry and development trend in the future, production and management of the company, direction of strategic development in the future and progress of issuance of H shares
March 2008	Shouguang, Shandong	Investigation and research on site	CITIC Securities' researchers and investment managers of Huatai Assets Management Co., Ltd	Recent development of the industry and development trend in the future, production and management of the company, direction of strategic development in the future and progress of issuance of H shares
March 2008	Shouguang, Shandong	Investigation and research on site	Institutional researchers and fund managers of 國泰君安，中投證券，國金證券，招商證券，長盛基金，嘉實基金 and 諾安基金	Recent development of the industry and development trend in the future, production and management of the company, direction of strategic development in the future and progress of issuance of H shares
March 2008	Shouguang, Shandong	Investigation and research on site	Researchers and fund managers of 中金公司，華寶興業基金，寶鋼財務，富國基金LibraCap(QFII) and 嘉實基金	Recent development of the industry and development trend in the future, production and management of the company, direction of strategic development in the future and progress of issuance of H shares
March 2008	Shouguang, Shandong	Investigation and research on site	Institutional researchers and investment managers of 長江證券，泰達荷銀基金，博時基金，第一創業證券，工銀瑞信基金 and 兵器財務公司	Recent development of the industry and development trend in the future, production and management of the company, direction of strategic development in the future and progress of issuance of H shares

X. Material Matters

IX. Launch various channels to communicate and strengthen investor's relation management (continued)

Reception of activities including research, communication and interviews (continued)

Time of reception	Place of reception	Manner of reception	Received parties	Main contents of conversation and information provided
March 2008	Shouguang, Shandong	Investigation and research on site	Researchers and fund managers of 中銀國際，天弘基金，華安基金，海富通基金，中海基金，平安資產，Lehman Brothers and 長城基金	Recent development of the industry and development trend in the future, production and management of the company, direction of strategic development in the future and progress of issuance of H shares
June 2008	Shouguang, Shandong	Investigation and research on site	Sales director and analysts of Merrill Lynch Securities and representatives of 富達資產管理公司	Recent development of the industry and development trend in the future, production and management of the company, direction of strategic development in the future and progress of issuance of H shares
June 2008	Shouguang, Shandong	Investigation and research on site	Investment directors and industry researchers of 中海基金	Recent development of the industry and development trend in the future, production and management of the company, direction of strategic development in the future and progress of issuance of H shares
September 2008	Shouguang, Shandong	Investigation and research on site	Researchers of 台證綜合證券	Recent development of the industry and development trend in the future, production and management of the company, and direction of strategic development in the future
September 2008	Shouguang, Shandong	Investigation and research on site	Vice-president of Deutsche Bank	Recent development of the industry and development trend in the future, production and management of the company, and direction of strategic development in the future

X. Material Matters

IX. Launch various channels to communicate and strengthen investor's relation management (continued)

Reception of activities including research, communication and interviews (continued)

Time of reception	Place of reception	Manner of reception	Received parties	Main contents of conversation and information provided
September 2008	Shouguang, Shandong	Investigation and research on site	Customers of 中金證券 (橡樹資本上市證券公司)	Recent development of the industry and development trend in the future, production and management of the company, and direction of strategic development in the future
October 2008	Shouguang, Shandong	Investigation and research on site	Study group of Hong Kong analysts	Recent development of the industry and development trend in the future, production and management of the company, and direction of strategic development in the future
November 2008	Shouguang, Shandong	Investigation and research on site	Analysts of 中國銀河證券股份有限公司	Recent development of the industry and development trend in the future, production and management of the company, and direction of strategic development in the future
December 2008	Shouguang, Shandong	Investigation and research on site	Investment directors of 海角資產管理有限公司	Recent development of the industry and development trend in the future, production and management of the company, and direction of strategic development in the future
December 2008	Shouguang, Shandong	Investigation and research on site	Shareholders of the Company	Recent development of the industry and development trend in the future, production and management of the company, and direction of strategic development in the future
December 2008	Shouguang, Shandong	Investigation and research on site	Researchers of research institute of Shenyin Wanguo	Recent development of the industry and development trend in the future, production and management of the company, and direction of strategic development in the future

X. Material Matters

X. Other material matters

Independent Directors of the Company expressed the following opinions on the use of funds by related parties and external guarantee provided during the reporting period:

Under the requirements of the listing rules of the Shenzhen Stock Exchange in relation to connected transactions, except for the matter set out in III.1 of section X of the Report, the Company had no material connected transactions, on which independent non-executive Directors of the Company had expressed their independent opinion, during the reporting period; according to the requirements of the Accounting Standards for Business Enterprises, except for the ordinary connected transactions between the Company and its controlling subsidiaries and interested companies of the Company (for details, please refer to PRC Auditors' Report and Financial Statements and Note VIII thereto Prepared in Accordance with Accounting Standards for Business Enterprises), there were no use of funds by controlling shareholders and other related parties; while the connected transaction took place were true and accurate reflection of the ordinary connected transactions of the Company that were fair and reasonable and in compliance with the relevant requirements of the Company Law and the Articles of Association, the transaction price was objective and just and without prejudice to the interests of the Company and its shareholders (especially minority shareholders and non-related shareholders).

Upon validation, except for the above guarantees provided to controlling subsidiaries, the Company had provided RMB0 of external guarantee for the period of and accrued up to 2008. The Company strictly followed the relevant requirements of the Notice on Regulation of External Guarantee Provided by Listed Companies (Zheng Jian Fa [2005] No.120) (《關於規範上市公司對外擔保行為的通知》(證監發[2005]120號)) and the Articles of Association to earnestly perform its information disclosure obligations in respect of external guarantees and honestly provided information concerning all external guarantee matters to the public accountant. During the reporting period, the guarantee provided guarantee for controlling subsidiaries for their ordinary production and operation and to meet reasonable funding needs, the decision procedures were legal and without prejudice to the interests of the Company and the shareholders of the Company (especially minority shareholders).

X. Material Matters

XI. Index of information disclosure in 2008

Announcement date	Subject matter	Media for publication
2008-1-10	Clarification announcement	C12 of China Securities Journal, B6 of Hong Kong Commercial Daily http://www.cninfo.com.cn
2008-1-22	Announcement in respect of the resolutions passed at the fifth meeting of the fifth session of the Board Announcement in respect of the resolutions passed at the fifth meeting of the fourth session of the Board Connected transaction announcement and announcement in respect of Zhanjiang Chenming and the syndicated loan agreement Independent opinion of the independent Directors on writing off bad debts of sales branches Independent opinion of the independent Directors on further increase in the shareholdings of the Company in Chenming Power	D045 of China Securities Journal, B3 of Hong Kong Commercial Daily http://www.cninfo.com.cn
2008-2-26	Indicative announcement in respect of the listing of foreign shares listed overseas approved by the China Securities Regulatory Commission	D005 of China Securities Journal, A9 of Hong Kong Commercial Daily http://www.china.com.cn
2008-3-25	Announcement in respect of the granting of financial subsidy Announcement in respect of the resolutions passed at the sixth meeting of the fifth session of the Board Notice in respect of the convention of 2008 first extraordinary general meeting	C12 of China Securities Journal, B7 of Hong Kong Commercial Daily http://www.cninfo.com.cn

X. Material Matters

XI. Index of information disclosure in 2008 (continued)

Announcement date	Related matters	Media for publication
2008-3-26	Announcement in respect of the external guarantees	D141 of China Securities Journal, B9 of Hong Kong Commercial Daily http://www.cninfo.com.cn
2008-4-12	Announcement in respect of the resolutions passed at the 2008 first extraordinary general meeting	C045 of China Securities Journal, A3 of Hong Kong Commercial Daily http://www.cninfo.com.cn
2008-4-15	Summary of 2007 annual report Announcement in respect of the resolutions passed at the seventh meeting of the fifth session of the Board and announcement in respect of the resolutions passed at the fifth meeting of the fifth session of the Supervisory Committee	D053 of China Securities Journal, A7 of Hong Kong Commercial Daily http://www.cninfo.com.cn
2008-4-24	Indicative announcement in respect of the change of the disclosure date of 2008 first quarter report	A28 of China Securities Journal, A9 of Hong Kong Commercial Daily http://www.cninfo.com.cn
2008-4-29	Announcement in respect of the summary of 2008 first quarter report of estimated increase in the performance results	D076 of China Securities Journal, A10 of Hong Kong Commercial Daily http://www.cninfo.com.cn
2008-5-10	Announcement in respect of the undertakings associated with the share reform Announcement in respect of the change of on-going monitoring sponsor for the share reform	C005 of China Securities Journal, A9 of Hong Kong Commercial Daily http://www.cninfo.com.cn

X. Material Matters

XI. Index of information disclosure in 2008 (continued)

Announcement date	Related matters	Media for publication
2008-5-24	Announcement in respect of the application of the issue and listing of the H shares of the Company considered by the Hong Kong Stock Exchange and the web proof information pack of H shares issue	C021 of China Securities Journal, A10 of Hong Kong Commercial Daily http://www.cninfo.com.cn
2008-5-31	Announcement in respect of the resolutions passed at the eighth meeting of the fifth session of the Board	C009 of China Securities Journal, B6 of Hong Kong Commercial Daily http://www.cninfo.com.cn
2008-6-4	Announcement in respect of the related matters of H share prospectus, price range of H shares and the H share Hong Kong Public Offering	B of China Securities Journal, B3 of Hong Kong Commercial Daily http://www.cninfo.com.cn http://www.hkex.com.hk
2008-6-7	Announcement in respect of the resolutions passed at the ninth meeting of the fifth session of the Board Notice in respect of the convention of 2007 General Meeting	C012 of China Securities Journal, A8 of Hong Kong Commercial Daily http://www.cninfo.com.cn
2008-6-11	Announcement in respect of the offering price for the IPO of foreign shares listed overseas (H share)	D005 of China Securities Journal, B5 of Hong Kong Commercial Daily http://www.cninfo.com.cn http://www.hkex.com.hk
2008-6-17	Announcement in respect of the listing and quotation for the foreign shares listed overseas (H shares) of IPO	D005 of China Securities Journal, B5 of Hong Kong Commercial Daily http://www.cninfo.com.cn http://www.hkex.com.hk

X. Material Matters

XI. Index of information disclosure in 2008 (continued)

Announcement date	Related matters	Media for publication
2008-7-1	Announcement in respect of the resolutions passed at the 2007 shareholders' meeting	D013 of China Securities Journal, B10 of Hong Kong Commercial Daily http://www.cninfo.com.cn http://www.hkex.com.hk
2008-7-1	Legal opinions as witnessed by lawyers on the announcement in respect of the resolutions passed at the 2007 shareholders' meeting	http://www.cninfo.com.cn http://www.hkex.com.hk
2008-7-3	Announcement in respect distribution of bonus and dividends in 2007	D004 of China Securities Journal, B6 of Hong Kong Commercial Daily http://www.cninfo.com.cn http://www.hkex.com.hk
2008-7-11	The articles of association of the Company (June 2008)	http://www.cninfo.com.cn http://www.hkex.com.hk
2008-7-17	Announcement in respect of action in price stabilization and end of period for the price stabilization	D012 of China Securities Journal, B4 of Hong Kong Commercial Daily http://www.cninfo.com.cn http://www.hkex.com.hk
2008-7-19	The special system to take precautions against controlling shareholders and related parties from embezzling the Company's fund	http://www.cninfo.com.cn http://www.hkex.com.hk
2008-7-19	Announcement in respect of the resolutions passed at the second extraordinary meeting of the fifth session of the Board	C086 of China Securities Journal, A6 of Hong Kong Commercial Daily http://www.cninfo.com.cn http://www.hkex.com.hk
2008-7-19	Explanation of governance and rectification	http://www.cninfo.com.cn http://www.hkex.com.hk

X. Material Matters

XI. Index of information disclosure in 2008 (continued)

Announcement date	Related matters	Media for publication
2008-8-04	Announcement in respect of revision of expected results	D004 of China Securities Journal, A5 of Hong Kong Commercial Daily
	Announcement in respect of the resolutions passed at the third extraordinary meeting of the fifth session of the Board	http://www.cninfo.com.cn http://www.hkex.com.hk
2008-8-19	Announcement in respect of the Board meeting date	http://www.cninfo.com.cn http://www.hkex.com.hk
2008-8-21	Announcement in respect of procurement contracts entered into for main apparatus used in the Zhanjiang pulp project	A16 of China Securities Journal http://www.cninfo.com.cn http://www.hkex.com.hk
2008-8-26	Reminder announcement in respect of issuing the short-term financing certificates	C04 of China Securities Journal, A5 of Hong Kong Commercial Daily http://www.cninfo.com.cn http://www.hkex.com.hk
2008-8-29	2008 interim report 2008 interim report (English version) 2008 interim financial report	http://www.cninfo.com.cn http://www.hkex.com.hk
2008-8-29	Summary of 2008 interim report Announcement in respect of the resolutions passed at the tenth meeting of the fifth session of the Board Announcement in respect of estimated increase in the performance results	D060 of China Securities Journal, A7-A8 of Hong Kong Commercial Daily http://www.cninfo.com.cn http://www.hkex.com.hk
2008-10-17	H share announcement	http://www.cninfo.com.cn http://www.hkex.com.hk

X. Material Matters

XI. Index of information disclosure in 2008 (continued)

Announcement date	Related matters	Media for publication
2008-10-31	2008 third quarter report (Chinese and English version) Announcement in respect of the resolutions passed at the eleventh meeting of the fifth session of the Board	D025 of China Securities Journal, A5 of Hong Kong Commercial Daily http://www.cninfo.com.cn http://www.hkex.com.hk
2008-11-06	H share announcement	http://www.cninfo.com.cn http://www.hkex.com.hk
2008-12-20	H share announcement	http://www.cninfo.com.cn http://www.hkex.com.hk

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

Deloitte.

德勤

De Shi Bao (Shen) Zi (09) No. P0262

TO THE SHAREHOLDERS OF SHANDONG CHENMING PAPER HOLDINGS LIMITED

We have audited the accompanying financial statements of Shandong Chenming Paper Holdings Limited (collectively referred to as the "Group"), which comprise the company and consolidated balance sheets as at 31 December 2008, the company and consolidated income statements, the company and consolidated statements of changes in equity and the company and consolidated cash flow statements for 2008 and notes to the financial statements.

1. MANAGEMENT'S RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The Chenming Group's management is responsible for preparing financial statements in accordance with Accounting Standards for Business Enterprises. This responsibility includes (1) designing, implementing and maintaining internal controls relevant to the preparation of the financial statements that are free from material misstatement whether due to fraud or error; (2) selecting and applying appropriate accounting policies; and (3) making accounting estimates that are reasonable in the circumstances.

2. AUDITORS' RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the Chinese Auditing Standards issued by the Chinese Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain a reasonable assurance as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider the internal controls relevant to the entity's preparation of financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of the accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

3. OPINION

In our opinion, the Chenming Group's financial statements have been prepared in accordance with Accounting Standards for Business Enterprises and present fairly, in all material aspects, the company and consolidated financial position of Chenming Group as at 31 December 2008 and the results of their operations and their cash flows for 2008.

Deloitte Touche Tohmatsu CPA Ltd.,
Shanghai, The People's Republic of China
童傳江
張扣娣
Chinese Certified Public Accountant

8 April 2009

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

Balance Sheets

As at 31 December 2008

ASSETS	Notes VII	Consolidated		The Company	
		Closing balance	Opening balance	Closing balance	Opening balance
		RMB	RMB	RMB	RMB
CURRENT ASSETS					
Bank balances and cash	1	2,853,418,128.07	740,621,843.91	2,142,439,739.51	348,948,724.68
Derivative financial instruments	20	—	5,955,480.00	—	—
Bills receivable	2	974,009,788.24	1,676,684,054.95	465,681,067.32	998,809,409.00
Accounts receivable	3	1,752,409,349.17	1,660,020,696.84	1,937,280,312.86	1,466,109,588.60
Advance to suppliers	4	462,526,338.87	574,014,801.43	438,759,362.48	279,890,382.88
Dividends receivable		—	—	164,874,997.10	42,933,862.14
Other receivables	5	135,889,612.93	196,162,672.11	936,468,514.72	776,521,148.45
Inventories	6	3,397,792,930.38	1,744,492,612.36	1,682,657,074.51	721,354,749.54
Entrusted loans due within one year	7	—	—	982,000,000.00	1,864,000,000.00
Other current assets	8	151,993,045.95	—	52,747,204.98	—
Total current assets		9,728,039,193.61	6,597,952,161.60	8,802,908,273.48	6,498,567,865.29
NON-CURRENT ASSETS					
Entrusted loans	7	—	—	965,000,000.00	625,000,000.00
Long-term investments	9	92,673,769.14	96,289,936.43	4,081,859,577.02	2,194,652,949.31
Investment properties	10	28,164,724.15	29,902,980.19	28,164,724.15	29,902,980.19
Fixed assets	11	14,213,441,758.08	13,243,156,039.93	6,258,618,550.53	6,555,767,873.32
Construction in progress	12	431,379,272.50	904,753,634.02	59,788,891.26	275,351,308.78
Project materials		42,079,864.21	44,433,213.61	1,981,408.48	6,850,752.92
Intangible assets	13	1,277,076,588.53	822,301,826.32	364,509,396.99	377,022,979.83
Goodwill	14	20,283,787.17	20,283,787.17	—	—
Long-term deferred expenditure	15	37,227,730.36	56,513,234.75	—	—
Deferred income tax assets	16	127,916,366.12	103,361,571.98	78,605,721.73	72,516,429.65
Consumable biological assets	17	301,212,691.14	92,159,871.29	—	—
Total non-current assets		16,571,456,551.40	15,413,156,095.69	11,838,528,270.16	10,137,065,274.00
TOTAL ASSETS		26,299,495,745.01	22,011,108,257.29	20,641,436,543.64	16,635,633,139.29

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

LIABILITIES AND OWNERS' EQUITY	Notes VII	Consolidated		The Company	
		Closing balance RMB	Opening balance RMB	Closing balance RMB	Opening balance RMB
CURRENT LIABILITIES					
Short-term loans	19	1,516,945,042.67	3,594,000,057.28	1,144,068,305.68	3,350,420,391.17
Financial liability					
held for trading	20	198,900.00	—	—	—
Notes payable	21	367,627,562.14	130,056,316.74	210,151,045.59	121,487,222.14
Accounts payable	22	2,642,308,185.90	1,656,706,980.62	1,716,031,795.17	1,332,552,331.70
Advances from customers	23	101,693,578.57	170,286,629.21	66,019,457.87	92,126,887.49
Employee benefits payable	24	190,209,067.13	234,880,219.06	98,888,359.60	119,224,432.42
Taxes payable	25	49,965,982.34	102,444,450.86	16,156,180.51	100,151,250.80
Dividends payable	26	36,089.31	36,075.17	36,089.31	36,075.17
Other payables	27	346,226,242.06	305,050,016.38	283,099,241.86	278,838,344.66
Non-current liabilities					
due within one year	28	1,038,125,240.62	667,746,417.91	883,602,600.00	586,144,500.00
Short-term debentures	29	1,941,874,444.43	506,212,916.67	1,941,874,444.43	—
Total current liabilities		8,195,210,335.17	7,367,420,079.90	6,359,927,520.02	5,980,981,435.55
NON-CURRENT LIABILITIES					
Long-term loans	30	4,019,250,823.86	4,056,194,662.35	3,064,076,035.94	2,899,617,835.94
Deferred income	31	56,828,375.23	830,000.00	5,537,541.95	—
Deferred income tax liabilities	32	6,431,545.79	6,103,850.08	—	—
Total non-current liabilities		4,082,510,744.88	4,063,128,512.43	3,069,613,577.89	2,899,617,835.94
TOTAL LIABILITIES		12,277,721,080.05	11,430,548,592.33	9,429,541,097.91	8,880,599,271.49

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

LIABILITIES AND OWNERS' EQUITY	Notes VII	Consolidated		The Company	
		Closing balance RMB	Opening balance RMB	Closing balance RMB	Opening balance RMB
OWNERS' EQUITY					
Share capital	33	2,062,045,941.00	1,706,345,941.00	2,062,045,941.00	1,706,345,941.00
Capital surplus	34	6,093,483,801.92	3,737,991,906.21	6,184,215,988.77	3,827,378,359.74
Surplus reserve .	35	825,476,850.53	723,742,920.58	813,287,268.62	711,553,338.67
Undistributed profits	36	3,277,192,810.40	2,576,650,349.38	2,152,346,247.34	1,509,756,228.39
Translation reserve .		879,498.14	303,894.68	—	—
Equity attributable to equity holders of the Company		12,259,078,901.99	8,745,035,011.85	11,211,895,445.73	7,755,033,867.80
Minority Interests	37	1,762,695,762.97	1,835,524,653.11	—	—
Total Owners' equity		14,021,774,664.96	10,580,559,664.96	11,211,895,445.73	7,755,033,867.80
TOTAL LIABILITIES AND OWNERS' EQUITY		26,299,495,745.01	22,011,108,257.29	20,641,436,543.64	16,635,633,139.29

The notes form an integral part of the financial statements.

The financial statements as set out from pages 121 to 271 have been signed by:

Chen Hongguo
Head of Corporation

Liu Junwu
Chief Financial Officer

Wang Chunfang
Head of the finance section

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

Income statements

For the year ended 31 December 2008

	Notes VII	Consolidated		The Company	
		Accumulated for this year RMB	Accumulated for last year RMB	Accumulated for this year RMB	Accumulated for last year RMB
Operating Revenue	38	15,529,593,435.77	15,164,742,450.26	13,557,782,274.40	12,552,589,262.55
Less: Cost of main operations	39	12,556,762,340.80	12,074,481,475.02	11,949,922,698.03	10,887,601,388.35
Tax and levies on main operations	40	12,582,354.31	17,854,424.80	306,581.16	282,690.99
Selling and distribution expenses		705,595,565.95	783,289,341.85	340,787,921.65	397,932,244.92
General and administrative expenses		561,194,537.62	530,820,858.29	207,830,251.32	210,224,821.41
Finance expenses	41	287,136,504.05	392,163,050.56	197,961,693.30	303,883,491.96
Loss on impairment of assets	42	93,125,334.87	102,198,629.26	11,932,470.59	4,908,666.11
Add: Gain on change in fair value	43	2,656,651.60	30,370,880.31	—	—
Investment income	44	(23,081,752.26)	(9,461,550.75)	302,967,881.91	222,885,767.76
Including: Investment income from associates and joint ventures		(23,167,629.22)	(9,461,550.75)	(23,167,629.22)	(9,461,550.75)
Operating profit		1,292,771,697.51	1,284,844,000.04	1,152,008,540.26	970,641,726.57
Add: Non-operating income	45	274,366,224.82	232,218,083.67	142,693,393.66	47,503,266.20
Less: Non-operating expenses	46	11,798,611.64	27,725,881.15	5,983,889.34	10,417,366.26
Including: Loss on disposal of non-current assets		5,007,364.04	27,181,945.34	1,388,338.83	10,400,342.17
Total profit		1,555,339,310.69	1,489,336,202.56	1,288,718,044.58	1,007,727,626.51
Less: Income tax expenses	47	295,797,856.42	270,795,013.27	271,378,745.12	197,214,107.46
Net profit		1,259,541,454.27	1,218,541,189.29	1,017,339,299.46	810,513,519.05

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

	Notes VII	Consolidated		The Company	
		Accumulated for this year RMB	Accumulated for last year RMB	Accumulated for this year RMB	Accumulated for last year RMB
Net profit attributable to the equity holders of the Company		1,075,291,741.53	967,636,172.39	1,017,339,299.46	810,513,519.05
Minority interests		184,249,712.74	250,905,016.90	—	—
Earnings per share					
Basic	49	0.57	0.60	0.54	0.50
Diluted	49	N/A	0.59	N/A	0.50

The notes form an integral part of the financial statements.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

Cash Flow Statements

For the year ended 31 December 2008

Notes VII	Consolidated		The Company	
	Accumulated for this year RMB	Accumulated for last year RMB	Accumulated for this year RMB	Accumulated for last year RMB
Cash Flows from Operating Activities				
Cash received from sales of goods, rendering of services	16,583,978,475.35	15,346,933,191.88	12,816,080,559.54	14,486,782,584.79
Refund of taxes and levies	33,851,926.78	75,372,967.36	—	—
Cash received relating to other operating activities 53	237,097,779.40	118,085,044.97	163,421,906.83	539,291,856.66
Subtotal of cash inflows from operating activities	16,854,928,181.53	15,540,391,204.21	12,979,502,466.37	15,026,074,441.45
Cash paid for goods and services	12,123,175,577.65	11,811,905,431.94	10,851,617,699.47	12,261,934,180.86
Cash paid to and on behalf of employees	696,574,804.91	487,126,693.03	272,735,589.72	180,749,301.33
Payments of taxes and levies	1,312,935,590.68	1,039,124,100.69	782,472,375.13	561,696,003.74
Cash paid relating to other operating activities 54	788,101,405.25	877,971,853.54	511,205,605.42	470,013,272.89
Subtotal of cash outflows from operating activities	14,920,787,378.49	14,216,128,079.20	12,418,031,269.74	13,474,392,758.82
Net cash flows from investing activities	1,934,140,803.04	1,324,263,125.01	561,471,196.63	1,551,681,682.63
Cash Flows from Investing Activities				
Cash received from investments	—	—	2,332,000,000.00	620,000,000.00
Cash received from returns on investments	85,876.96	—	187,328,257.66	200,606,101.29
Cash received from disposal of fixed assets, intangible assets and other long-term assets	603,818.56	15,746,133.62	1,193,105.59	962,227.06
Cash received relating to other investing activities 55	57,823,238.62	—	5,643,238.62	—
Subtotal of cash inflows from investing activities	58,512,934.14	15,746,133.62	2,526,164,601.87	821,568,328.35

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

Notes VII	Consolidated		The Company	
	Accumulated for this year RMB	Accumulated for last year RMB	Accumulated for this year RMB	Accumulated for last year RMB
Cash paid to acquire fixed assets, intangible assets and other long-term assets	1,542,798,830.74	884,022,116.21	108,944,870.20	677,874,762.20
Cash paid on investments	19,564,645.55	108,725,512.44	3,618,100,000.00	1,338,426,063.80
Subtotal of cash outflows from investing activities	1,562,363,476.29	992,747,628.65	3,727,044,870.20	2,016,300,826.00
Net cash flows from investing activities	(1,503,850,542.15)	(977,001,495.03)	(1,200,880,268.33)	(1,194,732,497.65)
Cash Flows from Financing Activities				
Cash received from investment	2,711,191,895.71	37,554,000.00	2,711,191,895.71	—
Cash received from borrowings	6,002,051,512.02	8,076,267,182.50	5,332,258,412.74	6,241,624,261.50
Cash received from issuance of short-term debentures	1,892,400,000.00	496,965,000.00	1,892,400,000.00	—
Cash received relating to other financing activities 56	—	—	50,557,068.28	—
Subtotal of cash inflows from financing activities	10,605,643,407.73	8,610,786,182.50	9,986,407,376.73	6,241,624,261.50
Cash repayments of amounts borrowed	7,546,630,384.92	6,137,101,438.52	6,890,979,853.42	4,053,206,228.24
Cash payments for interest expenses, and distribution of dividends or profits	858,902,641.36	897,534,770.36	596,770,954.15	620,902,705.10
Including: Dividend and profit paid by subsidiaries to minority shareholders	142,483,663.78	139,553,201.91	—	—
Cash repayments for conversion of short-term debentures	500,000,000.00	2,000,000,000.00	—	2,000,000,000.00
Cash payments relating to other financing activities 57	39,043,580.93	89,146,310.05	—	117,291,492.65

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

	Notes VII	Consolidated		The Company	
		Accumulated for this year RMB	Accumulated for last year RMB	Accumulated for this year RMB	Accumulated for last year RMB
Subtotal of cash outflows from financing activities		8,944,576,607.21	9,123,782,518.93	7,487,750,807.57	6,791,400,425.99
Net cash flows from financing activities		1,661,066,800.52	(512,996,336.43)	2,498,656,569.16	(549,776,164.49)
Effect of foreign exchange rate changes on cash		(17,604,358.18)	(4,759,232.11)	(15,199,414.35)	(3,154,716.00)
Net increase in cash and cash equivalents	51	2,073,752,703.23	(170,493,938.56)	1,844,048,083.11	(195,981,695.51)
Add: Balance of cash and cash equivalents at the beginning of the year	51	613,826,456.62	784,320,395.18	235,957,551.29	431,939,246.80
Balance of cash and cash equivalents at the end of the year	51	2,687,579,159.85	613,826,456.62	2,080,005,634.40	235,957,551.29

The notes form an integral part of the financial statements.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

Statement of Change in Shareholders' Equity

For the year ended 31 December 2008

	Consolidated												
	Share capital	Capital surplus	Surplus reserve	Undistributed profit	Exchange differences	Attributable to the equity holders of the parent company	Minority interests	Total equity	Share capital	Capital surplus	Surplus reserve	Undistributed profit	Total equity
	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB
I. Balance at prior year end	1,706,945,941.00	3,737,991,906.21	723,742,920.63	2,576,650,446.38	303,894.63	8,745,055,011.85	1,685,524,653.11	10,590,559,694.96	1,706,945,941.00	3,827,376,389.74	711,553,338.67	1,509,736,228.39	7,755,633,867.80
II. Changes in the current year (+/-)	355,700,000.00	2,355,491,895.71	101,733,929.95	700,542,461.02	575,603.46	3,514,043,890.14	(72,828,890.14)	3,441,215,000.00	355,700,000.00	2,355,837,629.03	101,733,929.95	642,530,018.95	3,456,861,577.93
(I) Net profit	-	-	-	1,075,291,741.53	-	1,075,291,741.53	184,249,712.74	1,259,541,454.27	-	-	-	1,017,339,299.46	1,017,339,299.46
(II) Profit and loss directly dealt with in shareholders' equity	-	-	-	-	575,603.46	575,603.46	-	575,603.46	-	1,345,733.32	-	-	1,345,733.32
(I) Others	-	-	-	-	575,603.46	575,603.46	-	575,603.46	-	1,345,733.32	-	-	1,345,733.32
Sub-total of (I) and (II)	-	-	-	1,075,291,741.53	575,603.46	1,075,867,344.99	184,249,712.74	1,260,117,057.73	-	1,345,733.32	-	1,017,339,299.46	1,018,685,027.78
(III) Shareholders' contributions and decrease in capital	355,700,000.00	2,355,491,895.71	-	-	-	2,711,191,895.71	-	2,711,191,895.71	355,700,000.00	2,355,491,895.71	-	-	2,711,191,895.71
1. Shareholders' contributions in capital	355,700,000.00	-	-	-	-	355,700,000.00	-	355,700,000.00	355,700,000.00	-	-	-	355,700,000.00
2. Capital premium	-	2,355,491,895.71	-	-	-	2,355,491,895.71	-	2,355,491,895.71	-	2,355,491,895.71	-	-	2,355,491,895.71
(IV) Profit distribution	-	-	101,733,929.95	(374,749,200.51)	-	(273,015,330.56)	(142,483,663.78)	(415,499,014.34)	-	-	101,733,929.95	(374,749,200.51)	(273,015,330.56)
1. Transfer to surplus reserves	-	-	101,733,929.95	(101,733,929.95)	-	-	-	-	-	-	101,733,929.95	(101,733,929.95)	-
2. Distribution to shareholders	-	-	-	(273,015,330.56)	-	(273,015,330.56)	(142,483,663.78)	(415,499,014.34)	-	-	-	(273,015,330.56)	(273,015,330.56)
(V) Acquisition of minority interest	-	-	-	-	-	-	(114,594,938.10)	(114,594,938.10)	-	-	-	-	-
III. Balance at the end of the current year	2,062,645,941.00	6,093,483,801.92	825,476,850.58	3,277,192,907.40	879,498.14	12,259,075,901.99	1,782,895,762.97	14,021,771,654.96	2,062,645,941.00	6,184,215,988.77	812,287,268.62	2,152,246,547.34	11,211,885,445.73

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

Statement of Change in Shareholders' Equity (continued)

For the year ended 31 December 2007

	Consolidated						The Company						
	Share capital	Capital surplus	Surplus reserve	Unsubscribed profit	Exchange differences	Attributable to the equity holders of the parent company	Minority interests	Total equity	Share capital	Capital surplus	Surplus reserve	Unsubscribed profit	Total equity
	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB
I. Balance at prior year end	1,365,670,155.00	1,917,855,010.34	677,829,746.88	2,040,792,497.87	(2,440.00)	6,010,124,970.09	1,739,491,572.97	7,749,616,540.06	1,365,670,155.00	2,065,990,970.86	665,640,764.97	1,249,622,724.97	5,946,923,315.80
1. Changes in accounting policies	-	330,821,007.98	(85,138,172.20)	(163,965,456.06)	-	141,517,373.72	(1,881,791.33)	139,655,582.33	-	280,161,081.14	(561,381,778.20)	(64,566,530.81)	(639,523,647.87)
II. Balance at the beginning of the current year	1,365,670,155.00	2,248,456,018.32	642,691,574.68	1,876,827,041.81	(2,440.00)	6,151,642,343.81	1,737,609,781.58	7,889,252,125.39	1,365,670,155.00	2,326,171,951.80	630,571,986.77	985,055,574.16	5,307,399,667.73
III. Changes in the current year (+/-)	340,675,766.00	1,489,535,887.89	81,051,351.90	681,823,307.57	306,334.68	2,350,392,668.04	97,914,871.53	2,691,307,539.57	340,675,766.00	1,501,208,407.94	81,051,351.90	524,700,654.23	2,447,684,200.07
(I) Net profit	-	-	-	967,636,172.39	-	967,636,172.39	250,905,016.90	1,218,541,189.29	-	-	-	810,513,519.05	810,513,519.05
(II) Profit and loss directly dealt with in shareholders' equity	-	1,000,000.00	-	-	306,334.68	1,306,334.68	-	1,306,334.68	-	12,670,520.05	-	-	12,670,520.05
I. Others	-	1,000,000.00	-	-	306,334.68	1,306,334.68	-	1,306,334.68	-	12,670,520.05	-	-	12,670,520.05
Sub-total of (I) and (II)	-	1,000,000.00	-	967,636,172.39	306,334.68	969,945,507.07	250,905,016.90	1,219,847,523.97	-	12,670,520.05	-	810,513,519.05	823,184,039.10
(III) Shareholders' contributions and decrease in capital	340,675,766.00	1,489,535,887.89	-	-	-	1,829,211,673.89	37,554,000.00	1,866,765,673.89	340,675,766.00	1,489,535,887.89	-	-	1,829,211,673.89
1. Shareholders' contributions in capital	-	-	-	-	-	-	37,554,000.00	37,554,000.00	-	-	-	-	-
2. Increase in capital	-	-	-	-	-	-	-	-	-	-	-	-	-
from conversion of convertible bonds	340,675,766.00	1,489,535,887.89	-	-	-	1,829,211,673.89	-	1,829,211,673.89	340,675,766.00	1,489,535,887.89	-	-	1,829,211,673.89
(IV) Profit distribution	-	-	81,051,351.90	(265,812,264.82)	-	(204,761,512.92)	(139,553,201.91)	(344,314,714.83)	-	-	81,051,351.90	(265,812,264.82)	(204,761,512.92)
1. Transfer to surplus reserves	-	-	81,051,351.90	(81,051,351.90)	-	-	-	-	-	-	81,051,351.90	(81,051,351.90)	-
2. Distribution to shareholders	-	-	-	(204,761,512.92)	-	(204,761,512.92)	(139,553,201.91)	(344,314,714.83)	-	-	-	(204,761,512.92)	(204,761,512.92)
(V) Acquisition of minority interest	-	-	-	-	-	-	(50,990,943.46)	(50,990,943.46)	-	-	-	-	-
IV. Balance at the end of the current year	1,706,345,941.00	3,737,991,906.21	723,742,926.58	2,576,650,349.39	309,834.68	8,745,035,011.85	1,835,524,653.11	10,580,559,664.46	1,706,345,941.00	3,827,378,359.74	711,553,338.67	1,509,756,228.39	7,755,033,667.80

The notes form an integral part of the financial statements.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

Notes to the financial statements

For the year ended 31 December 2008

I. General Information

Shandong Chenming Paper Holdings Limited (hereinafter referred as the "Company"), whose predecessor was Shandong Shouguang Paper Mill Corporation, was reorganized to become a joint stock limited company by way of private placement in May 1993. In December 1996, with the approval issued by the Shandong Provincial Government (Lu Gu Zi [1996] Document No. 270) and by the Securities Committee of the State Council (Zheng Wei [1996] Document No.59), the Company was reorganized to become a joint stock limited company by way of public subscription.

In May 1997, with the approval issued by the Securities Committee of the State Council (Zheng Wei Fa [1997] Document No. 26), the Company issued 115 million B Shares in connection with its international offering. B-shares from this issuance were listed on the Shenzhen Stock Exchange since 26 May 1997.

In September 2000, with the approval issued by China Securities Regulatory Committee (hereinafter referred as the "CSRC") (Zheng Jian Gong Si Zi [2000] Document No. 151), the Company issued 70 million A Shares. A-shares from this issuance were listed on the Shenzhen Stock Exchange on 20 November 2000.

In June 2008, with the approval issued by the Stock Exchange of Hong Kong Limited (hereinafter referred as the "Stock Exchange"), the Company issued 355,700,000 H shares. Meanwhile, the relevant state shareholders of the Company performed the reduction of state-owned shares, by way of transferring to the Social Security Fund Council (the "NSSF Council") such number of shares held by it, representing 35,570,000 shares, which were to be converted into overseas listed foreign shares (H shares). This issuance of 391,270,000 H-shares were listed on the Hong Kong Stock Exchange on 18 June 2008.

As at 31 December 2008, the Company has a total of 2,062,045,941 shares (refer to note VII.33).

The business scope of the Company and its subsidiaries (hereinafter referred as the "Group") covers: processing and sale of paper products (including machine made paper and paper board), paper making raw materials and machinery; generation and sale of electric power and thermal power; forestry, saplings growing, processing and sale of timber; manufacturing, processing and sale of wood products; and manufacturing and sale of laminated boards and fortified wooden floorboards.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

2 Statement of Compliance with the Accounting Standards for Business Enterprises ("ASBEs")

The financial statements have been prepared in conformity with the ASBEs, which truly and fully reflect the financial positions of the Company and the Group as at 31 December 2008, and the operating results and cash flows of the Company and the Group for the year ended 31 December 2008.

3. Significant Accounting Policies and Estimates

The following principal accounting policies and accounting estimates are determined based on the ASBEs.

Accounting Year

The fiscal year of the Group is from 1 January to 31 December of each calendar year.

Reporting currency

The currency of the primary economic environment in which the Company and its domestic subsidiaries operate is Renminbi ("RMB"). The Company and its domestic subsidiaries regard RMB as their reporting currency. Overseas subsidiaries of the Company recognize U.S. dollar as their reporting currency according to the primary economic environment in which they subsidiaries operate. The Group prepares its financial statement based on RMB.

Basis of preparation and principle of measurement

The Group's financial statements have been prepared on an accrual basis. Except for consumable biological assets and certain financial instruments which are measured at fair value, the financial statements are prepared under the historical cost convention. A provision for impairment of assets was made according to the accounting policies.

Cash equivalents

Cash equivalents held by the Group represent short-term and highly liquid investments that are readily convertible to known amounts of cash and which are subject to insignificant risk of value change.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

3. Significant Accounting Policies and Estimates (continued)

Foreign currency translation

On initial recognition, foreign currency transactions are translated into the reporting currency using the spot exchange rate prevailing at the date of transaction.

At the balance sheet date, monetary items denominated in foreign currencies are translated to RMB using the spot exchange rate at that date. Exchange differences arising from the difference between the spot exchange rate on the balance sheet date on which foreign currency monetary items are translated at the spot exchange rate and the spot exchange rate at the time of initial recognition or on the last balance sheet date shall be recorded into the profit or loss for the current period.

Non-monetary items denominated in foreign currency measured at historical cost shall continue to be translated into the reporting currency at the spot exchange rate at the date of transaction.

Exchange differences arising from change in exchange rate where the preparation of consolidated financial statements relates to overseas operation and foreign currency monetary items materially constitute net investment in overseas operation shall be recorded into "translation reserve" in the shareholders' equity: disposal of overseas operation shall be included into profits and losses on disposal in the current period.

Method of determination of the fair value for financial instruments

The fair value refers to the amount, at which both willing parties to a fair transaction who are familiar with the condition exchange their assets or clear off their debts under fair conditions. Financial instruments exist in an active market. Fair value is determined based on the quoted price in such market. An active market refers to where pricing is easily and regularly obtained from exchanges, brokers, industrial organizations and price-fixing service organizations, representing the actual price of a market transaction that takes place in a fair deal. Financial instruments not only exist in an active market, but fair value is also determined using valuation techniques. Valuation technologies include reference to be familiar with situation and prices reached in recent market transactions entered into by both willing parties, reference to present fair values of similar other financial instruments, cash flow discounting method and option pricing models.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

3. Significant Accounting Policies and Estimates (continued)

Recognition and measurement of the financial assets

By way of buying and selling the financial assets in a regular way, recognition and derecognition are carried out according to the accounts on the transaction day. Financial assets are divided into financial assets at fair value through profit or loss, held-to-maturity investments, loans and the account receivables and available-for-sale financial assets when they are initially recognized. Financial assets and financial liabilities are initially recognized at fair value. For financial assets and financial liabilities classified as at fair value through profit or loss, relevant transaction costs are directly recognized in profit or loss for the current period. For financial assets classified as other categories, relevant transaction costs are included in the amount initially recognized.

Financial assets are classified at initial recognition with reference to the nature and the purpose of holding. The Group's financial assets are mainly trust loans and accounts receivable.

Loans and accounts receivable

Trust loans and accounts receivable adopt the actual interest rate method to carry out the ongoing measure based on amortized costs. On derecognition, profit or loss arising from impairment or amortization is carried as at profit or loss

Impairment of financial assets

In addition to financial assets at fair value through profit or loss, the Group reviews the book value of other financial assets in each balance sheet date and provide for impairment where there is objective evidence that financial assets are impaired.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

3. Significant Accounting Policies and Estimates (continued)

Impairment of financial assets (continued)

Objective evidence of impairment on financial asset includes those observable matters listed as follows: (1) issuers or debtors encounter severe financial difficulties; (2) debtors violate terms of contract, such as a breach of rules or delay during settlement of interests or principal; (3) the Group gives way to those under financial difficulty accounting on economic or legal reasons; (4) debtors may go into liquidation or conduct other financial reorganization; (5) transaction of the financial assets ceases in the active market as the issuer encounters great financial difficulties; (6) any reduction in cash flow of certain assets among a group of financial assets cannot be identified, while it is discovered that the estimated future cash flow of the financial assets has been reduced and can be measured since initial recognition after an overall evaluation based on disclosed information, including that the repayment capability of the debtor of the group of financial assets gradually deteriorates, economy difficulties of the country or region where the debtor is staying appear a situation where this group of financial assets cannot be paid; (7) significant and adverse changes have taken place in the technological, market, economic or legal environments in which the debtor operates, making investors of equity instruments difficult to recover the investment cost; (8) substantial or non-temporary reduction of the fair value of investment on equity instruments; (9) other objective evidence showing signs of impairment on financial assets.

For a financial asset that is individually significant, the Group assesses the asset individually for impairment. For a financial asset that is not individually significant, the Group assess the asset individually for impairment or include the asset in a group of financial assets with similar credit risk characteristics and collectively assess them for impairment. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether the financial asset is individually significant or not, the financial asset is included in a group of financial assets with similar credit risk characteristics and collectively assessed for impairment. Financial assets for which an impairment loss is individually recognized are not included in the collective assessment for impairment.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

3. Significant Accounting Policies and Estimates (continued)

Impairment of financial assets (continued)

Impairment of loans and accounts receivable

The carrying amount of financial assets measured as costs or amortized costs are subsequently reduced to the present value discounted from its projected future cash flow. The reduced amount is recognized as impairment loss and recorded as profit or loss for the period. Upon recognition of the impairment loss from financial assets, if there is objective evidence showing recovery in value of the amount of such financial assets so impaired and which is related to any event occurring after such recognition, the impairment loss originally recognized shall be reversed to the extent that the carrying value of the financial assets upon reversal will not exceed the amortized cost as at the reversal date assuming there is no provision for impairment.

Derecognition of Financial Asset

Financial asset that satisfied any of the following criteria shall be derecognized: (1) the contract right to recover the cash flows of the financial asset has terminated; (2) the financial asset, along with substantially all the risk and return arising from the ownership of the financial asset, has been transferred to the transferee; (3) the financial asset has been transferred to the transferee, and the transferor has given up the control on such financial asset, though it does not assign maintain substantially all the risk and return arising from the ownership of the financial asset.

Inventories

Inventories of the Group mainly include raw materials, products and finished products. Inventories include purchasing cost, processing cost and other expenses that help deliver the inventories to the current location and situation.

Inventories are stated at standard costs upon delivery. The amount is adjusted for price variance to arrive at actual cost at the end of month.

The inventory taking system shall use permanent inventory system.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

3. Significant Accounting Policies and Estimates (continued)

Provision for Inventory Impairment

At the balance sheet date, inventories were calculated at the lower of cost and net realizable value. Provision for inventory impairment is made when the net realizable value is lower than the cost. Provisions for impairment of inventory shall be made according to the amount by which the cost of a single item exceeds its net realizable value.

After making the provision for inventory impairment, in case the factors causing inventory impairment no longer exists, and the net realizable value of an inventory is higher than its book-value, the original provision for inventory impairment shall be transferred back and incorporated into the profit or loss for the current period.

Net realizable value refers to the amount of the estimated price of inventories less the estimated cost incurred upon completion, estimated sales expenses and other amounts after tax and levies in daily operation. The realizable value of inventories shall be determined on the basis of definite evidence, purpose of holding the inventories and effect of after-balance-sheet-date events.

Consumable biological assets

Consumable biological assets refer to biological assets held for sale or to be harvested as agricultural produce in the future, which include growing commercial forests. Consumable biological assets are stated at cost at initial recognition. The cost of self-planting, self-cultivating consumable biological assets is the necessary expenses directly attributable to such assets prior to canopy closure, including borrowing costs eligible for capitalization. Subsequent expenses incurred after canopy closure shall be included in profit or loss for the current period.

The cost of consumable biological assets shall, at the time of harvest or disposal, be carried forward at carrying value using the rotation age method.

All the consumable biological assets of the Group are subsequently measured at fair value as they are quoted in an active market where the Group can obtain a quoted market price and other information of the assets, and thus their fair values can be reliably estimated. Changes in fair values shall be recognized as profit or loss in the current period.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

3. Significant Accounting Policies and Estimates (continued)

Investment Property

Investment property is held to earn rentals or for capital appreciation or both, including buildings leased out.

Investment property is initially measured at cost. Subsequent expenditures related to an investment property shall be included in cost of investment property only when the economic benefits associated with the asset will likely flow to the Group and its cost can be measured reliably. All other expenditures on investment property shall be included in profit or loss for the current period when incurred.

The Group adopts cost method for subsequent measurement of investment property, which is depreciated or amortized using the same policy as that for buildings and land use rights.

In the event that an owner-occupied property is converted to an investment property (or vice versa), upon the conversion, the property shall be stated at the carrying amount prior to the conversion.

When an investment property is sold, transferred, retired or damaged, the amount of proceeds on disposal of the property net of the carrying amount and related tax and surcharges is recognized in profit or loss for the current period.

Long-term equity investments

For a long-term equity investment acquired through a business combination involving enterprises under common control, the initial investment cost of the long-term equity investment shall be the absorbing party's share of the carrying amount of the owner's equity of the party being absorbed at the date of combination. For a long-term equity investment acquired through business combination not involving enterprises under common control, the initial investment cost of the long-term equity investment acquired shall be the cost of acquisition. The long-term equity investment acquired through means other than a business combination shall be initially measured at its cost.

Cost method is used to account for a long-term equity investment where the investor does not have joint control or significant influence over the investee, and the investment is not quoted in an active market and its fair value cannot be reliably measured. Long-term equity investment with joint control or significant influence on the investee is accounted for using equity method. Long-term equity investment without control or joint control or significant influence with a fair value which can be reliably measured is accounted for as available-for-sale financial assets.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

3. Significant Accounting Policies and Estimates (continued)

Long-term equity investments (continued)

In addition, long-term equity investment with control on the investee is accounted for using equity method and record in the Company's financial statement.

The term "control" means that the Group has the power to decide an enterprise's financial and operating policy, pursuant to which, the Group can get the power to obtain benefits from its operating activities. Joint control is the contractually agreed sharing of control over an economic activity, which only exists when relevant and important financial affairs and management decisions related to such economic activity require sharing of control by investors who unanimously agree upon. Significant influence is the power to participate in the financial and operating policy decisions of an enterprise, but to fail to control or joint control the formulation of such policies together with other parties.

Long-term equity investment accounted for using the cost method

Under the cost method, a long-term equity investment is measured at its initial investment cost. Investment income recognized in the current period shall be limited to the amount distributed to it out of accumulated net profits of the investee arising after the investment was made. Any cash dividends or distributions declared by the investee received in excess of this amount shall be treated as return of initial investment cost to reduce the carrying amount of the investment.

Long-term equity investment accounted for using the equity method

Under the equity method, where the initial investment cost of a long-term equity investment exceeds the investor's interest in the fair value of the investee's identifiable net assets at the acquisition date, no adjustment shall be made to the initial investment cost. Where the initial investment cost is less than the investor's interest in the fair value of the investee's identifiable net assets at the acquisition date, the difference shall be charged to profit or loss for the current period, and the cost of the long-term equity investment shall be adjusted accordingly.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

3. Significant Accounting Policies and Estimates (continued)

Long-term equity investments (continued)

Long-term equity investment accounted for using the equity method (continued)

Under the equity method, investment gain or loss represents the Group's share of the net profits or losses made by the investee for the current period. The Group shall recognize its share of the investee's net profits or losses based on the fair values of the investee's individual separately identifiable assets at the time of acquisition, after making appropriate adjustments thereto in conformity with the accounting policies and accounting periods of the Group. The unrealized gain or loss from internal transactions entered into between the Group and its associated enterprises and joint ventures is set off according to the shareholding attributable to the Group and accounted for as investment income and loss based such basis. However, the unrealized gain or loss from internal transactions entered into between the Group and its investee is not set up if belonging to impairment loss from assets transferred according to regulations such as "Accounting Standards for Business Enterprises No. 8 "Assets impairment". For any changes in shareholders' equity other than net profits or losses in the investee, the Group shall adjust the carrying amount of the long-term equity investment and include the corresponding adjustment in shareholders' equity.

The Group's share of net losses of the investee shall be recognized to the extent that the carrying amount of the long-term equity investment together with any long-term interests that in substance form part of the investor's net investment in the investee are reduced to zero. If the Group has to assume additional obligations, the estimated obligation assumed shall be provided for and charged to the profit or loss as investment loss for the period. Where the investee is making profits in subsequent periods, the Group shall resume recognizing its share of profits after setting off against the share of unrecognized losses.

Disposal of long-term equity investments

On disposal of a long-term investment, the difference between the carrying amount of the investment and the actual consideration paid is recognized in current profit or loss. Where the equity method is adopted, the amount attributable to the long-term equity investment previously included shareholders' equity shall be transferred to current profit or loss on a pro-rata basis.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

3. Significant Accounting Policies and Estimates (continued)

Long-term equity investments (continued)

Acquisition of minority interests

As for minority interests of subsidiaries acquired before 7 August 2008, since acquisition of minority interests increased cost of long-term equity investment which was compared to fair value of identifiable net assets recognized on the acquisition date of subsidiaries attributable to the Group calculated according to the proportion of newly acquired shares, the difference of which recognized as goodwill in the consolidated balance sheet. Since acquisition of minority interests increased cost of long-term equity investment which was compared to fair value of identifiable net assets recognized which are measured based on the continuous measurement since the acquisition date (or combination date) of subsidiaries attributable to the Group calculated according to the proportion of newly acquired shares, the difference of which recognized as a portion of goodwill, capital premium of adjusted capital surplus, the remaining sum of the capital premium insufficient to set off impairment, adjusted retained earnings.

As for minority interests of subsidiaries acquired on and after 7 August 2008 and upon the preparation of the consolidated financial statements, since acquisition of minority interests increased cost of long-term equity investment which was compared to fair value of identifiable net assets recognized which are measured based on the continuous measurement since the acquisition date (or combination date) of subsidiaries attributable to the Group calculated according to the proportion of newly acquired shares, the difference of which recognized as adjusted capital surplus, capital surplus insufficient to set off impairment and adjusted retained earnings.

The Group had not acquired minority interests in any subsidiaries since 7 August 2008.

Fixed assets and depreciation

Fixed assets are tangible assets that are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and have a useful life of more than one accounting year.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

3. Significant Accounting Policies and Estimates (continued)

Fixed assets and depreciation (continued)

Fixed assets shall be initially measured at cost and the effect of any expected costs of abandoning the asset at the end of its use. Depreciation is provided over their estimated useful lives from the month after they have reached the working condition for their intended use using the straight-line method. The useful life, estimated residual value and annual depreciation rate of each category of fixed assets are as follows:

Category	Estimated residual value	Useful life	Annual depreciation rate
Buildings and structures	5-10%	20-40 years	2.25- 4.75%
Machinery and equipment	5-10%	8-20 years	4.50-11.88%
Vehicles	5-10%	5-8 years	11.25-19.00%
Electronic equipment and others	5-10%	5 years	18.00 -19.00%

Estimated net residual value of a fixed asset is the estimated amount that the Group would currently obtain from disposal of the asset, after deducting the estimated costs of disposal, if the asset were already of the stage and in the condition expected at the end of its useful life.

Subsequent expenditures incurred for a fixed asset shall be included in the cost of the fixed asset, only if it is probable that economic benefits associated with the asset will flow to the Company and the relevant cost can be measured reliably; meanwhile the carrying amount of the replaced part shall be derecognized. Other subsequent expenditures shall be charged to profit or loss when incurred.

The Group reviews the useful life and estimated net residual value of a fixed asset and the depreciation method applied at least at each financial year-end. A change in the useful life or estimated net residual value of a fixed asset or the depreciation method used shall be accounted for as a change in accounting estimate.

When a fixed asset is sold, transferred, retired or damaged, the Group shall recognize the amount of any proceeds on disposal of the asset net of the carrying amount and related taxes in profit or loss for the current period.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

3. Significant Accounting Policies and Estimates (continued)

Construction in progress

Construction in progress is recognized based on the actual construction cost, including all expenditures incurred for construction projects, capitalized borrowing costs for the construction in progress before it has reached the working condition for its intended use, and other related expenses during the construction period. A construction in progress is transferred to fixed assets when it has reached the working condition for its intended use.

Intangible assets

An intangible asset is an identifiable non-monetary asset without physical substance owned or controlled by the Group.

An intangible asset shall be initially measured at cost. The expenditures incurred on an intangible asset shall be recognized as cost of the intangible asset only if it is probable that economic benefits associated with the asset will flow to the Group and the cost of the asset can be measured reliably. Other expenditures on an intangible asset shall be charged to profit or loss when incurred.

Land use right acquired shall normally be recognized as an intangible asset. Self-constructed buildings (e.g. plants), related land use right and the buildings shall be separately accounted for as an intangible asset and fixed asset. For buildings and structures purchased, the purchase consideration shall be allocated among the land use right and the buildings on a reasonable basis. In case there is difficulty in making a reasonable allocation, the consideration shall be recognized in full as fixed assets.

All the intangible assets of the Group have a finite useful life. An intangible asset with a finite useful life shall be amortized using the straight-line method over its useful life when the asset is available for use. The Group shall review the useful life of intangible asset and the amortization method applied at least at each financial year-end. A change in the useful life or amortization method used shall be accounted for as a change in accounting estimate.

The estimated useful life of the Company's intangible assets is set out as follows:

Category	Useful life
Land use rights	50 years
Software	5 -10 years

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3. Significant Accounting Policies and Estimates (continued)

Long-term deferred expenses

Long-term deferred expenses are expenditures and other expenses which have incurred but that shall be amortized over the current period and subsequent periods of more than one year. Long-term deferred expenses are amortized evenly over the estimated benefit period.

Impairment of non-monetary assets

The Group assesses at each balance sheet date whether there is any indication that any long-term equity investment, investment properties, fixed assets, construction in progress, construction materials and intangible assets may be impaired. If there is any evidence indicating that an asset may be impaired, recoverable amount shall be estimated for the individual asset. If it is not possible to estimate the recoverable amount of the individual asset, the Group shall determine the recoverable amount of the asset group to which the asset belongs. If the recoverable amount of an asset is less than its carrying amount, the reduction is recognized as an impairment loss and charged to profit or loss for the current period. A provision for impairment loss of the asset is recognized accordingly.

Goodwill arising in a business combination shall be tested for impairment annually, irrespective of whether there is any indication that the asset may be impaired. For the purpose of impairment testing, goodwill shall be considered together with the related asset groups or sets of asset groups. For the purpose of impairment testing, the carrying amount of goodwill shall, from the acquisition date, be allocated on a reasonable basis to each of the related asset groups. If the recoverable amount is less than the carrying amount, the Group shall recognize an impairment loss. The amount of impairment loss shall first reduce the carrying amount of any goodwill allocated to the asset group or set of asset groups, and then reduce the carrying amount of other assets (other than goodwill) within the asset group or set of asset groups, pro rata on the basis of the carrying amount of each asset.

The recoverable amount of an asset is the higher of its fair value less costs of disposal and the present value of the future cash flows expected to be derived from the asset. An asset's fair value is the price in a sale agreement in an arm's length transaction. If there is no sale agreement but the asset is traded in an active market, fair value shall be determined based on the bid price. If there is neither sale agreement nor active market for an asset, fair value shall be based on the best available information. Costs of disposal are expenses attributable to disposal of the asset, including legal fee, relevant tax and surcharges, transportation fee and direct expenses incurred to prepare the asset for its intended sale.

An impairment loss recognized shall not be reversed in a subsequent period.

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3. Significant Accounting Policies and Estimates (continued)

Financial liability

At initial recognition, financial liabilities are classified either as “financial liabilities at fair value through profit or loss” or “other financial liabilities”. The financial liabilities of the Group are mainly other financial liabilities, which include payables, loans and debenture payables.

Other financial liabilities are subsequently measured at amortized cost using the effective interest method. Gains or losses arising from derecognition or amortization is recognized in profit or loss for the period.

Financial Guarantee Contract

Financial guarantee contracts other than those designated as financial liabilities at fair value through profit or loss are initially recognized at fair value, and shall be subsequently measured at the higher of the following: (1) the amount determined in accordance with Accounting Standard for Business Enterprises No. 13 “Contingencies”; and (2) the amount initially recognized less cumulative amortization recognized in accordance with the principles set out in Accounting Standard for Business Enterprises No. 14 “Revenue”.

Derivative Instruments

Derivative instruments are initially recognized at fair value on the date on which a derivative contract is entered into and are subsequently measured at fair value. Any gains or losses arising from changes in fair value of derivatives are taken directly to profit or loss for the period, except for derivative instruments that are designated as hedging instruments and which are highly effective in hedging, gains or losses arising from changes in their fair value are taken to the profit or loss for the period in accordance with the hedge accounting requirement based on the nature of hedging relationships.

Employee Benefits

In the accounting period in which an employee has rendered services, the Group shall recognize the employee benefits payable as a liability.

The Group participates in social security systems operated by the government. Payments of social security contributions for employees, such as premiums or contributions on pensions, medical insurance, payments of housing funds and other social welfare contributions shall be included in the cost of related assets or profit or loss for the period in which they are incurred.

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3. Significant Accounting Policies and Estimates (continued)

Employee Benefits (continued)

When the Group terminates the employment relationship with employees before the expiry of the employment contracts or provides compensation as an offer to encourage employees to accept voluntary redundancy, if the Group has a formal plan for termination of employment relationship or has made an offer for voluntary redundancy, which will be implemented immediately, and the Group cannot unilaterally withdraw from the termination plan or the redundancy offer, a compensation liability arising from the termination of employment relationship with employees should be charged to the profit or loss for the current period.

An internal retirement plan is accounted for using the same principles as described above. Salaries and social insurance contributions to be paid to the internally retired employees by the Group during the period from the date when the employee ceases to provide services to the normal retirement date are recognized in profit or loss for the period when the recognition criteria for provisions are met (termination benefits).

Offset of Financial Assets and Financial Liabilities

If the Group owns the legitimate rights of offsetting the recognized financial assets and financial liabilities, which are enforceable currently, and the Group plans to realize the financial assets or to clear off the financial liabilities by net amount method, the amount of the offsetting financial assets and financial liabilities shall be reported in the balance sheet. Otherwise, financial assets and financial liabilities are presented separately in the balance sheet without offsetting.

Revenue recognition

Revenue from sales of goods

Revenue is recognized when the Company has transferred to the buyer the significant risks and rewards of ownership of the goods, retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold, will receive the economic benefits associated with the transaction, and can reliably measure the relevant amount of revenue and costs.

Sales of electricity

Sales of electricity are recognised when electricity are generated and transmitted to the power grid operated by the local electric power company.

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3. Significant Accounting Policies and Estimates (continued)

Revenue recognition (continued)

Sales of steam

Sales of steam are recorded based upon output delivered and capacity provided at rates specified under contract terms.

Interest income

Interest income is measured based on the length of time for which the Group's cash is used by others and the effective interest rate.

Government grant

Government grants are transfer of monetary assets or non-monetary assets from the government to the Group at no consideration, excluding capital considerations from the government as an owner of the Group. Government grants are classified into government grants related to assets and government grants related to income. Government grant shall be recognized when, and only when the related criteria are met.

If a government grant is in the form of a transfer of monetary asset, the item shall be measured at the amount received or receivable. If a government grant is in the form of a transfer of non-monetary asset, the item shall be measured at fair value. If fair value is not reliably determinable, the item shall be measured at a nominal amount and recognized immediately in profit or loss for the current period.

A government grant related to an asset shall be recognized as deferred income, and evenly amortized to profit or loss over the useful life of the asset. For a government grant related to income, if the grant is a compensation for related expenses or losses to be incurred in subsequent periods, the grant shall be recognized as deferred income, and recognized in profit or loss over the periods in which the related costs are recognized; if the grant is a compensation for related expenses or losses already incurred, the grant shall be recognized immediately in profit or loss for the current period.

For the repayment of a government grant already recognized, if there is any related deferred income, the repayment shall be off set against the carrying amount of the deferred income, and any excess shall be recognized in profit or loss for the current period; if there is no related deferred income, the repayment shall be recognized immediately in profit or loss for the current period.

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3. Significant Accounting Policies and Estimates (continued)

Borrowing costs

Borrowing costs include interest, amortization of discounts or premiums related to borrowings, ancillary costs incurred in connection with the arrangement of borrowings, and exchange differences arising from foreign currency borrowings. For borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset, when expenditures for the asset and borrowing costs are being incurred, activities relating to the acquisition, construction or production of the asset that are necessary to prepare the asset for its intended use or sale have commenced, such borrowing costs shall be capitalized as part of the cost of that asset; and capitalization shall discontinue when the qualifying asset is ready for its intended use or sale. Other borrowing costs shall be recognized as expense in the period in which they are incurred.

Where funds are borrowed for a specific purpose, the amount of interest to be capitalized shall be the actual interest expense incurred on that borrowing for the period less any bank interest earned from depositing the borrowed funds before being used into banks or any investment income on the temporary investment of those funds. Where funds are borrowed for general purpose, the Group shall determine the amount of interest to be capitalized on such borrowings by applying a capitalization rate to the weighted average of the excess amounts of cumulative expenditures on the asset over and above the amounts of specific-purpose borrowings. The capitalization rate shall be the weighted average of the interest rates applicable to the general-purpose borrowings.

During the capitalization period, exchange differences related to the principal and interest on a specific purpose borrowing denominated in foreign currency shall be capitalized as part of the cost of the qualifying asset. Exchange differences related to the principal and interest on general-purpose borrowings denominated in foreign currency shall be included in profit or loss for the current period.

Qualifying assets are assets (fixed assets, investment property, consumable biological assets, etc) that necessarily take a substantial period of time for acquisition, construction or production to get ready for their intended use or sale.

Capitalization of borrowing costs shall be suspended during periods in which the acquisition, construction or production of a qualifying asset is interrupted abnormally, when the interruption is for a continuous period of more than 3 months, until the acquisition, construction or production of the qualifying asset is resumed.

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3. Significant Accounting Policies and Estimates (continued)

Income Tax

Current income tax

At the balance sheet date, current income tax liabilities (or assets) for the current and prior periods shall be measured at the amount expected to be paid (or recovered) according to the requirements of tax laws. Taxable profits, which are the basis for calculating the current income tax expense, are determined after adjusting the accounting profits before tax for the period in accordance with relevant requirements of tax laws.

Deferred income tax assets and deferred income tax liabilities

Temporary differences arising from the difference between the carrying amount of an asset or liability and its tax base, and the difference between the tax base and the carrying amount of those items that are not recognized as assets or liabilities but have a tax base that can be determined according to tax laws, shall be recognized as deferred income tax assets and deferred income tax liabilities using the balance sheet liability method.

Deferred income tax liabilities are not recognized for taxable temporary differences related to: the initial recognition of goodwill; and the initial recognition of an asset or liability in a transaction which is neither a business combination nor affects accounting profit or taxable profit (or deductible loss) at the time of the transaction. In addition, the Group recognizes the corresponding deferred income tax liability for taxable temporary differences associated with investments in subsidiaries, associates and joint ventures, except when both of the following conditions are satisfied: the Group able to control the timing of the reversal of the temporary difference; and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets are not recognized for deductible temporary differences related to the initial recognition of an asset or liability in a transaction which is neither a business combination nor affects accounting profit or taxable profit (or deductible loss) at the time of the transaction. In addition, the Group recognizes the corresponding deferred income tax asset for deductible temporary differences associated with investments in subsidiaries, associates and joint ventures to the extent that it is probable that taxable profits will be available against which the deductible temporary differences can be utilized, except when both of the following conditions are satisfied: it is not probable that the temporary difference will reverse in the foreseeable future; and it is not probable that taxable profits will be available in the future, against which the temporary difference can be utilized.

The Company recognizes a deferred income tax asset for the carry forward of deductible losses and tax credits to subsequent periods, to the extent that it is probable that future taxable profits will be available against which the deductible losses and tax credits can be utilized.

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3. Significant Accounting Policies and Estimates (continued)

Income Tax (continued)

Deferred income tax assets and deferred income tax liabilities (continued)

At the balance sheet date, deferred income tax assets and deferred income tax liabilities are measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled, according to the requirements of tax laws.

At the balance sheet date, the Company shall review the carrying amount of a deferred income tax asset. If it is probable that sufficient taxable profits will not be available in future periods to allow the benefit of the deferred income tax asset to be utilized, the carrying amount of the deferred income tax asset shall be reduced. Any such reduction in amount shall be reversed when it becomes probable that sufficient taxable profits will be available.

Income tax expense

Income tax expense comprises current income tax expense and deferred income tax expense.

Current income tax expense (current income tax income) and deferred income tax expense (deferred income tax income) are included in profit or loss for the current period, except for: current income tax and deferred income tax related to transactions or events that are directly recognized in owners' equity, which are recognized directly in owners' equity, and deferred income tax arising from a business combination, which is adjusted against the carrying amount of goodwill.

Offset of income tax

After granted the legal rights of net settlement and with the intention to use net settlement or obtain assets, repay debt, the Group, at the same time, records the net amount after offsetting its current income tax assets and current income tax liabilities.

The Group was granted the legal rights of net settlement of current income tax assets and current income tax liabilities. Deferred income tax assets and deferred income tax liabilities are related to income tax to be paid by the same entity liable to pay tax to the same tax collection and management authority or related to different entities liable to pay tax, but the relevant entity liable to pay tax is intended to apply net settlement of current income tax assets and liabilities or, at the same time, obtain assets, repay debt whenever every deferred income tax assets and liabilities with importance would be reversed in the future, the Group records the net amount after offsetting its current income tax assets and current income tax liabilities.

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3. Significant Accounting Policies and Estimates (continued)

Business combination

Business combination refers the transaction or event to combine two or more independent entities into one reporting subject. Business combination is classified into business combination under common control and not under common control.

The Group recognizes assets and liabilities obtained arising from business combination recognized on the date of merger or acquisition. The date of merger or acquisition means the date on which the controlling right of the entity being merged or of the acquiree is obtained, which is the date on which the control over the net assets or production and management decision is assigned to the Group.

Business combinations and goodwill not involving entities under common control

A business combination not involving entities under common control is a business combination in which all of the combining entities are not ultimately controlled by the same party or parties both before and after the business combination. For business combination not involving entities under common control, the acquirer is the entity that obtains control of the other entities participating in the combination at the acquisition date, and the other entities participating in the combination are the acquirees.

For business combination not involving entities under common control, the cost of a business combination is the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the acquirer, in exchange for control of the acquiree plus any costs directly attributable to the business combination. When the business combination is achieved in stage, the cost of the combination is the aggregate cost of the individual transactions. When a business combination agreement provides for an adjustment to the cost of the combination contingent on future events, the acquirer shall include the amount of that adjustment in the cost of the combination at the acquisition date if the adjustment is probable and can be measured reliably

The acquiree's identifiable assets, liabilities and contingent liabilities acquired from business combination not involving entities under common control are recognised at their fair values at the acquisition date if the recognition conditions are met.

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3. Significant Accounting Policies and Estimates (continued)

Business combination (continued)

Business combinations and goodwill not involving entities under common control (continued)

Where the cost of a business combination exceeds the acquirer's interest in the fair value of the acquiree's identifiable net assets, the difference is recognized as goodwill. Where the cost of a business combination is less than the acquirer's interest in the fair value of the acquiree's identifiable net assets, the acquirer reassesses the measurement of the fair values of the acquiree's identifiable net assets, liabilities and contingent liabilities and the measurement of the cost of combinations. If after that reassessment, the cost of combination is still less than the acquirer's interest in the fair value of the acquiree's identifiable net assets, the difference is recognized in the profit or loss for the current period.

Debt restructuring

The term "debt restructuring" refers to an event in which the settlement of a debt is arrived in as a result of a mutual agreement between a debtor and a creditor or a judgment of a court when the debtor gets into a financial problem.

Obligations to record debt restructuring as debtor

When a debt is liquidated by cash, the debtor shall include the difference between the book value of the debt to be restructured and the actual payment into the current profits and losses. When a debt is liquidated by a non-cash asset, the debtor shall include the difference between the book value of the debt to be restructured and the fair value of the non-cash asset transferred into the current profits and losses. The difference between fair value of the non-cash asset transferred and its book value shall be included in the current profits and losses. When a debt is converted into capital, the debtor shall include the difference between the book value of the debt to be restructured and the fair value of shares to which the creditor becomes entitled for waiver of the credit into the current profits and losses. Where other terms of a debt are modified, the debtor shall regard the post-modification fair value of the debt as the entry value of the restructured debt, and shall include the difference between the book value of the debt to be restructured and the book value of the restructured debt in the current profits and losses. Where a debt restructuring is made by a combination of several methods, the debtor shall offset, one by one, the cash paid, the fair value of the non-cash asset transferred, and the fair value of the shares to which the creditor becomes entitled, against the book value of the debt to be restructured, then handle it in accordance with the aforesaid provisions of modification of other terms of a debt.

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3. Significant Accounting Policies and Estimates (continued)

Debt restructuring (continued)

Obligations to record debt restructuring as creditor (continued)

When a debt is liquidated by cash, the creditor shall include the difference between the book balance of the debt to be restructured and the cash received in the current profits and losses. When a debt is liquidated by a non-cash asset, the creditor shall include the difference between the book balance of the debt to be restructured and the fair value of the non-cash asset received in the current profits and losses. When a debt is converted into capital, the creditor shall include the difference between the fair value of the shares to which it becomes entitled as investment to the debtor and the book balance of the debt to be restructured into the current profits and losses. Where other terms of a debt are modified, the creditor shall regard the post-modification fair value of the debt as the book value of the restructured debt, and shall include the difference between the book balance of the debt to be restructured and the book value of the restructured debt in the current profits and losses. Where a debt restructuring is made by a combination of several methods, the debtor shall offset, one by one, the cash received, the fair value of the non-cash asset received, and the fair value of the shares to which the creditor becomes entitled to offset against the book balance of the debt to be restructured, then handle it in accordance with the aforesaid provisions of modification of other terms of a debt.

If the creditor has made provision for the impairment of the debt to be restructured, it shall first offset the aforesaid difference against the impairment provision, and then include the shortfall in the current profits and losses.

Lease

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. Title may or may not eventually be transferred. All other leases are classified as operating leases.

Operating lease business with the Group recorded as lessee

Lease payment for operating lease is recognized as related asset cost or profits and losses for the current period using the straight-line method over the lease term. The initial direct cost is directly accounted in profit or loss for the current period. Contingent rent is recognized as profit or loss for the current period upon occurrence.

Operating lease business with the Group recorded as lessor

Rental income is recognized in profit or loss for the current period using the straight-line method over the lease term. The initial direct cost where the amount is larger is capitalized when incurred, and accounted for as profit or loss for the current period on the same basis as recognition of rental income over the entire lease period. Contingent rental is accounted for as profit or loss for the period in which it is incurred.

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3. Significant Accounting Policies and Estimates (continued)

Basis for Preparation of Consolidated Financial Statements

The scope of consolidated financial statements is determined on the basis of control. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its operating activities.

The Group recognizes the date when control of subsidiaries was substantially transferred as the date of acquisition or disposal. For disposal of subsidiaries, operating results and cash flows of such subsidiaries from the period beginning to the date of disposal are included into the consolidated income statement and consolidated cash flow statement; for disposal of subsidiaries during the reporting period, no adjustment shall be made to the opening balance of the consolidated balance sheet. For those subsidiaries acquired not controlled by the same parent, the operating results and cash flows after the acquisition date have been properly included in the consolidated income statements and consolidated cash flow statements. No adjustments shall be made to the opening balance of the consolidated balance sheet and the comparative consolidated financial statements amount. For those subsidiaries acquired or disposed controlled by the same parent company, the operating results and cash flows from the opening of the consolidation period to the consolidation date are also presented in the consolidated income statement and the consolidated cash flow statements. The comparative consolidated financial statements amount is also adjusted respectively.

Major accounting policies and accounting periods adopted by the subsidiaries are defined according to the standardized accounting policies and accounting periods stipulated by the Company.

All significant intra-group accounts and transactions between the parent company and its subsidiaries or between subsidiaries are eliminated on consolidation.

The portion of a subsidiary's equity that is not attributable to the parent is treated as minority interests and presented as "minority interest" in the consolidated balance sheet within owners' equity. The portion of net profits or losses of subsidiaries for the period attributable to minority interests is presented in the consolidated income statement under the "net profit" line item as "minority interests". When the amount of loss attributable to the minority shareholders of a subsidiary exceeds the minority shareholders' portion of the opening balance of owners' equity of the subsidiary, where the minority shareholders have a binding obligation under the articles of association or an agreement and are able to make an additional investment to cover the loss, the excess amount shall be allocated against minority interest; otherwise the excess amount shall be allocated against shareholders' equity attributable to the parent. If the subsidiary subsequently reports profits, such profits shall be allocated to shareholders' equity attributable to the parent until the minority shareholders' share of losses previously absorbed by the parent has been recovered.

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3. Significant Accounting Policies and Estimates (continued)

Translation of Financial Statements Denominated in Foreign Currency

The financial statements denominated in foreign currency of a foreign operation are translated to RMB in comply with the following requirement: assets and liabilities on the balance sheet are translated at the spot exchange rate prevailing at the balance sheet date; all equity items except for inappropriate profits are translated at the spot exchange rates at the dates on which such items arose; income and expenses in the income statement are translated at the spot exchange rate at the date of transaction; the inappropriate profits brought forward are reported at the prior year's closing balance; the inappropriate profits carried forward are calculated, based on the translated amounts of profits and other profit appropriation items; and all exchange differences resulting from the translation are recognized separately as "translation reserve" in the shareholders' equity on the balance sheet.

On disposal of foreign operations, exchange differences arising from the translation of financial statements denominated in foreign currencies related to the disposed foreign operation which has been included in shareholders' equity in the balance sheet, shall be transferred to profit or loss in whole or in proportionate share in the period in which the disposal took place.

Cash flow dominated in foreign currency or from foreign subsidiaries shall be translated at the spot exchange rate when it incurs. Effects arising from changes of exchange rate of cash and cash equivalents shall be presented separately as "Effect of changes in exchange rates on cash and cash equivalents" in the cash flow statement.

The opening balances and prior year's figures are presented according to the translated amounts of the prior year.

Related parties

If a party has the power to control, jointly control or exercise significant influence over another party, they are regarded as related parties. Two or more parties are also regarded as related parties if they are subject to control, joint control or significant influence from the same party.

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IV. Critical judgments based on Significant Accounting Policies and Key Assumptions and Uncertainties in Accounting Estimates

In the application of the Group's accounting policies, which are described in Note III, the Group is required to make judgments, estimates and assumptions about the carrying amounts of items in the financial statements due to the uncertainties associated with operating activities. These judgments, estimates and assumptions are based on historical experience of the Group's management as well as other factors that are considered to be relevant. Actual results may differ from these estimates.

The aforementioned judgments, estimates and assumptions are reviewed regularly by the Group on a going concern basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Critical judgments in applying the Group's accounting policies

In the application of the Group's accounting policies, management has made the following judgments that have the most significant effect on the amounts recognized in the consolidated financial statements:

Timing of transfer of constructions in progress to fixed assets

In determining the timing when the construction in progress, especially for large-scale paper manufacturing plant and machinery, is transferred to fixed assets requires the Group to determine whether all the activities necessary to bring fixed assets to be ready for their intended use are completed and related direct expenditure are included in the cost of asset. Such determination requires the use of management's judgment and experience.

Provision for bad debts

The Group recognizes provision for bad debts according to the recoverability of receivables. When there is evidence indicating that a receivable item is not collectible, provision for bad debts will be recognized. Recognition of bad debts requires the use of judgments and estimates. If the result of new estimates differs from the original estimates, such difference will impact the carrying amount of receivables for the corresponding period.

Provision for inventory impairment

Provision for inventory impairment is recognized according to the net realizable value of the inventory. Provision for inventory impairment will be recognized when there is evidence indicating that the net realizable value is lower than the cost. Recognition of net realizable value involves the use of judgments and estimates. If the result of new estimates differs from the original estimates, such difference will impact the carrying value of inventory for the corresponding period.

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IV. Critical judgments based on Significant Accounting Policies and Key Assumptions and Uncertainties in Accounting Estimates (continued)

Recognition of deferred income tax assets

The Group assesses whether recognition of deferred income tax assets is required at each balance sheet date. Deferred income tax assets relating to certain deductible temporary differences and tax losses are recognized when the Group considers it is probable that future deductible taxable profits will be available against which the temporary differences or tax losses can be utilized. In assessing whether it is probable that future deductible taxable profits will be available against which the temporary differences or tax losses can be utilized requires the use of appropriate judgments and estimates.

Depreciation of fixed assets

Fixed assets are provided and depreciated on a straight-line basis over their estimated useful lives, after taking into account their residual value. The Group assesses annually the residual value and the useful life of the fixed assets. If revaluation takes place, the expectation differs from the original estimate. Such difference will impact the book value of fixed assets in the year in which such estimate has been changed.

Impairment of fixed assets

The Group assesses annually whether fixed assets have any indication of impairment in accordance with the accounting policy. The recoverable amounts of fixed assets have been determined based on the higher of value-in-use calculations and fair value less cost to sell. These calculations require the use of judgment and estimates. Where the actual future cash flows are less than expected, a material impairment loss may arise.

Impairment of goodwill

When conducting goodwill impairment test, the present value of projected future cash flow of the underlying assets or portfolio of assets incorporating such goodwill will be calculated, and projection of the future cash flow of those assets or portfolio of assets will be made, and a pre-tax interest rate shall be determined which can properly reflect the prevailing time value of currency in the market as well as the specific risks relevant to such assets. If such estimated interest rate is lower than the actual interest rate or the actual cash flow is lower than the initial estimated cash flow, it is required to recognize additional impairment. Such impairment will impact the goodwill impairment during the period when such judgment was made.

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V. Taxation

Taxes that the Group is subject to include value added tax, enterprise income tax, business tax, and property tax and land use tax.

Value Added Tax

Value added tax ("VAT") payable is the net difference between output VAT less deductible input VAT. The effective tax rates of output VAT and input VAT of the Group's relevant VAT items are as follows:

Item	Tax rate %
Product sold in the domestic market (output VAT)	17
Paper core sales, printing (output VAT)	17
Purchase of barley grass, pampas grass (input VAT)	13
Steam power for production use (input VAT)	13
Electric power for production use (input VAT)	17
Sodium silicate, paperboard for production use (input VAT)	17
Purchase of waste paper (input VAT)	10
Coal (input VAT)	13

Pursuant to Cai Shui [1995] No. 44 "Circular on VAT Exemption for Certain Products Applying Integrated Use of Resources" issued by the State Administration of Taxation (《國家稅務總局對部分資源綜合利用產品免徵增值稅的通知》), enterprises engaged in utilization of raw materials containing not less than 30% of coal gangue, stone coal, coal ash, bottom ash of coal boiler (excluding blast furnace water quenching residue) in the production of buildings products shall be exempted from VAT. Wuhan Chenjian New-style Wall Materials Co., Ltd. (武漢晨建新型牆體材料有限公司), a subsidiary of the Company, utilizes raw materials containing above 30% of coal ash in its production. It is thus qualified as an enterprise engaged in the utilization of waste in production and is exempted from VAT in the latter half of 2008.

Pursuant to Cai Shui [2001] No. 78 "Circular on the VAT Policy concerning Waste Collection Business" issued by the State Administration of Taxation (《國家稅務總局關於廢舊物資回收經營業務有關增值稅政策的通知》), since 2001, general taxpayers engaging in the sale of waste materials business will be exempted from VAT. Accordingly, Qihe Chenming Waste Collection Co., Ltd. (齊河晨鳴廢舊物資收購有限公司), Jilin Chenming Waste Collection Co., Ltd. (吉林晨鳴廢舊物資回收有限公司) and Shouguang City Run Sheng Wasted Paper Recycle Co., Ltd. (壽光市潤生廢紙回收有限責任公司), subsidiaries of the Company, are covered by the preferential policy of VAT exemption.

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V. Taxation (continued)

Value Added Tax (continued)

Pursuant to Cai Shui Zi [1995] No. 44 “Circular on VAT Exemption for Certain Products Applying Integrated Use of Resources” issued by the Ministry of Finance and the State Administration of Taxation (《財政部、國家稅務總局關於對部分資源綜合利用產品免徵增值稅問題的通知》) and the relevant requirements of Cai Shui Zi [2001] Document No. 72, Shandong Chenming Panels Co., Ltd. (山東晨鳴板材有限責任公司), Qihe Chenming Panels Co., Ltd. (齊河晨鳴板材有限責任公司), Juancheng Chenming Panels Co., Ltd (鄆城晨鳴板材有限責任公司) and Heze Chenming Panels Co., Ltd. (荷澤晨鳴板材有限責任公司), all being subsidiaries of the Company and produce products that applied integrated use of resources, are subject to an immediate VAT refund policy.

Other Taxes

Enterprise Income Tax

Income tax rates applicable to the Company and its subsidiaries

Hailaer Chenming Paper Co., Ltd. (海拉爾晨鳴紙業有限責任公司), a subsidiary of the Company established in the Inner Mongolia Autonomous Region and covered by the preferential tax policy for industries encouraged by the State Government, enjoyed the preferential income tax rate of 15% from 2001 to 2010 pursuant to Guo Shui Fa (2002) Document No. 47 issued by the State Administration of Taxation.

Pursuant to the Guo Xi Ban Zong [2001] Document No. 10 “Written Reply concerning the Application of the Preferential Tax Policies on Development of the Western Region in Yanbian Korean Autonomous Prefecture ” issued by the Office of the Leading Group for Western Region Development of the State Council (《國家稅西部開發辦關於延邊朝鮮族自治州參照報行國家西部大開發優惠政策的復函》) and Yanzhou local tax notice [2001] Document No. 99 “Letter confirming the entitlement of 吉林晨鳴亞松漿紙有限公司 to preferential tax policy” issued by the local tax bureau of Yanbian Korean Autonomous Prefecture (《延邊州地方稅務局關於吉林晨鳴亞松紙有限公司享受稅收優惠政策承諾的函》), Yanbian Chenming Paper Co., Ltd. (延邊晨鳴紙業有限公司), a subsidiary of the Company, is covered by the preferential tax policies on development of the Western Region and thus enjoys preferential tax rate of 15% from 2001 to 2010.

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V. Taxation (continued)

Other Taxes (continued)

Enterprise Income Tax (continued)

Income tax rates applicable to the Company and its subsidiaries (continued)

Shandong Chenming Xinli Power Co., Ltd. (山東晨鳴新力熱電有限公司), a subsidiary of the Company, was established in 2001 as a Sino-foreign joint venture and engaged in the business of electric power and thermal power generation. Pursuant to Rule No. 73 of "Detailed Rules on the Implementation of the Income Tax Law of The People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises" (《中華人民共和國外商投資企業和外國企業所得稅法實施細則》) and rules under the State Council's Circular on Expanding Application Scope of Income Tax Preferential Treatment on Enterprises with Foreign Investment Engaged in Energy or Traffic Infrastructure Projects (《國務院關於擴大外商投資企業從事能源交通基礎設施項目稅收優惠規定使用範圍的通知》) (Guo Fa [1999] No. 13), and Guo Shui Han [2002] Document No. 1032 "Written Reply on issues regarding the application of preferential enterprise income tax rate to Shandong Chenming Xinli Power Co., Ltd." from the State Council (《國家稅務總局關於山東晨鳴新力熱電有限公司適用企業所得稅率問題的批復》), Shandong Chenming Xinli Power Co., Ltd. is subject to income tax rate of 15%. Pursuant to Guo Fa [2007] Document No. 39 "Circular on Transitional Preferential Enterprise Income Tax Policy" issued by the State Council (《國務院關於實施企業所得稅過渡優惠政策的通知》), the subsidiary was subject to the income tax rate of 18% in 2008.

Wuhan Chenming Hanyang Paper Co., Ltd. (武漢晨鳴漢陽紙業股份有限公司), a subsidiary of the Company, was transformed into an EFI in April 2005. Pursuant to the Income Tax Law of The People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises and its implementation rules, and as approved by State Taxation Administration of Economic and Technological Development Zone of Wuhan City, the income tax for 2007 was reduced in half. Pursuant to Guo Fa [2007] Document No. 39 "Circular on Transitional Preferential Enterprise Income Tax Policy" issued by the State Council (《國務院關於實施企業所得稅過渡優惠政策的通知》), the subsidiary was subject to income tax rate of 9% in 2008.

Jiangxi Chenming Paper Co., Ltd. (江西晨鳴紙業有限責任公司), a subsidiary of the Company, was transformed into an EFI in 2004. It engaged in production with a period of operation of more than 10 years as a foreign-investment enterprise. 2008 was the second year since it started to make profits. Pursuant to Guo Fa [2007] Document No. 39 "Circular on Transitional Preferential Enterprise Income Tax Policy" issued by the State Council (《國務院關於實施企業所得稅過渡優惠政策的通知》), the subsidiary was exempt from the income tax this year.

Except for the above preferential enterprise income tax policies, the Company and its remaining subsidiaries are subject to enterprise income tax rate of 25% in the reporting period.

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V. Taxation (continued)

Other Taxes (continued)

Crediting Payment on Purchase of Domestically-Made Equipment as Investments

Pursuant to the Circular on Several Issues concerning Crediting Payment on Purchase of Domestically-Made Equipment as Investments against Enterprise Income Tax by Foreign-invested Enterprises and Foreign Enterprises (《關於外商投資企業和外國企業購買國產設備投資抵免企業所得稅有關問題的通知》) issued by the Ministry of Finance and the State Administration of Taxation (Cai Shui [2000] No. 49) and the Provisional Measures concerning Crediting Payment on Purchase of Technologically Improved Domestically-Made Equipment as Investments against Enterprise Income Tax (《技術改造國產設備投資抵免企業所得稅暫行辦法》) (Cai Shui Zi [1999] No. 290), the 40 percent of the Group's payments on domestically-made equipment is creditable against the increased amount in its enterprise income taxes in the year of purchase over that of the year before. The allowable tax credit of an enterprise shall not exceed its newly increased enterprise income tax for the year of purchase over that of the year before. If the amount of newly increased enterprise income tax is not sufficient for tax credit, the remaining part of the investment which exceeds the tax credit shall be refundable against the newly increased tax of the next year over that of the year before the year of purchase. However, the period for continuous tax credit shall not exceed five years.

Pursuant to Guo Shui Fa [2008] Document No. 52 "Circular on Policy Question about Postponement to Implement to Set Off Enterprise Income Tax with Investment To Acquire Domestic Equipment by Enterprise" issued by State General Tax Bureau (《關於停止執行企業購買國產設備投資抵免企業所得稅政策問題的通知》), postponement to implement to the policy to set off enterprise income tax with investment to acquire domestic equipment by an enterprise has been carried out since 1 January 2008. Income tax credits in respect of investments in domestic-manufactured equipment as approved in prior years will continue to be credited within the extended period.

Business tax

Business tax is calculated and paid at 5% of the maintenance fee income and interest income, and at 3% of transportation fee income.

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V. Taxation (continued)

Urban maintenance and construction tax and educational surcharges

The Company and certain of its subsidiaries, including Wuhan Chenming Hanyang Paper Co., Ltd., Shandong Chenming Xinli Power Co., Ltd., Jiangxi Chenming Paper Co., Ltd., and Jilin Chenming Paper Co., Ltd. are EFIs, and therefore are exempted from urban maintenance and construction tax and education surcharges. As for Shandong Chenming Paper Group Qihe Paperboard Co., Ltd., urban maintenance and construction tax and education surcharges are calculated and paid at 5% and 3%, respectively, on the total amount of VAT payable and business tax payable; while that for other subsidiaries of the Company are calculated and paid at 7% and 3%, respectively, on the total amount of VAT payable and business tax payable.

Individual income tax

Individual income tax payable by the Group's employees is withheld and paid by the Group.

Property tax and land use tax

Property tax is levied based on 70% of the original cost of the building properties of the Group at the tax rate of 1.2%. Land use tax is calculated based on the actual area of land used by the Group and is levied in accordance with the stipulated tax rate.

VI. The scope of consolidated financial statement and controlling subsidiaries

The subsidiaries of the Company were established in the purpose of investment:

Name	Enterprise type	Organization Code	Legal representative	Place of Incorporation	Principal activity	Registered capital (in ten thousand)	The actual investment by the Group at the end of the year (in ten thousand)	The aggregate shareholding of the Group (%)	The aggregate voting rights held by the Group (%)
武漢晨鳴漢陽紙業股份有限公司 (Wuhan Chenming Hanyang Paper Holdings Co., Ltd.)	Foreign investment enterprise	27189235-4	譚道成	Wuhan City	Manufacture and sales of paper products, the materials of manufacture of paper and machinery	21,136	20,283	50.93	50.93

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VI. The scope of consolidated financial statement and controlling subsidiaries (continued)

Name	Enterprise type	Organization Code	Legal representative	Place of Incorporation	Principal activity	Registered capital (in ten thousand)	The actual investment by the Group at the end of the year (in ten thousand)	The aggregate shareholding of the Group (%)	The aggregate voting rights held by the Group (%)
山東晨鳴紙業集團齊河板紙有限責任公司 (Shandong Chenming Paper Group Qihe Paperboard Co., Ltd.)	Limited liability company	72074277-4	刑方同	Qihe, Shandong	Manufacture, processing and sales of paperboard and packaging paper	37,620	37,620	100	100
山東晨鳴熱電股份有限公司 (Shandong Chenming Power Supply Holdings Co., Ltd.)	Limited liability company	70620711-8	孫洪吉	Shouguang, Shandong	Manufacture and supply of electricity and heat	9,955	15,781	86.71	86.71
延邊晨鳴紙業有限責任公司 (Yanbian Chenming Paper Co., Ltd.)	Limited liability company	72958840-0	桑景高	Longjing, Jilin	Mucilage glue fiber pulp, pulp and machine-made paper	8,163.3	4,009	76.73	76.73
江西晨鳴紙業有限責任公司 (Jiangxi Chenming Paper Co., Ltd.)	Foreign investment enterprise	74426460-7	譚道成	Nanchang city	Production and sales of high-grade paper, paperboard (ex. newsprint) and homemade pulp	USD172,000 (in ten thousand)	69,755	51	51
壽光市晨鳴天園林業有限公司 (Shouguang Chenming Tianyuan Arboriculture Co., Ltd.)	Limited liability company	73925671-7	李德江	Shouguang, Shandong	Development, nurture of fast growth poplar, forest, vegetable and fruit	1,059	720	68	68

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VI. The scope of consolidated financial statement and controlling subsidiaries (continued)

Name	Enterprise type	Organization Code	Legal representative	Place of Incorporation	Principal activity	Registered capital (in ten thousand)	The actual investment by the Group at the end of the year (in ten thousand)	The aggregate shareholding of the Group (%)	The aggregate voting rights held by the Group (%)
海拉爾晨鳴紙業 有限責任公司 (Hailaer Chenming Paper Co., Ltd.)	Limited liability company	70130836-6	高子偉	Hailaer City	Sales of machine-made paper and pulp paper	1,600	1,200	75	75
赤壁晨鳴紙業 有限公司 (Chibi Chenming Paper Co., Ltd.)	Limited liability company	42203935-3	陳建明	Chibi, Hubei	Production and sales of paper pulp, paper products and the materials of production of paper, and Production, processing, import and export of the machine of manufacture of paper	17,742	3,548	51	51
武漢晨鳴乾能熱電 有限責任公司 (Wuhan Chenming Qianneng Electric Power Co., Ltd.)	Limited liability company	72579372-2	張利平	Wuhan City	Generation and sales of electricity and heat	8,824	4,500	51	51
武漢晨建新型牆體材料 有限公司 (Wuhan Chenjian New-style Wall Materials Co., Ltd.)	Limited liability company	74475404-0	呂學峰	Wuhan City	Production, operation and sales of aerated fly ash Concrete block	1,000	510	51	51

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VI. The scope of consolidated financial statement and controlling subsidiaries (continued)

Name	Enterprise type	Organization Code	Legal representative	Place of Incorporation	Principal activity	Registered capital (in ten thousand)	The actual investment by the Group at the end of the year (in ten thousand)	The aggregate shareholding of the Group (%)	The aggregate voting rights held by the Group (%)
山東晨鳴新力熱電有限公司(Shandong Chenming Xinli Power Co., Ltd.)	Limited liability company	72073121-5	孫洪吉	Shouguang, Shandong	Generation and supply of electricity and heat	USD1,180 (in ten thousand)	7,239	51	51
壽光市晨鳴水泥有限公司(Shouguang Chenming Cement Co., Ltd.)	Limited liability company	73720178-X	孫洪吉	Shouguang, Shandong	Utilization of ash in the production of cement and sales of cement	700	700	100	100
山東晨鳴板材有限公司(Shandong Chenming Panels Co., Ltd.)	Limited liability company	73816170-8	劉樹森	Shouguang, Shandong	Production, processing and sales of the decorative board of the layer of laminated board, wooden products, laminated board, fortified wooden floorboard and impregnated paper	3,000	3,000	100	100
壽光晨鳴地板有限公司(Shouguang Chenming Floor Board Co., Ltd.)	Limited liability company	76366212-5	劉樹森	Shouguang, Shandong	Production, processing and sales of fortified wooden floorboard and impregnated paper	50	50	100	100

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VI. The scope of consolidated financial statement and controlling subsidiaries (continued)

Name	Enterprise type	Organization Code	Legal representative	Place of Incorporation	Principal activity	Registered capital (in ten thousand)	The actual investment by the Group at the end of the year (in ten thousand)	The aggregate shareholding of the Group (%)	The aggregate voting rights held by the Group (%)
齊河晨鳴板材有限公司(Qihe Chenming Panels Co., Ltd.)	Limited liability company	76001404-2	劉樹森	Qihe, Shandong	Production, processing and sales of high-density (medium-density) fiberboard, decorative panel, melamine impregnated paper and composite floor	4,082	4,082	100	100
菏澤晨鳴板材有限公司(Heze Chenming Panels Co., Ltd.)	Limited liability company	75827615-8	劉樹森	Heze, Shandong	Production, processing and sales of high-density (medium-density) fiberboard, decorative panel, melamine impregnated paper and composite floor	3,000	3,000	67	67
陽江晨鳴林業發展有限公司(Yangjiang Chenming Arboriculture Co., Ltd.)	Limited liability company	78487434-6	尹同遠	Yangjiang, Guangdong	Cultivation and development forest, and technology consultation of forestry	100	100	100	100

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VI. The scope of consolidated financial statement and controlling subsidiaries (continued)

Name	Enterprise type	Organization Code	Legal representative	Place of Incorporation	Principal activity	Registered capital (in ten thousand)	The actual investment by the Group at the end of the year (in ten thousand)	The aggregate shareholding of the Group (%)	The aggregate voting rights held by the Group (%)
湛江晨鳴林業發展有限公司(Zhanjiang Chenming Arboriculture Co., Ltd.)	Limited liability company	78298807-5	王在國	Zhanjiang, Guandong	Cultivation of forest, nutrition and sales of seedling, processing and sales of timber and processing and sales of by-products of timber	100	100	100	100
吉林晨鳴紙業有限公司(Jilin Chenming Paper Co., Ltd.)	Limited liability company	78298556-0	王在國	Jilin City, Jilin province	Processing and sales of machine-made paper, paperboard, paper product, paper pulp, machinery and equipment of manufacture of paper	150,000	150,135	100	100
鄧城晨鳴板材有限公司(Juancheng Chenming Panels Co., Ltd.)	Limited liability company	77872435-X	侯煥才	Juancheng, Shandong	Production and sales of particle board, decorative particle board and melamine impregnated paper	1,500	1,500	100	100

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VI. The scope of consolidated financial statement and controlling subsidiaries (continued)

Name	Enterprise type	Organization Code	Legal representative	Place of Incorporation	Principal activity	Registered capital (in ten thousand)	The actual investment by the Group at the end of the year (in ten thousand)	The aggregate shareholding of the Group (%)	The aggregate voting rights held by the Group (%)
山東樂景大酒店有限公司 (Shandong Grand View Hotel Co., Ltd.)	Limited liability company	97529857-8	劉樹森	Shouguang, Shandong	Restaurant and beverage services	USD1,391 (in ten thousand)	8,050	70	70
湛江晨鳴漿紙有限公司 (Zhanjiang Chenming Paper Pulp Co., Ltd.)	Limited liability company	77527884-1	馮新泉	Zhanjiang, Guangdong	Improvement of plant fostering, true planting and soil, research of forestry, manufacture, production, processing and sales of paper pulp	50,000	50,000	100	100
晨鳴(香港)有限公司 (Chenming (HK) Limited)	Limited liability company	3734927300011088	魏克雨	Hong Kong, China	Export and import trade of paper products and market research	USD10 (in ten thousand)	78	100	100
壽光晨鳴現代物流有限公司 (Shouguang Chenming Modern Logistic Co., Ltd.)	Limited liability company	66015223-7	陳洪國	Shouguang, Shandong	Transportation of good	1,000	1,000	100	100
壽光市潤生廢紙回收有限責任公司 (Shouguang City Run Sheng Wasted Paper Recycle Co., Ltd.) (Note 1)	Limited liability company	77316557-9	陳洪國	Shouguang, Shandong	Purchase and sales of waste goods and materials	100	100	100	100

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VI. The scope of consolidated financial statement and controlling subsidiaries (continued)

Name	Enterprise type	Organization Code	Legal representative	Place of Incorporation	Principal activity	Registered capital (in ten thousand)	The actual investment by the Group at the end of the year (in ten thousand)	The aggregate shareholding of the Group (%)	The aggregate voting rights held by the Group (%)
壽光晨鳴美術紙有限公司 (Shouguang Chenming Art Paper Co., Ltd.)	Limited liability company	79867677-0	尹同遠	Shouguang, Shandong	Production of art paper, and sales of the product which produced by the Company	USD2,000 (in ten thousand)	11,362	75	75
齊河晨鳴廢舊物資收購有限公司 (Qihe Chenming Waste Collection Co., Ltd.)	Limited liability company	75825591-2	李峰	Qihe, Shandong	Purchase and sales of waste and old material	50	50	98	98
吉林晨鳴廢舊物資回收有限公司 (Jilin Chenming Waste Collection Co., Ltd.)	Limited liability company	77872731-5	張邦吉	Jilin	Purchase and sales of waste and old material	100	100	100	100
吉林市晨鳴機械製造有限公司 (Jilin Chenming Machinery Manufacturing Co., Ltd.)	Limited liability company	66012410-5	張春林	Jilin	Processing of machinery, manufacture, installation and repair of the equipment of machinery	60	60	100	100
南昌晨鳴林業發展有限公司 (Nanchang Chenming Arboriculture Co., Ltd.)	Limited liability company	66204306-9	張國英	Nanchang, Jiangxi chips	Processing and sales of wood	1,000	1,000	100	100

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VI. The scope of consolidated financial statement and controlling subsidiaries (continued)

Name	Enterprise type	Organization Code	Legal representative	Place of Incorporation	Principal activity	Registered capital (in ten thousand)	The actual investment by the Group at the end of the year (in ten thousand)	The aggregate shareholding of the Group (%)	The aggregate voting rights held by the Group (%)
富裕晨鳴紙業 有限責任公司 (Fuyu Chenming Paper Co., Ltd.)	Limited liability company	66389298-6	劉春山	Fuyu County, Qiqihar City	Production and sales of machine-made paper and paperboard	20,800	20,800	100	100
無錫松嶺紙業有限公司 (Wuxie Song Ling Paper Co., Ltd.) (Note 1)	Limited liability company	76243145-6	劉春山	Wuxie City	Sales, cutting and processing of paper	501	—	100	100
黃岡晨鳴林業發展 有限責任公司 (Huanggang Chenming Arboriculture Co., Ltd.) (Note 1)	Limited liability company	67036898-X	王在國	Huanggang city	Nutrition of forest resources, cultivation, processing and sales of forest	1,000	1,000	100	100
黃岡晨鳴漿紙有限公司 (Huanggang Chenming Paper Co., Ltd.) (Note 1)	Limited liability company	67976586-9	肖翔	Huanggang city, Hubei	Operation and acquisition of forest; establishment of paper projects	2,000	2,000	100	100
咸甯晨鳴林業發展 有限責任公司 (Xianning Chenming Arboriculture development Co., Ltd. (Note 1)	Limited liability company	67975036-8	王在國	Xianning, Hubei	Plantation of forest, processing and sales	1,000	1,000	100	100

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VI. The scope of consolidated financial statement and controlling subsidiaries (continued)

Note 1: Newly acquired subsidiaries which were consolidated in this year:

咸寧晨鳴林業發展有限責任公司(Xianning Chenming Arboriculture development Co., Ltd.)

The Company contributed capital to set up Xianning Chenming Arboriculture development Co., Ltd. on 1 September 2008, its registered capital amounts to RMB 10 million, wholly owned by Shandong Chenming Paper Holdings Limited.

黃岡晨鳴漿紙有限公司(Huanggang Chenming Paper Co., Ltd.)

The Company contributed capital to set up Huanggang Chenming Paper Co., Ltd. on 26 September 2008, its registered capital amounts to RMB 20 million, wholly owned by Shandong Chenming Paper Holdings Limited.

黃岡晨鳴林業發展有限責任公司(Huanggang Chenming Arboriculture Co., Ltd.)

The Company contributed capital to set up Huanggang Chenming Arboriculture Co., Ltd. on 23 January 2008, its registered capital amounts to RMB 10 million, wholly owned by Shandong Chenming Paper Holdings Limited.

無錫松嶺紙業有限公司(Wuxie Song Ling Paper Co., Ltd.)

富裕晨鳴紙業股份有限責任公司(Fuyu Chenming Paper Co., Ltd.), a subsidiary of the Company entered into the share transfer agreement with four natural persons of 無錫松嶺紙業有限公司 in June of 2008, according to which, 100% of equity interest of 無錫松嶺紙業有限公司 was transferred from such four natural persons to Fuyu Chenming Paper Co., Ltd.. Please refer to Note VII.58 for details of the operating results of 無錫松嶺紙業有限公司 as at the acquisition date.

壽光市潤生廢紙回收有限責任公司(Shouguang City Run Sheng Wasted Paper Recycle Co., Ltd.)

壽光晨鳴現代物流有限公司(Shouguang Chenming Modern Logistic Co., Ltd.), a subsidiary of the Company entered into the share transfer agreement with shareholders of 壽光潤生廢紙回收有限公司 on 31 October 2008, according to which, 100% of equity interest of 壽光潤生廢紙回收有限公司 was transferred at the consideration of RMB 1 million. Please refer to Note VII.58 for details of the operating results of 壽光市潤生廢紙回收有限公司 as at the acquisition date.

Note 2: Subsidiaries disposed of during the year:

襄樊晨鳴銅版紙有限責任公司(Xiangfan Chenming Copperplate Pater Co., Ltd)

Xiangfan Chenming Copperplate Pater Co., Ltd completed cancellation of business registration on 11 April 2008. The specifics of its cancellation and its operating results from the beginning of the year to the date of cancellation are set out in Note VII.59.

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VII. Notes to the financial statements

1. Cash & cash equivalents

The Group						
The Group	Closing balance			Opening balance		
	Foreign currency amount	Exchange Rate	RMB	Foreign currency amount	Exchange Rate	RMB
Cash						
RMB	—	—	1,341,632.42	—	—	2,575,501.44
USD	—	—	—	15,464.00	7.3046	112,958.33
Cash in Bank						
RMB	—	—	2,530,753,538.10	—	—	480,381,438.50
HKD	595,685.04	0.8819	525,334.64	25,388.73	0.9347	23,730.85
USD	22,155,641.87	6.8346	151,424,949.93	17,855,321.74	7.3046	130,425,983.18
EURO	365,845.82	9.6590	3,533,704.76	30,586.86	10.0319	306,844.32
Other bank balances and cash						
RMB	—	—	162,711,256.24	—	—	126,795,387.29
USD	457,629.12	6.8346	3,127,711.98	—	—	—
Total			2,853,418,128.07			740,621,843.91

As at 31 December 2008, balance of other bank balances and cash contained bank acceptance deposit of RMB86,551,105.84, letter of credit deposit of RMB62,061,946.79 and covenants of deposits of RMB 17,225,915.59.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

1. Cash & cash equivalents (continued)

The Company

The Company	Closing balance			Opening balance		
	Foreign currency amount	Exchange Rate	RMB	Foreign currency amount	Exchange Rate	RMB
Cash						
RMB	—	—	30,527.86	—	—	11,938.36
USD	—	—	—	15,464.00	7.3046	112,958.33
Cash in Bank						
RMB	—	—	2,060,669,780.07	—	—	207,482,933.56
HKD	595,685.04	0.8819	525,334.64	—	—	—
USD	2,747,651.12	6.8346	18,779,096.34	3,881,077.82	7.3046	28,349,721.04
EURO	92.71	9.6590	895.49	—	—	—
Other bank balances and cash						
RMB	—	—	62,434,105.11	—	—	112,991,173.39
Total			2,142,439,739.51			348,948,724.68

As at 31 December 2008, the balance of other bank balances and cash contained bank acceptance deposit of RMB24,919,105.11 and letter of credit deposit of RMB37,515,000.00.

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VII. Notes to the financial statements (continued)

2. Bills receivable

The Group

	Closing balance RMB	Opening balance RMB
Bank acceptance	974,009,788.24	1,676,684,054.95

As at 31 December 2008, the following portion of bills receivable has used for pledged loads:

Name of issuer	Issue date	Maturity date	Amount RMB
江陰市西城鋼鐵有限公司	2008.07.30	2009.01.30	200,000.00
重慶賽迪重工設備有限公司	2008.09.25	2009.03.25	500,000.00
哈爾濱博鑫盛華紙業有限公司	2008.10.31	2009.04.30	570,000.00
天津國美電器有限公司	2008.10.23	2009.04.23	508,705.32
汕頭市建基發展有限公司	2008.10.30	2009.04.30	900,000.00
汕頭市永江貿易有限公司	2008.10.30	2009.04.30	500,000.00
Total			3,178,705.32

As at 31 December 2008, the bank acceptance of the Group (including bank acceptance discounted with recourse) amounts RMB401,110,381.77 (31 December 2007: RMB428,227,235.41).

The Company

	Closing balance RMB	Opening balance RMB
Bank acceptance	465,681,067.32	998,809,409.00

As at 31 December 2008, the bank acceptance of the Company (including bank acceptance discounted with recourse) amounts RMB217,370,008.75 (31 December 2007: RMB 405,483,351.17)

The Group and the Company had no outstanding amount within the notes receivable due from shareholders holding 5% or more (including 5%) in the shares at the end of the year.

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VII. Notes to the financial statements (continued)

3. Accounts receivable

The Group

Aging analysis of accounts receivable is as follows:

	Closing balance				Opening balance			
	Amount	Ratio	Bad debts provision	Book value	Amount	Ratio	Bad debts provision	Book value
	RMB	(%)	RMB	RMB	RMB	(%)	RMB	RMB
Within 1 year	1,829,658,612.65	95.31	(118,450,388.95)	1,711,208,223.70	1,787,271,407.44	95.10	(172,190,525.37)	1,615,080,882.07
1 to 2 years	37,381,104.32	1.95	(10,075,170.73)	27,305,933.59	45,856,276.10	2.44	(5,554,796.50)	40,301,479.60
2 to 3 years	19,485,384.07	1.02	(5,590,192.19)	13,895,191.88	6,830,375.88	0.36	(2,192,040.71)	4,638,335.17
3 to 4 years	6,219,182.05	0.32	(6,219,182.05)	—	10,454,274.19	0.56	(10,454,274.19)	—
Over 4 years	26,893,037.29	1.40	(26,893,037.29)	—	28,914,026.07	1.54	(28,914,026.07)	—
Total	1,919,637,320.38	100.00	(167,227,971.21)	1,752,409,349.17	1,879,326,359.68	100.00	(219,305,662.84)	1,660,020,696.84

The breakdown of accounts receivable according to customer's classifications is as follows:

	Closing balance				Opening balance			
	Amount	Ratio	Bad debts provision	Book value	Amount	Ratio	Bad debts provision	Book value
	RMB	(%)	RMB	RMB	RMB	(%)	RMB	RMB
Single item with significant amount of money	1,624,743,533.96	84.64	(57,263,087.60)	1,567,480,446.36	1,582,443,231.69	84.20	(172,157,112.36)	1,410,286,119.33
Single item without significant amount of money but considered to be greater risks after arrived at by credit risk characteristics	35,390,449.48	1.84	(30,409,266.30)	4,981,183.18	38,553,985.25	2.05	(34,387,291.31)	4,166,693.94
Other items without significant amount of money	259,503,336.94	13.52	(79,555,617.31)	179,947,719.63	258,329,142.74	13.75	(12,761,259.17)	245,567,883.57
Total	1,919,637,320.38	100.00	(167,227,971.21)	1,752,409,349.17	1,879,326,359.68	100.00	(219,305,662.84)	1,660,020,696.84

The movements of the provision of the bad debts of accounts receivable see notes VII.18.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

3. Accounts receivable (continued)

The Group (continued)

As at 31 December 2008, information on single items recognized to be impaired of accounts receivable is as follows:

1. Payment for goods of RMB119,457,668.56 receivable by the Group from 佛山市順德星辰紙業有限公司(Shunde Xing shen paape Co., Ltd.) on 31 December 2007, which was under the threat of bankruptcy due to poor management; therefore, RMB88,517,668.56 were provided as bad debts in 2007 after considering its collectability. During this year, the state of affairs in 順德星辰紙業有限公司 (Shunde Xing shen paape Co., Ltd.) improved and it had repaid RMB39,718,405.84, the Company reversed corresponding amount originally provided as bad debts amounting to RMB39,718,405.84.
2. Save for designated customers who were given credit periods of over 90 days, other customers of the Group were generally given credit periods within 90 days.
3. According to past experience, receivables aged over three years are generally non-recoverable, for such portion of receivables, the Group and the Company had provided in full for bad debts. Apart from accounts receivable recognized as losses of bad debts, good subsequent repayments and other credit qualities were observed on the remaining receivables, therefore are deemed by the directors of the Company to be recoverable. As such, the Group had not provided for impairment of such overdue accounts receivable.

Top five accounts receivable is as follows:

Top five balances of accounts receivable RMB	Percentage of the total balance of accounts receivable %
214,662,074.18	11.18

At the end of the year, top five balances of accounts receivable of the Group were related to sales of paper products.

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VII. Notes to the financial statements (continued)

3. Accounts receivable (continued)

The Group (continued)

Ageing analysis of accounts receivable that were overdue but not provided for impairment:

	At the end of the year RMB	At the beginning of the year RMB
0-90 days	224,355,326.78	63,604,915.22
91-180 days	11,626,631.11	15,387,866.75
181-365 days	104,986,895.58	54,812,296.84
1-2 years	27,305,933.59	40,301,479.60
2-3 years	13,895,191.88	4,638,335.17
Total	382,169,978.94	178,744,893.58

The Company

Aging analysis of accounts receivable is as follows:

	Closing balance				Opening balance			
	Amount RMB	Ratio (%)	Bad debts Provision RMB	Book value RMB	Amount RMB	Ratio (%)	Bad debts Provision RMB	Book value RMB
Within 1 year	2,028,288,765.78	97.90	(113,715,919.27)	1,914,572,846.51	1,598,791,086.58	97.86	(153,712,615.62)	1,445,078,470.96
1 to 2 years	28,865,325.57	1.39	(9,455,622.85)	19,409,702.72	22,545,280.51	1.38	(2,254,528.05)	20,290,752.46
2 to 3 years	4,122,204.54	0.20	(824,440.91)	3,297,763.63	863,657.72	0.05	(123,292.54)	740,365.18
3 to 4 years	329,884.43	0.02	(329,884.43)	—	3,877,308.99	0.24	(3,877,308.99)	—
Over 4 years	10,275,982.13	0.49	(10,275,982.13)	—	7,603,430.23	0.47	(7,603,430.23)	—
Total	2,071,882,162.45	100.00	(134,601,849.59)	1,937,280,312.86	1,633,680,764.03	100.00	(167,571,175.43)	1,466,109,588.60

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

3. Accounts receivable (continued)

The Company (continued)

The breakdown of accounts receivable according to customer's classifications is as follows:

	Closing balance				Opening balance			
	Amount RMB	Ratio (%)	Bad debts provision RMB	Book value RMB	Amount RMB	Ratio (%)	Bad debts provision RMB	Book value RMB
Single item with significant amount of money	1,851,137,454.18	89.34	(50,850,881.28)	1,800,286,572.90	1,415,437,242.18	86.65	(150,200,716.99)	1,265,236,525.19
Single item without significant amount of money but considered to be greater risks after arrived at by credit risk characteristics	8,260,094.93	0.40	(6,855,682.91)	1,404,412.02	6,611,676.72	0.40	(6,180,656.34)	431,020.38
Other items without significant amount of money	212,484,613.34	10.26	(76,895,285.40)	135,589,327.94	211,631,845.13	12.95	(11,189,802.10)	200,442,043.03
Total	2,071,882,162.45	100.00	(134,601,849.59)	1,937,280,312.86	1,633,680,764.03	100.00	(167,571,175.43)	1,466,109,588.60

Top five accounts receivable is as follows:

Top five balances of accounts receivable RMB	Percentage of the total balance of accounts receivable %
550,097,638.72	26.55

Top five balances of accounts receivable of the Company are related to sales of paper products and sales of materials by the Company at the end of reported year.

No outstanding amount within the accounts receivable due from shareholders holding 5% or more (including 5%) in the shares of the accounts receivable of the Company and the Group.

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VII. Notes to the financial statements (continued)

4. Advance to suppliers

The Group

Aging Analysis of the advance to suppliers is as follows:

	Closing balance		Opening balance	
	Amounts RMB	Ratio (%)	Amounts RMB	Ratio (%)
Within 1 year	422,828,184.88	91.42	480,857,224.46	83.77
1 to 2 years	39,698,153.99	8.58	93,157,576.97	16.23
Total	462,526,338.87	100.00	574,014,801.43	100.00

The breakdown of advance to suppliers according to customer's classifications is as follows:

	Closing balance		Opening balance	
	Amounts RMB	Ratio (%)	Amounts RMB	Ratio (%)
Single item with significant amount of money	354,789,557.91	76.71	472,934,987.83	82.39
Other items without significant amount of money	107,736,780.96	23.29	101,079,813.60	17.61
Total	462,526,338.87	100.00	574,014,801.43	100.00

The Company

Aging analysis of the advance to suppliers is as follows:

	Closing balance		Opening balance	
	Amounts RMB	Ratio (%)	Amounts RMB	Ratio (%)
Within 1 year	414,158,895.27	94.39	265,774,588.11	94.96
1 to 2 years	24,600,467.21	5.61	14,115,794.77	5.04
Total	438,759,362.48	100.00	279,890,382.88	100.00

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

4. Advance to suppliers (continued)

The Company (continued)

The breakdown of advance to suppliers according to customer's classifications is as follows:

	Closing balance		Opening balance	
	Amounts RMB	Percentage (%)	Amounts RMB	Percentage (%)
Single item with significant amount of money	408,602,400.53	93.13	247,160,724.92	88.31
Other items without significant amount of money	30,156,961.95	6.87	32,729,657.96	11.69
Total	438,759,362.48	100.00	279,890,382.08	100.00

No outstanding amount within the advance to suppliers due from shareholders holding 5% or more (including 5%) in the shares of the Company and the Group at the end of the year.

5. Other receivables

The Group

Aging analysis of other receivables is as follows:

	Closing balance				Opening balance			
	Amounts RMB	Ratio (%)	Bad debts provision RMB	Book value RMB	Amounts RMB	Percentage (%)	Bad debts provision RMB	Book value RMB
Within 1 year	93,786,094.02	50.04	(3,872,487.84)	89,913,606.18	159,129,344.63	62.26	(2,771,058.73)	156,358,285.90
1 to 2 years	44,225,959.55	23.60	(3,729,817.78)	40,496,141.77	24,068,633.93	9.42	(3,573,370.18)	20,495,263.75
2 to 3 years	5,891,292.30	3.14	(411,427.32)	5,479,864.98	35,160,118.15	13.76	(15,850,995.69)	19,309,122.46
3 to 4 years	16,139,721.78	8.61	(16,139,721.78)	—	8,383,711.19	3.28	(8,383,711.19)	—
Over 4 years	27,392,512.33	14.61	(27,392,512.33)	—	28,825,828.19	11.28	(28,825,828.19)	—
Total	187,435,579.98	100.00	(51,545,967.05)	135,889,612.93	255,567,636.09	100.00	(59,404,963.98)	196,162,672.11

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

5. Other receivables (continued)

The Group (continued)

The breakdown of other receivables according to customer's classifications is as follows:

	Closing balance				Opening balance			
	Amounts	Ratio	Bad debts		Amounts	Ratio	Bad debts	
			provision	Book value			provision	Book value
RMB	(%)	RMB	RMB	RMB	(%)	RMB	RMB	
Single item with significant amount of money	103,576,084.49	55.26	(26,076,824.29)	77,499,260.20	166,845,002.20	65.29	(25,576,316.60)	141,268,685.60
Single item without significant amount of money but considered to be greater risks after arrived at by credit risk characteristics	32,720,842.25	17.46	(18,238,351.44)	14,482,490.81	52,450,199.27	20.52	(26,450,569.75)	25,999,629.52
Other items without significant amount of money	51,138,653.24	27.28	(7,230,791.32)	43,907,861.92	36,272,434.62	14.19	(7,378,077.63)	28,894,356.99
Total	187,435,579.98	100.00	(51,545,967.05)	135,889,612.93	255,567,636.09	100.00	(59,404,963.98)	196,162,672.11

The movements of the provision of the bad debts of other receivables see notes VII.18.

As at 31 December 2008, there were overdue debt obligations from debtors amounting to RMB13,396,091.07 which had evidence showing debtors' inability to repay and were determined to be impaired on individual basis.

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VII. Notes to the financial statements (continued)

5. Other receivables (continued)

The Group (continued)

Top five other receivables is as follows:

Top five balances of other receivables RMB	Total balance of other receivables %
64,594,338.97	34.46

At the end of the year, top five other receivables to the Group include RMB 24,077,914.40 of prepaid tax to customs, RMB13,760,216.44 of electricity fee due from its associated company 阿爾諾維根斯晨鳴特種紙有限公司 (Arjo Wiggins Chenming Specialty Paper Co., Ltd.) and advance receivables.

The Company

Aging analysis of other receivables is as follows:

	Closing balance				Opening balance			
	Amounts RMB	Ratio (%)	Bad debts provision RMB	Book value RMB	Amounts RMB	Ratio (%)	Bad debts provision RMB	Book value RMB
Within 1 year	903,553,335.31	94.58	(3,538,709.30)	900,014,626.01	722,772,013.66	91.18	(1,960,790.29)	720,811,223.37
1 to 2 years	37,815,787.23	3.96	(3,577,895.16)	34,237,892.07	47,844,292.42	6.04	(1,299,726.66)	46,544,565.76
2 to 3 years	2,474,881.24	0.26	(258,884.60)	2,215,996.64	11,022,711.25	1.39	(1,857,351.93)	9,165,359.32
3 to 4 years	2,591,793.46	0.27	(2,591,793.46)	—	2,848,382.90	0.36	(2,848,382.90)	—
Over 4 years	8,933,317.48	0.93	(8,933,317.48)	—	8,174,993.62	1.03	(8,174,993.62)	—
Total	955,369,114.72	100.00	(18,900,600.00)	936,468,514.72	792,662,393.85	100.00	(16,141,245.40)	776,521,148.45

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

5. Other receivables (continued)

The Company(continued)

The breakdown of other receivables according to customer's classifications is as follows:

	Closing balance				Opening balance			
	Amounts	Ratio	Bad debts	Book value	Amounts	Ratio	Bad debts	Book value
			provision				provision	
RMB	(%)	RMB	RMB	RMB	(%)	RMB	RMB	
Single item with significant amount of money	903,048,155.67	94.52	(6,401,477.54)	896,646,678.13	748,545,105.73	94.43	(7,099,864.57)	741,445,241.16
Single item without significant amount of money but considered to be greater risks after arrived at by credit risk characteristics	12,054,200.78	1.26	(5,680,014.20)	6,374,186.58	11,805,959.28	1.49	(6,835,422.68)	4,970,536.60
Other items without significant amount of money	40,266,758.27	4.22	(6,819,108.26)	33,447,650.01	32,311,328.84	4.08	(2,205,958.15)	30,105,370.69
Total	955,369,114.72	100.00	(18,900,600.00)	936,468,514.72	792,662,393.85	100.00	(16,141,245.40)	776,521,148.45

Top five other receivables is as follows:

Top five balances of other receivables RMB	Total balance of other receivables %
780,425,815.83	81.69

All of the top five other receivables to the Company represented short-term loans due from subsidiaries of the Company at the end of the year.

No outstanding amount within the other receivables due from shareholders holding 5% or more (including 5%) in the shares of the Company and the Group at the end of the year.

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VII. Notes to the financial statements (continued)

6. Inventories and provision of inventories

The Group

	Closing balance			Opening balance		
	Amounts	Provision of	Book value	Amounts	Provision of	Book value
		impairment			impairment	
RMB	RMB	RMB	RMB	RMB	RMB	
Raw materials	1,617,795,107.45	(38,053,661.45)	1,579,741,446.00	1,113,790,466.49	—	1,113,790,466.49
Goods-in stock	1,837,434,737.58	(92,580,212.31)	1,744,854,525.27	564,307,993.16	(6,114,277.85)	558,193,715.31
Work-in-progress	77,369,465.81	(4,172,506.70)	73,196,959.11	72,508,430.56	—	72,508,430.56
Total	3,532,599,310.84	(134,806,380.46)	3,397,792,930.38	1,750,606,890.21	(6,114,277.85)	1,744,492,612.36

Provision of inventories is as follows:

	Opening balance	Addition for the year	Reversal for the year	Closing balance
	RMB	RMB	RMB	RMB
During the year				
Raw materials	—	38,053,661.45	—	38,053,661.45
Work-in-progress	6,114,277.85	93,523,466.33	(7,057,531.87)	92,580,212.31
Goods-in stock	—	4,172,506.70	—	4,172,506.70
Total	6,114,277.85	135,749,634.48	(7,057,531.87)	134,806,380.46
In the prior year				
Goods-in stock	5,232,293.42	881,984.43	—	6,114,277.85

There was an increase in provision for impaired goods-in stock during the year, because 壽光晨鳴現代物流有限公司(Shouguang Chenming Modern Logistic Co., Ltd.), a subsidiary of the Company, acquired 潤生廢紙回收有限責任公司(Run Sheng Wasted Paper Recycle Co., Ltd.), resulting in a rise of RMB943,254.02 in provision for impaired goods-in stock.

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VII. Notes to the financial statements (continued)

6. Inventories and provision of inventories (continued)

The Company

	Closing balance			Opening balance		
	Amounts RMB	Provision of impairment RMB	Book value RMB	Amounts RMB	Provision of impairment RMB	Book value RMB
Raw materials	598,215,785.94	—	598,215,785.94	417,274,191.57	—	417,274,191.57
Goods-in stock	1,124,422,916.85	(46,500,597.16)	1,077,922,319.69	301,748,451.47	(6,114,277.85)	295,634,173.62
Work-in-progress	6,518,968.88	—	6,518,968.88	8,446,384.35	—	8,446,384.35
Total	1,729,157,671.67	(46,500,597.16)	1,682,657,074.51	727,469,027.39	(6,114,277.85)	721,354,749.54

Provision of inventories is as follows:

	Opening balance RMB	Addition for the year RMB	Reversal for the year RMB	Closing balance RMB
During the year	6,114,277.85	46,500,597.16	(6,114,277.85)	46,500,597.16
In the prior year	5,232,293.42	881,984.43	—	6,114,277.85

As at 31 December 2008, the Company and the Group have not secured any inventories for any debts.

7. Entrusted loan

The Company

	Closing balance RMB	Opening balance RMB
Entrusted loan made to subsidiaries		
– Due within in a year	982,000,000.00	1,864,000,000.00
– Due in a year later	965,000,000.00	625,000,000.00
Net value of entrusted loan	1,947,000,000.00	2,489,000,000.00

The Company entrusted banks to provide funds for its subsidiaries, the above terms of entrusted loan ranges from 1 to 10 years, and the interest rate ranges from 5.022% to 7.830%.

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VII. Notes to the financial statements (continued)

8. Other current assets

The Group

	At the end of the year RMB	At the beginning of the year RMB
Non-credited input tax amount in value added tax	124,905,083.61	—
Prepaid enterprise income tax	27,087,962.34	—
Total	151,993,045.95	—

The Company

	At the end of the year RMB	At the beginning of the year RMB
Non-credited input tax amount in value added tax	39,110,582.59	—
Prepaid enterprise income tax	13,636,622.39	—
Total	52,747,204.98	—

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

9. Long-term equity investment

The Group

(1) The details of long-term equity investments as follow:

Name of investee companies	Initial investment	opening balance	Additions for the year	Equity adjustments for the year	Cash bonus for the year	Other deductions	Closing balance
	RMB	RMB	RMB	RMB	RMB	RMB	RMB
Equity method							
阿爾諾維根斯晨鳴特種紙有限公司(Arjo Wiggins Chenming Specialty Paper Co., Ltd.)	80,100,000.00	51,022,755.23	20,100,000.00	(22,643,889.73)	—	—	48,478,865.50
壽光麗奔制紙有限公司(Shouguang Liben Paper Making Co., Ltd.)	19,550,000.00	18,867,181.20	—	(523,739.49)	—	—	18,343,441.71
青州市晨鳴變性澱粉有限公司(Qingzhou Chenming Denaturation Amylum Co., Ltd.)	540,000.00	900,000.00	—	—	—	—	900,000.00
	100,190,000.00	70,789,936.43	20,100,000.00	(23,167,629.22)	—	—	67,722,307.21
Cost method							
濰坊創業投資有限公司	1,000,000.00	1,000,000.00	—	—	—	—	1,000,000.00
泰山保險經紀有限公司	2,000,000.00	2,000,000.00	—	—	—	—	2,000,000.00
山東紙業集團總公司	200,000.00	200,000.00	—	—	—	—	200,000.00
浙江省廣育報業印務有限公司	2,000,000.00	2,000,000.00	—	—	—	—	2,000,000.00
濟南商友商務有限公司	350,000.00	350,000.00	—	—	—	—	350,000.00
上海林嘉紙電子商務有限公司	1,400,000.00	1,400,000.00	—	—	—	—	1,400,000.00
壽光灤河水務有限公司	20,000,000.00	20,000,000.00	—	—	—	—	20,000,000.00
	26,950,000.00	26,950,000.00	—	—	—	—	26,950,000.00
Total	127,140,000.00	97,739,936.43	20,100,000.00	(23,167,629.22)	—	—	94,672,307.21
Less : provision for impairment		(1,450,000.00)					(1,998,538.07)
Net amount of long-term equity investment		96,289,936.43					92,673,769.14

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

9. Long-term equity investment (continued)

The Group (continued)

The movement of provision of impairment of long-term equity investment as follows:

Name of investee companies	Opening balance RMB	Additions for the period RMB	Retirements and disposals for the period RMB	Closing balance RMB
青州市晨鳴變性澱粉有限 責任公司(Qingzhou Chenming Denaturation Amylum Co., Ltd.)	900,000.00	—	—	900,000.00
山東紙業集團總公司	200,000.00	—	—	200,000.00
濟南商友商務有限責任公司	350,000.00	—	—	350,000.00
濰坊創業投資有限公司	—	80,385.84	—	80,385.84
上海林嘉紙電子商務有限公司	—	468,152.23	—	468,152.23
Total	1,450,000.00	548,538.07	—	1,998,538.07

(2) List of the associates and their financial information

Name of investee units	Registration place	Nature of business	Registered capital RMB	Percentage of the registered capital of the investee units %	Percentage of the voting right of investee units %	Total asset of the investee units in the end of the year RMB	Total liability of the investee units in the end of the year RMB	Total operation income of the investee units in the end of the year RMB	Total net profit of the investee units in the end of the year RMB
阿爾諾維根斯晨鳴特種紙有限公司(Arjo Wiggins Chenming Specialty Paper Co., Ltd.)	Shandong	Manufacture of paper	267,368,330.00	30	30	516,138,520.15	354,542,301.82	150,408,389.01	(75,479,632.43)
壽光麗奔制紙有限公司 (Shouguang Liben Paper Making Co., Ltd.)	Shandong	Manufacture of paper	74,070,000.00	26.4	26.4	78,281,498.26	8,798,764.52	92,921,716.83	(1,983,861.71)

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

9. Long-term equity investment (continued)

The Company

(1) The details of long-term equity investments as follow:

Name of investee companies	Initial investment RMB	Opening balance RMB	Investment addition for the year RMB	Investment deduction for the year RMB	Equity adjustment for the year RMB	Closing balance RMB
Investment made to subsidiaries						
武漢晨鳴漢陽紙業股份有限公司(Wuhan Chenming Hanyang Paper Holdings Co., Ltd.)	202,824,716.34	202,824,716.34	—	—	—	202,824,716.34
山東晨鳴紙業集團齊河板紙有限公司(Shandong Chenming Paper Group Qihe Paperboard Co., Ltd.)	376,200,000.00	376,200,000.00	—	—	—	376,200,000.00
山東晨鳴熱電股份有限公司(Shandong Chenming Power Supply Holdings Co., Ltd.) (note 1)	157,810,117.43	71,434,605.00	86,375,512.43	—	—	157,810,117.43
赤壁晨鳴紙業有限公司(Chibi Chenming Paper Co., Ltd.)	26,270,460.90	26,270,460.90	—	—	—	26,270,460.90
襄樊晨鳴銅版紙有限公司(Xiangfan Chenming Copperplate Paper Co., Ltd.) (note 7)	3,552,717.43	3,552,717.43	—	(3,552,717.43)	—	—
延邊晨鳴紙業有限公司(Yanbian Chenming Paper Co., Ltd.)	40,083,733.01	40,083,733.01	—	—	—	40,083,733.01

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

9. Long-term equity investment (continued)

The Company (continued)

(1) The details of long-term equity investments as follow: (continued)

Name of investee companies	Initial investment RMB	Opening balance RMB	Investment addition for the year RMB	Investment deduction for the year RMB	Equity adjustment for the year RMB	Closing balance RMB
海拉爾晨鳴紙業有限 責任公司(Hailaer Chenming Paper Co., Ltd.)	12,000,000.00	12,000,000.00	—	—	—	12,000,000.00
江西晨鳴紙業有限 責任公司(Jiangxi Chenming Paper Co., Ltd.)	697,548,406.40	697,548,406.40	—	—	—	697,548,406.40
壽光市晨鳴天園 林業有限公司 (Shouguang Chenming Tianyuan Arboriculture Co., Ltd.)	7,199,000.00	7,199,000.00	—	—	—	7,199,000.00
吉林晨鳴紙業有限 公司(Jilin Chenming Paper Co., Ltd.) (note 2)	1,501,350,000.00	401,350,000.00	1,100,000,000.00	—	—	1,501,350,000.00
鄧城晨鳴板材有限 公司(Juancheng Chenming Panels Co., Ltd.)	15,000,000.00	15,000,000.00	—	—	—	15,000,000.00
山東禦景大酒店 有限公司 (Shandong Grand View Hotel Co., Ltd.)	80,500,000.00	80,500,000.00	—	—	—	80,500,000.00

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VII. Notes to the financial statements (continued)

9. Long-term equity investment (continued)

The Company (continued)

(1) The details of long-term equity investments as follow: (continued)

Name of investee companies	Initial investment RMB	Opening balance RMB	Investment addition for the year RMB	Investment deduction for the year RMB	Equity adjustment for the year RMB	Closing balance RMB
湛江晨鳴漿紙有限公司 (Zhanjiang Chenming Paper Pulp Co., Ltd.) (note 3)	500,000,000.00	20,000,000.00	480,000,000.00	—	—	500,000,000.00
晨鳴(香港)有限公司 (Chenming (HK) Limited)	783,310.00	783,310.00	—	—	—	783,310.00
壽光晨鳴現代物流有限公司(Shouguang Chenming Modern Logistic Co., Ltd.)	10,000,000.00	10,000,000.00	—	—	—	10,000,000.00
壽光晨鳴美術紙有限公司 (Shouguang Chenming Art Paper Co., Ltd.)	113,616,063.80	113,616,063.80	—	—	—	113,616,063.80
富裕晨鳴紙業股份有限公司(Fuyu Chenming Paper Co., Ltd.) (note 4)	208,000,000.00	20,000,000.00	188,000,000.00	—	—	208,000,000.00
咸寧晨鳴林業發展有限責任公司 (Xianning Chenming Arboriculture development Co., Ltd.) (note 5)	10,000,000.00	—	10,000,000.00	—	—	10,000,000.00
黃岡晨鳴漿紙有限公司 (Huanggang Chenming Paper Co., Ltd.) (note 5)	20,000,000.00	—	20,000,000.00	—	—	20,000,000.00
黃岡晨鳴林業發展有限責任公司(Huanggang Chenming Arboriculture Co., Ltd.) (note 5)	10,000,000.00	—	10,000,000.00	—	—	10,000,000.00
Sub-total	3,992,738,525.31	2,098,363,012.88	1,894,375,512.43	(3,552,717.43)	—	3,989,185,807.88

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

9. Long-term equity investment (continued)

The Company (continued)

(1) The details of long-term equity investments as follow: (continued)

Name of investee companies	Initial investment RMB	Opening balance RMB	Investment addition for the year RMB	Investment deduction for the year RMB	Equity adjustment for the year RMB	Closing balance RMB
Investment made to associates						
壽光麗奔制紙有限公司 (Shouguang Liben Paper Making Co., Ltd.)	19,550,000.00	18,867,181.20	—	—	(523,739.49)	18,343,441.71
阿爾諾維根斯晨鳴特種紙有限公司(Arjo Wiggins Chenming Specialty Paper Co., Ltd.) (note 6)	80,100,000.00	51,022,755.23	20,100,000.00	—	(22,643,889.73)	48,478,865.50
青州市晨鳴變性澱粉有限公司(Qingzhou Chenming Denaturation Amylum Co., Ltd.)	540,000.00	900,000.00	—	—	—	900,000.00
Sub-total	100,190,000.00	70,789,936.43	20,100,000.00	—	(23,167,629.22)	67,722,307.21
Other investments						
濰坊創業投資有限公司	1,000,000.00	1,000,000.00	—	—	—	1,000,000.00
泰山保險經紀有限公司	2,000,000.00	2,000,000.00	—	—	—	2,000,000.00
山東紙業集團總公司	200,000.00	200,000.00	—	—	—	200,000.00
浙江省廣育報業印務有限公司	2,000,000.00	2,000,000.00	—	—	—	2,000,000.00
濟南商友商務有限責任公司	350,000.00	350,000.00	—	—	—	350,000.00
壽光彌河水務有限公司	20,000,000.00	20,000,000.00	—	—	—	20,000,000.00
上海林嘉紙電子商務有限公司	1,400,000.00	1,400,000.00	—	—	—	1,400,000.00
Sub-total	26,950,000.00	26,950,000.00	—	—	—	26,950,000.00
Impairment of provision of long-term investment	—	(1,450,000.00)				(1,998,538.07)
Total	4,119,878,525.31	2,194,652,949.31				4,081,859,577.02

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

9. Long-term equity investment (continued)

The Company (continued)

(1) The details of long-term equity investments as follow: (continued)

Note 1: According to the share transfer agreement entered into between the Company and the State Assets Administration Bureau of Shouguang city and the People's Municipal Government of Shouguang city, the Company purchased 35.71% of equity interest in 山東晨鳴熱電股份有限公司 held by the State Assets Administration Bureau of Shouguang city at the consideration of RMB 86,375,512.43 in January 2008.

Note 2: The Company contributed additional capital of RMB 1,100,000,000.00 to 吉林晨鳴紙業有限公司, a wholly-owned subsidiary of the Company, on 6 August 2008.

Note 3: The Company contributed additional capital of RMB480,000,000.00 to 湛江晨鳴漿紙有限公司, a wholly-owned subsidiary of the Company, on 15 October 2008.

Note 4: The Company contributed additional capital of RMB188,000,000.00 to 富裕晨鳴紙業有限公司, a wholly-owned subsidiary of the Company, on 18 July 2008.

Note 5: During 2008, the Company contributed capital to establish 黃岡晨鳴林業發展有限公司, 黃岡晨鳴漿紙有限公司 and 咸寧晨鳴林業發展有限公司, details of which set out on annotation 1 of note 6.

Note 6: According to resolutions passed by the tenth meeting of the fifth session of the board of directors on 28 August 2008, the Company and 阿爾諾維根斯香港有限公司 contributed capital to their joint venture, 阿爾諾維根斯晨鳴特種紙有限公司, in the proportion of their shareholding. The Company contributed RMB20,100,000.00. After contribution, the shareholding of these two parties remains unchanged.

Note 7: The Company and its subsidiary, 武漢晨鳴漢陽紙業股份有限公司, disposed of their 51% equity interest in total of 襄樊晨鳴銅版紙有限公司 on 11 April 2008 (refer to annotation 2 of note 6).

(2) There is no restriction on the ability of the investee in which the long-term equity investments are held by the Group and the Company as at 31 December 2008 to transfer capital to the Group.

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VII. Notes to the financial statements (continued)

10. Investment Properties

The Group and the Company

	Building RMB
Original value	
Opening balance	38,291,395.70
Increased for the period	—
Closing balance	38,291,395.70
Accumulated depreciation	
Opening balance	8,388,415.51
Increased for the period	1,738,256.04
Closing balance	10,126,671.55
Net amount	
Opening balance	29,902,980.19
Closing balance	28,164,724.15

Properties held for investment represent part of the buildings of 北京數碼大廈(for lease out) as held by the Company.

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VII. Notes to the financial statements (continued)

11. Fixed Assets

The Group

	Buildings RMB	Machinery & Equipment RMB	Vehicles RMB	Electric appliance and others RMB	Total RMB
Cost					
Opening balance	2,834,298,999.94	14,113,557,143.84	121,248,746.36	361,881,284.67	17,430,986,174.81
Increase due to acquisition of subsidiaries	—	—	—	9,500.00	9,500.00
Decrease due to cancellation of subsidiaries	(10,928,161.61)	(18,526,210.32)	(1,088,760.00)	(1,067,421.01)	(31,610,552.94)
Additions	80,040,585.72	62,824,220.73	18,291,791.34	23,822,097.70	184,978,695.49
Transfers from construction in progress	410,303,663.81	1,388,699,791.71	7,771,938.66	132,346,169.39	1,939,121,563.57
Deductions	(11,035,531.23)	(13,132,471.04)	(9,939,019.18)	(1,213,621.06)	(35,320,642.51)
Closing balance	3,302,679,556.63	15,533,422,474.92	136,284,697.18	515,778,009.69	19,488,164,738.42
Accumulated depreciation					
Opening balance	458,971,467.09	3,461,553,778.37	52,068,227.45	207,162,373.08	4,179,755,845.99
Decrease due to cancellation of subsidiaries	(4,800,216.58)	(10,451,921.43)	(681,519.16)	(835,672.97)	(16,769,330.14)
Additions	108,187,414.79	987,242,642.41	8,883,682.16	18,984,884.71	1,123,298,624.07
Deductions	(551,806.69)	(6,993,158.22)	(4,922,625.68)	(890,567.84)	(13,358,158.43)
Closing balance	561,806,858.61	4,431,351,341.13	55,347,764.77	224,421,016.98	5,272,926,981.49
Impairment provision					
Opening balance	6,928,487.84	1,145,801.05	—	—	8,074,288.89
Decrease due to cancellation of subsidiaries	(6,928,487.84)	(7,273,746.08)	(407,240.84)	(231,748.04)	(14,841,222.80)
Increased provision	—	7,923,943.88	407,240.84	231,748.04	8,562,932.76
Reversals	—	—	—	—	—
Closing balance	—	1,795,998.85	—	—	1,795,998.85
Net value					
Opening balance	2,368,399,045.01	10,650,857,564.42	69,180,518.91	154,718,911.59	13,243,156,039.93
Closing balance	2,740,872,698.02	11,100,275,134.94	80,936,932.41	291,356,992.71	14,213,441,758.08

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VII. Notes to the financial statements (continued)

11. Fixed Assets (continued)

The Group (continued)

Note 1: International Finance Corporation (“IFC”), Deutsche Bank AG (“DEG”) and China Construction Bank Nanchang Changbei Branch entered into an loan agreement with Jiangxi Chenming Paper Co., Ltd, a subsidiary of the Company, pursuant to which, secured loans of USD 40,000,000.00, USD 9,411,765.00 and USD 17,500,000.00 were provided to Jiangxi Chenming Paper Co., Ltd by the above financial institutions respectively. The collateral was the fixed assets and land use rights of Jiangxi Chenming Paper Co., Ltd. On 31 December 2008, USD 10,918,791.23 of the above borrowed amount has been already repaid. On 31 December 2008, the net book value of the collateral with regard to fixed assets was RMB 1,144,235,273.50 and that with regard to the land use rights and intangible assets was RMB 74,653,598.66.

Note 2: At as 31 December 2008, the Group had no fixed assets held under operation lease.

Note 3: At as 31 December 2008, the net book value of the buildings without house property right certificates in the fixed assets of the Group was RMB 242,268,202.56 (2007: RMB253,656,589.82). The related house property right certificates were being applied.

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VII. Notes to the financial statements (continued)

11. Fixed Assets (continued)

The Company

	Buildings	Machinery & equipment	Vehicles	Electric appliance and others	Total
	RMB	RMB	RMB	RMB	RMB
Cost					
Opening balance	972,211,978.91	7,999,338,053.06	31,396,652.54	31,464,803.11	9,034,411,487.62
Additions	2,271,437.73	20,475,450.48	5,916,223.58	3,935,580.90	32,598,692.69
Transfers from construction in progress	40,189,947.33	279,701,782.77	870,443.00	776,711.20	321,538,884.30
Deductions	(10,287,039.97)	(6,204,169.84)	(3,359,472.00)	(631,678.48)	(20,482,360.29)
Closing balance	1,004,386,324.00	8,293,311,116.47	34,823,847.12	35,545,416.73	9,368,066,704.32
Accumulated depreciation					
Opening balance	186,778,016.25	2,258,838,541.75	14,814,444.14	18,212,612.16	2,478,643,614.30
Additions	38,865,679.27	590,859,911.77	2,859,790.96	4,279,789.67	636,865,171.67
Deductions	(353,265.02)	(3,251,517.25)	(1,976,424.29)	(479,425.62)	(6,060,632.18)
Closing balance	225,290,430.50	2,846,446,936.27	15,697,810.81	22,012,976.21	3,109,448,153.79
Net value					
Opening balance	785,433,962.66	5,740,499,511.31	16,582,208.40	13,252,190.95	6,555,767,873.32
Closing balance	779,095,893.50	5,446,864,180.20	19,126,036.31	13,532,440.52	6,258,618,550.53

Note 1: At as 31 December 2008, the Group had no fixed assets held under operation lease.

Note 2: At as 31 December 2008, the net book value of the buildings without house property right certificates in the fixed assets of the Group was RMB 4,705,794.76 (2007: RMB5,988,190.06). The related house property right certificates were being applied.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

12 Construction in progress

The Group

Items	Opening balance RMB	Additions RMB	Transfers to fixed assets during the year RMB	At the end of the year RMB	Sources of funds	Budgeted costs RMB100 million	Investment to budgeted costs %
98,000-tonne waste paper de-inking project	193,142,988.50	70,202,947.54	263,345,936.04	—	Borrowings	3.66	71.95
200,000-tonne light weight coated paper project	1,000,000.00	740,000.00	—	1,740,000.00	Self-owned funds	27.50	89.90
Grand View Hotel	181,059,912.64	78,284,956.35	259,344,868.99	—	Self-owned funds	2.30	122.57
Technological improvement to fixed asset (Jilin Chenming)	6,880,933.81	15,925,215.78	4,550,120.61	18,256,028.98	Borrowings and Self-owned funds	N/A	N/A
Zhanjiang pulp project	14,090,236.83	7,864,516.05	4,016,849.51	17,937,903.37	Borrowings and fund raised	58.22	0.31
120,000-tonne art coated paper project	218,289,301.08	564,736,044.28	783,025,345.36	—	Self-owned funds	6.70	116.87
Transform of stove dilatation and evaporation stations	—	13,010,968.26	—	13,010,968.26	Self-owned funds	0.22	59.14
Transform of de-inking with dispersing hot and recovery bleaching	—	17,885,491.14	—	17,885,491.14	Self-owned funds	0.15	119.24
Transform project of desulphurization for coal powder stoves of power plants	—	13,646,962.99	—	13,646,962.99	Self-owned funds	0.15	90.98
Handling of middle level of water by draining workshops	—	35,159,901.70	—	35,159,901.70	Self-owned funds	0.39	90.87
Rubbish incineration stove project	162,055.01	91,537,493.67	—	91,699,548.68	Borrowings and Self-owned funds	0.87	104.86
Pulp board machine project	—	30,973,725.01	—	30,973,725.01	Self-owned funds	1.20	25.81
Technological improvement to paper machine project	—	32,808,843.00	—	32,808,843.00	Self-owned funds	0.32	102.21
Others	290,128,206.15	492,970,136.28	624,838,443.06	158,259,899.37	Self-owned funds	N/A	N/A
Total construction in progress	904,753,634.02	1,465,747,202.05	1,939,121,563.57	431,379,272.50			
Including: capitalized borrowing expenses from capitalization	1,794,383.80	24,043,281.70	24,051,702.20	1,785,963.30			
Net construction in progress	904,753,634.02	1,465,747,202.05	1,939,121,563.57	431,379,272.50			

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VII. Notes to the financial statements (continued)

12 Construction in progress

The Group (continued)

As at 31 December 2008, closing balance of construction in progress of the Group included RMB1,785,963.30 of interest capitalized. Borrowing expense from capitalization for the year included RMB24,043,281.70 (the prior year: RMB30,470,011.03). The capitalizing rate to determine the general borrowing capitalized was 6.72% (the prior year: 6.14%).

The Company

Items	Opening balance RMB	Additions RMB	Transfers to fixed assets during the year RMB	Closing balance RMB	Sources of funds	Budgeted costs RMB100 million	Investment to budgeted costs %
98,000-tonne waste paper de-inking project	193,142,988.50	70,202,947.54	263,345,936.04	—	Borrowings	3.66	71.95
Others	82,208,320.28	35,773,519.24	58,192,948.26	59,788,891.26	Self-owned funds	N/A	N/A
Total	275,351,308.78	105,976,466.78	321,538,884.30	59,788,891.26			

As at 31 December 2008, closing balance of construction in progress of the Company did not include interest capitalized (interest capitalized for the prior year: RMB11,879,372.75; the capitalizing rate was 6.07%).

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VII. Notes to the financial statements (continued)

13. Intangible assets

The Group

	Land use rights RMB	Software RMB	Total RMB
Cost			
Opening balance	895,170,184.86	14,818,173.05	909,988,357.91
Additions	483,136,480.78	297,450.00	483,433,930.78
Deductions	(3,874,161.38)	—	(3,874,161.38)
Closing balance	1,374,432,504.26	15,115,623.05	1,389,548,127.31
Accumulated depreciation			
Opening balance	83,609,773.41	4,076,758.18	87,686,531.59
Additions	23,258,233.54	1,526,773.65	24,785,007.19
Closing balance	106,868,006.95	5,603,531.83	112,471,538.78
Net value			
Opening balance	811,560,411.45	10,741,414.87	822,301,826.32
Closing balance	1,267,564,497.31	9,512,091.22	1,277,076,588.53

Note 1: For the details of intangible assets—land use rights as collateral, please refer to notes VII.11.

Note 2: As at 31 December 2008, the net book value of the buildings without house property right certificates in the intangible assets of the Group was RMB 147,502,707.53 (2007: RMB92,098,697.68). The related house property right certificates were being applied.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

13. Intangible assets (continued)

The Company

	Land use rights RMB	Software RMB	Total RMB
Cost			
Opening balance	390,308,640.44	14,787,993.05	405,096,633.49
Additions	553,275.00	—	553,275.00
Deductions	(3,874,161.38)	—	(3,874,161.38)
Closing balance	386,987,754.06	14,787,993.05	401,775,747.11
Accumulated depreciation			
Opening balance	24,006,955.48	4,066,698.18	28,073,653.66
Additions	7,713,897.10	1,478,799.36	9,192,696.46
Closing balance	31,720,852.58	5,545,497.54	37,266,350.12
Net value			
Opening balance	366,301,684.96	10,721,294.87	377,022,979.83
Closing balance	355,266,901.48	9,242,495.51	364,509,396.99

Note 1: As at 31 December 2008, the net book value of the buildings without house property right certificates in the intangible assets of the Company was RMB 87,510,874.22 (2007: RMB92,098,697.68). The related house property right certificates were being applied.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

14. Goodwill

The Group

	Accumulated for this year RMB	Accumulated for last year RMB
Cost	20,283,787.17	20,283,787.17
Opening balance		
Closing balance	20,283,787.17	20,283,787.17
Accumulated impaired loss	—	—
Book value		
Opening balance	20,283,787.17	20,283,787.17
Closing balance	20,283,787.17	20,283,787.17

Goodwill of the Group arose from the acquisition of minority interests in prior year by a subsidiary of the Company.

On balance sheet date, management of the Group assesses the recoverable amount of cash-generating unit which results goodwill, in order to determine whether to make provision for impairment loss accordingly. The recoverable amount of cash-generating unit is determined based on the estimated cash flow in financial budget of five years in the future by management, relying on the expected annual growth rate in GNP and the expected and steady annual growth rate in the industry by market players to calculate. Management of the Group expects no provision for impairment loss is necessary to be made for goodwill during the reporting period.

15. Long term expenses to be amortized

The Group

	Closing Balance RMB	Opening balance RMB
Transforming expense on fixed assets		
held under operation lease	37,227,730.36	41,516,344.21
Equipment leasing expense	—	14,996,890.54
Total	37,227,730.36	56,513,234.75

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

16. Deferred income tax assets

The Group

Items	Deductible temporary difference and deductible loss		Deferred income tax assets	
	Closing balance	Opening balance	Closing balance	Opening balance
	RMB	RMB	RMB	RMB
Impairment provision	355,721,066.79	294,491,403.56	73,033,025.79	76,061,834.86
Prepaid salaries of senior management	105,199,345.76	76,615,517.52	22,754,863.62	18,278,879.38
Deductible tax loss	44,187,567.66	7,072,653.00	11,046,891.91	1,768,163.25
Unpaid payables	46,165,858.44	9,467,054.69	10,870,385.92	2,366,763.67
Preliminary expenses	9,423,741.50	15,375,578.23	1,177,967.69	1,177,967.69
Unrealized profit arising from intra-group transactions	2,043,549.51	14,831,852.54	510,887.38	3,707,963.13
Deferred income	44,248,375.23	—	8,522,343.81	—
Total	606,989,504.89	417,854,059.54	127,916,366.12	103,361,571.98

According to the prediction result of future profit of the Company, it is very likely that the Company will generate sufficient taxable credit to set off deductible temporary difference and recognize the relevant deferred income tax to the extent of deductible loss.

Deductible loss of unrecognized deferred income tax will expire by the following periods:

	Closing Balance	Opening balance
	RMB	RMB
2009	978,280.51	978,280.51
2010	45,659,451.85	45,659,451.85
2011	12,921,487.95	59,596,156.75
2012	60,209,847.95	60,209,847.95
2013	52,264,974.70	—
Total	172,034,042.96	166,443,737.06

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

16. Deferred income tax assets (continued)

The Company

Items	Deductible temporary difference and deductible loss		Deferred income tax assets	
	Closing balance	Opening balance	Closing balance	Opening balance
	RMB	RMB	RMB	RMB
Impairment provision	202,143,794.82	191,418,908.68	50,835,948.71	53,645,227.74
Prepaid salaries of senior management	69,343,461.44	67,424,634.80	17,335,865.36	16,856,158.70
Unpaid payables	36,198,088.68	8,060,172.84	9,049,522.17	2,015,043.21
Deferred income	5,537,541.95	—	1,384,385.49	—
Total	313,222,886.89	266,903,716.32	78,605,721.73	72,516,429.65

17. Consumable biological assets

The Group

Item	Amount (000'mu)	Closing balance RMB	Purchase RMB	Breeding costs RMB	Change in fair value RMB	Disposal RMB	Fair Value at the end of the year RMB
Trees	335	92,159,871.29	95,238,808.73	113,091,127.38	918,451.60	(195,567.86)	301,212,691.14

On 31 December 2008, consumable biological assets held by Yangjiang Chenming Forestry Development Co., Ltd., Zhanjiang Chenming Forestry Development Co., Ltd. and Huanggang Chenming Arboriculture Co., Ltd., subsidiaries of the Company, were assessed to be RMB 301,212,691.14 in fair value by Jones Lang LaSalle Sallmanns Limited.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

18. Provision for impairment of assets

The Group

	Opening balance RMB	Charged during the year RMB	Reversals RMB	Other write-offs RMB	Closing balance RMB
Provisions for bad debts	278,710,626.82	25,330,768.69	(69,065,753.24)	(16,201,704.01)	218,773,938.26
Of which: trade receivables	219,305,662.84	15,072,005.89	(56,577,200.37)	(10,572,497.15)	167,227,971.21
other receivables	59,404,963.98	10,258,762.80	(12,488,552.87)	(5,629,206.86)	51,545,967.05
Provisions for inventory impairment	6,114,277.85	135,749,634.48	(7,057,531.87)	—	134,806,380.46
Impairment provisions for long-term equity investments	1,450,000.00	548,538.07	—	—	1,998,538.07
Impairment provisions for held-fo-maturity investments	142,210.00	—	—	—	142,210.00
Impairment provisions for fixed assets	8,074,288.89	8,562,932.76	—	(14,841,227.80)	1,795,998.85
Total	294,491,403.56	170,191,874.00	(76,123,285.11)	(31,042,926.81)	357,517,065.64

The Company

	Opening balance RMB	Charged during the year RMB	Reversals RMB	Other write-offs RMB	Closing balance RMB
Provisions for bad debts	183,712,420.83	17,963,503.38	(46,965,890.17)	(1,207,584.45)	153,502,449.59
Of which: trade receivables	167,571,175.43	8,752,403.53	(40,915,575.33)	(806,154.04)	134,601,849.59
Other receivables	16,141,245.40	9,211,099.85	(6,050,314.84)	(401,430.41)	18,900,600.00
Provisions for inventory impairment	6,114,277.85	46,500,597.16	(6,114,277.85)	—	46,500,597.16
Impairment provisions for long-term equity investments	1,450,000.00	548,538.07	—	—	1,998,538.07
Impairment provisions for held-fo-maturity investments	142,210.00	—	—	—	142,210.00
Total	191,418,908.68	65,012,638.61	(53,080,168.02)	(1,207,584.45)	202,143,794.82

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

19. Short-term borrowings

The Group

	Closing balance RMB	Opening balance RMB
Credit loans	1,055,569,455.58	3,045,252,736.25
Charged borrowings (Note 1)	57,086,500.00	120,520,085.62
Secured bill borrowings	3,178,705.32	—
Discounted bills	401,110,381.77	428,227,235.41
Total	1,516,945,042.67	3,594,000,057.28

Note 1: Charged borrowings were guarantees provided by the Company to its subsidiaries for their long-term and short-term borrowings. For details please see Note VIII.(3)(e).

Note 2: For types and amounts of secured assets under secured borrowings, please see Note VII.2.

The Company

	Closing balance RMB	Opening balance RMB
Credit loans	926,698,296.93	2,944,937,040.00
Discounted bills	217,370,008.75	405,483,351.17
Total	1,144,068,305.68	3,350,420,391.17

As at 31 December 2008, none of the short-term borrowings of the Group and the Company were overdue.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

20. Financial liabilities held for trading (assets)

The Group	Closing balance RMB	Opening balance RMB
Financial liabilities held for trading – future pooling foreign exchange contracts	198,900.00	(5,955,480.00)

21. Bills payable

The Group	At the end of the year RMB	At the beginning of the year RMB
Bank acceptance	367,627,562.14	130,056,316.74

The Company	At the end of the year RMB	At the beginning of the year RMB
Bank acceptance	210,151,045.59	121,487,222.14

As at 31 December 2008, the balance of the bills payable of the Group and the Company was not due to any shareholders holding over 5% (5% inclusive) of the Company's shares.

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VII. Notes to the financial statements (continued)

22. Accounts payable

The Group

	Closing balance		Opening balance	
	Amount RMB	Percentage (%)	Amount RMB	Percentage (%)
Within 1 year	2,493,702,616.41	94.38	1,528,958,398.71	92.29
1-2 years	98,420,284.82	3.72	79,536,914.07	4.80
2-3 years	17,647,797.85	0.67	24,233,413.86	1.46
Over 3 years	32,537,486.82	1.23	23,978,253.98	1.45
Total	2,642,308,185.90	100.00	1,656,706,980.62	100.00

The Company

	Closing balance		Opening balance	
	Amount RMB	Percentage (%)	Amount RMB	Percentage (%)
Within 1 year	1,675,493,370.59	97.64	1,297,738,134.18	97.39
1-2 years	17,223,583.36	1.00	17,432,596.61	1.31
2-3 years	7,450,362.04	0.43	5,704,136.35	0.43
Over 3 years	15,864,479.18	0.93	11,677,464.56	0.87
Total	1,716,031,795.17	100.00	1,332,552,331.70	100.00

At the end of the year, the balance of the accounts payable of the Group and the Company was not due to any shareholders holding over 5% (5% inclusive) of the Company's shares.

As at 31 December 2008, the accounts payable of the Group and the Company aged over three years were insignificant. There was no significant payable amounts aged over three years.

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VII. Notes to the financial statements (continued)

23. Advance receipts

The Group

	Closing balance		Opening balance	
	Amount	Percentage	Amount	Percentage
	RMB	(%)	RMB	(%)
Within 1 year	97,372,384.90	95.75	162,869,863.04	95.64
Over 1 year	4,321,193.67	4.25	7,416,766.17	4.36
Total	101,693,578.57	100.00	170,286,629.21	100.00

The Company

	Closing balance		Opening balance	
	Amount	Percentage	Amount	Percentage
	RMB	(%)	RMB	(%)
Within 1 year	65,671,850.62	99.47	85,788,060.04	93.12
Over 1 year	347,607.25	0.53	6,338,827.45	6.88
Total	66,019,457.87	100.00	92,126,887.49	100.00

At the end of the year, the advance receipts of the Group and the Company were not received from any shareholders holding over 5% (5% inclusive) of the Company's shares.

At the end of the year, the advance receipts of the Group and the Company aged over one year were insignificant. There were no significant advance receipts aged over one year.

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VII. Notes to the financial statements (continued)

24. Employee benefits payable

The Group

	Opening balance	Accrued during	Paid during	Closing balance
	RMB	the year	the year	RMB
		RMB	RMB	
Salaries, bonuses, allowance and subsidies	160,642,783.28	474,224,694.93	(517,879,300.80)	116,988,177.41
Staff welfare	7,030,517.94	48,215,018.01	(53,382,767.67)	1,862,768.28
Social insurance premiums	18,729,763.49	91,186,891.83	(90,192,838.33)	19,723,816.99
Of which:				
1. Medical insurance premium	12,006,319.21	22,669,324.25	(22,295,488.06)	12,380,155.40
2. Pension insurance premium	4,030,183.45	58,229,302.01	(57,430,804.73)	4,828,680.73
3. Unemployment insurance premium	439,015.11	5,148,233.20	(5,346,073.93)	241,174.38
4. Work-related injury insurance premium	40.00	3,319,144.41	(3,303,120.38)	16,064.03
5. Maternity insurance premium	2,254,205.72	1,820,887.96	(1,817,351.23)	2,257,742.45
Housing provident funds	7,411,830.96	24,894,958.05	(21,002,683.84)	11,304,105.17
Union operation costs and employee education costs	20,968,998.24	13,342,382.84	(13,663,716.42)	20,647,664.66
Others	20,096,325.15	39,707.32	(453,497.85)	19,682,534.62
Of which: housing subsidies for Chinese employees	18,722,869.49	—	—	18,722,869.49
Total	234,880,219.06	651,903,652.98	(696,574,804.91)	190,209,067.13

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

24. Employee benefits payable (continued)

The Company

	Opening balance	Accrued during	Paid during	Closing balance
	RMB	the year	the year	RMB
		RMB	RMB	
Salaries, bonuses, allowance and subsidies	91,012,875.58	189,392,636.51	(209,420,321.50)	70,985,190.59
Staff welfare	—	23,270,441.85	(23,270,441.85)	—
Social insurance premiums	—	27,261,544.01	(27,261,544.01)	—
Of which:				
1. Medical insurance premium	—	6,136,716.95	(6,136,716.95)	—
2. Pension insurance premium	—	17,535,401.89	(17,535,401.89)	—
3. Unemployment insurance premium	—	1,563,732.06	(1,563,732.06)	—
4. Work-related injury insurance premium	—	1,149,676.18	(1,149,676.18)	—
5. Maternity insurance premium	—	876,016.93	(876,016.93)	—
Housing provident funds	301,429.93	8,184,585.51	(7,147,884.60)	1,338,130.84
Union operation costs and employee education costs	7,615,692.55	4,290,309.02	(4,063,832.89)	7,842,168.68
Others	20,294,434.36	—	(1,571,564.87)	18,722,869.49
Of which: housing subsidies for Chinese employees	18,722,869.49	—	—	18,722,869.49
Total	119,224,432.42	252,399,516.90	(272,735,589.72)	98,888,359.60

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

25. Tax payables

The Group

	Closing balance RMB	Opening balance RMB
Value added tax	10,700,714.79	(37,746,067.23)
Business tax	8,328,952.19	8,857,642.18
Urban maintenance and construction tax	310,202.69	603,652.91
Corporate income tax	9,374,319.26	95,828,694.44
Individual income tax	663,205.18	9,884,850.76
Property tax	4,889,784.09	4,235,238.17
Stamp duty	4,259,535.24	3,377,040.15
Land use tax	10,025,255.88	12,020,128.08
Land appreciation tax	—	4,286,153.00
Educational surcharges and others	1,414,013.02	1,097,118.40
Total	49,965,982.34	102,444,450.86

The Company

	Closing balance RMB	Opening balance RMB
Value added tax	—	10,924,722.22
Business tax	7,376,897.19	8,695,193.52
Corporate income tax	—	63,493,393.03
Individual income tax	415,724.04	9,111,505.66
Property tax	1,797,106.29	1,750,586.84
Stamp duty	2,834,609.11	1,889,696.53
Land use tax	3,731,843.88	4,286,153.00
Total	16,156,180.51	100,151,250.80

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VII. Notes to the financial statements (continued)

26. Dividends payable

The Group and The Company

	Closing balance RMB	Opening balance RMB
Legal person shares	36,089.31	36,075.17

27. Other payables

The Group

	Closing balance		Opening balance	
	Amount RMB	Percentage (%)	Amount RMB	Percentage (%)
Within 1 year	205,978,354.37	59.49	107,189,167.02	35.14
1-2 years	23,880,416.86	6.90	121,510,348.87	39.83
2-3years	80,003,356.68	23.11	40,351,763.92	13.23
Over 3 years	36,364,114.15	10.50	35,998,736.57	11.80
Total	346,226,242.06	100.00	305,050,016.38	100.00

The Company

	Closing balance		Opening balance	
	Amount RMB	Percentage (%)	Amount RMB	Percentage (%)
Within 1 year	151,374,567.79	53.47	116,758,545.18	41.87
1-2 years	27,036,339.92	9.55	146,015,185.86	52.37
2-3years	91,357,173.17	32.27	9,606,328.08	3.45
Over 3 years	13,331,160.98	4.71	6,458,285.54	2.31
Total	283,099,241.86	100.00	278,838,344.66	100.00

The other payables of the Group and the Company at the end of the year were not due to any shareholders who holding over 5% (5% inclusive) of the Company's shares.

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VII. Notes to the financial statements (continued)

28. Non-current liabilities due within one year

The Group

Type	Closing balance RMB	Opening balance RMB
Long-term borrowings due within one year	1,038,125,240.62	667,746,417.91

The Company

Type	Closing balance RMB	Opening balance RMB
Long-term borrowings due within one year	883,602,600.00	586,144,500.00

29. Short-term debentures payable

The Group

Type	Closing balance RMB	Opening balance RMB
Short-term debentures	1,941,874,444.43	506,212,916.67

The Company

Type	Closing balance RMB	Opening balance RMB
Short-term debentures	1,941,874,444.43	—

The Company was approved, by a circular issued by the People's Bank of China (Yinfa [2007] No.427), to issue short-term debentures maturing in one year with aggregated par values of RMB700,000,000.00 and RMB1,200,000,000.00 on 10 June 2008 and 29 August 2008 respectively. The debentures are unsecured, bearing interest rate of 5.20% per annum and repayable on maturity with one-off interest payment.

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VII. Notes to the financial statements (continued)

30. Long-term borrowings

The Group

Type	Closing balance		Opening balance		RMB	RMB
	Amounts in original currency	Exchange rate on translation	Amount in original currency	Exchange rate on translation		
Credit loans – RMB	3,120,692,035.94	1.0000	3,120,692,035.94	1,436,896,605.93	1.0000	1,436,896,605.93
Credit loans – USD	121,000,000.00	6.8346	826,986,600.00	280,500,000.00	7.3046	2,048,940,300.00
Secured borrowings – USD	55,992,973.77	6.8346	382,689,578.54	62,398,977.95	7.3046	455,799,574.33
Charged borrowings – RMB (Note 1)	715,047,300.00	1.0000	715,047,300.00	775,000,000.00	1.0000	775,000,000.00
Charged borrowings – USD (Note 1)	1,750,000.00	6.8346	11,960,550.00	1,000,000.00	7.3046	7,304,600.00
Total			5,057,376,064.48			4,723,941,080.26
Less: long-term borrowings						
due within one year			1,038,125,240.62			667,746,417.91
Including: Credit loans – RMB	330,000,000.00	1.0000	330,000,000.00	166,204,570.00	1.0000	166,204,570.00
Credit loans – USD	81,000,000.00	6.8346	553,602,600.00	57,500,000.00	7.3046	420,014,500.00
Secured borrowings						
– USD	12,359,953.86	6.8346	84,475,340.62	6,369,595.58	7.3046	46,527,347.91
Charged borrowings						
– RMB	70,047,300.00	1.0000	70,047,300.00	35,000,000.00	1.0000	35,000,000.00
Long-term borrowings due after one year			4,019,250,823.86			4,056,194,662.35

The above borrowings have maturities between 2009 and 2023, include floating-rate and fixed-rate borrowings at interest rates ranging from 5.32% to 7.70% per annum.

Note 1: Guarantees provided by the Company to its subsidiaries, for specific amounts please see Note VIII.(3)(e).

Note 2: For types and amounts of secured assets under secured borrowings, please see Note VII.11.

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VII. Notes to the financial statements (continued)

30. Long-term borrowings (continued)

The Company

Type	Closing balance		RMB	Opening balance		RMB
	Amounts in original currency	Exchange rate on translation		Amounts in original currency	Exchange rate on translation	
Credit loans – RMB	3,120,692,035.94	1.0000	3,120,692,035.94	1,436,822,035.94	1.0000	1,436,822,035.94
Credit loans – USD	121,000,000.00	6.8346	826,986,600.00	280,500,000.00	7.3046	2,048,940,300.00
Total			3,947,678,635.94			3,485,762,335.94
Less: long-term borrowings due within one year			883,602,600.00			586,144,500.00
Including: Credit loans – RMB	330,000,000.00	1.0000	330,000,000.00	166,130,000.00	1.0000	166,130,000.00
Credit loans – USD	81,000,000.00	6.8346	553,602,600.00	57,500,000.00	7.3046	420,014,500.00
Long-term borrowings due after one year			3,064,076,035.94			2,899,617,835.94

The above borrowings have maturities between 2009 and 2013, include floating-rate and fixed-rate borrowings at interest rates ranging from 5.32% to 6.71% per annum.

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VII. Notes to the financial statements (continued)

31. Deferred income

The Group

Type	Opening balance RMB	Increase for the year RMB	Decrease for the year RMB	Closing balance RMB
Funds for three projects in connection with technology allocated by the local financial authority	80,000.00	—	—	80,000.00
Special subsidy funds for environmental protection (1)	750,000.00	12,890,000.00	223,500.00	13,416,500.00
Project fund for National technological support scheme (2)	—	1,790,900.00	59,696.67	1,731,203.33
Special subsidy fund for Songhuajiang environmental protection project (3)	—	32,350,000.00	1,497,916.72	30,852,083.28
Modification of alkaline recycling system (4)	—	1,500,000.00	43,750.00	1,456,250.00
Atmospheric pollution prevention and treatment subsidy fund (5)	—	1,000,000.00	—	1,000,000.00
Sewage treatment and water conservation reconfiguration project (6)	—	4,700,000.00	—	4,700,000.00
Financial grants for technological modification project (7)	—	2,000,000.00	—	2,000,000.00
Others	—	1,592,338.62	—	1,592,338.62
Total	830,000.00	57,823,238.62	1,824,863.39	56,828,375.23

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VII. Notes to the financial statements (continued)

31. Deferred income (continued)

The Company

Type	Opening balance RMB	Increase for the year RMB	Decrease for the year RMB	Closing balance RMB
Special subsidy funds for environmental protection	—	2,760,000.00	46,000.00	2,714,000.00
Project fund for National technological support scheme	—	1,790,900.00	59,696.67	1,731,203.33
Others	—	1,092,338.62	—	1,092,338.62
Total	—	5,643,238.62	105,696.67	5,537,541.95

- (1) Pursuant to the “Notice Regarding Budget for Distribution of the 2007 Environmental Protection Special Subsidy Funds Issued by the Environmental Protection Bureau of Nanchang City” (《南昌市環境保護局關於下達2007年環境保護專項資金預算的通知》), subsidiary of the Company Jiangxi Chenming Paper Co., Ltd. received special environmental protection subsidy fund of RMB5,000,000.00 in 2008, which was granted primarily for the construction work of mud burning facilities. Pursuant to the “Notice Regarding Distribution of 2008 Municipal Industrial Energy Conservation Special Subsidy Fund (First Batch)” (《關於下達2008年市工業節能專項資金計劃(第一批)的通知》) issued by the Financial Bureau of Wuhan City and the Economic Committee of Wuhan City, and pursuant to the “Notice Regarding Budget Indicators for Distribution of 2007 Energy Conservation and Technological Modification Financial Incentive Funds” (《關於下達2007年節能技術改造財政獎勵資金預算指標的通知》) issued by the Financial Department of Hubei Province, subsidiary of the Company Wuhan Chenming Hanyang Paper Co. Ltd. received special subsidy fund of RMB5,130,000.00 in 2008 for energy conservation and technological modification. Pursuant to Shou Cai Yu Zhi Zi No. [2008] Document 254 (壽財預指字[2008]第254號文) issued by the People’s Government of Shouguang City, the Company received financial incentive fund of RMB2,760,000.00 in 2008 with respect to its energy conservation and technological modification.
- (2) Pursuant to the “Notice Regarding Budget Indicators for Distribution of 2007 National Technological Support Scheme Project Funds (Second Batch)” (《關於下達2007年度國家科技支撐計劃課題(第二批)預算指標的通知》) issued by the Financial Department of Shandong Province and the Science and Technology Department of Shandong Province, the Company received the 2007 National technological support scheme project fund of RMB1,790,000.00 in 2008. The accounts payable of such project were used mainly for the pulping project that uses mixed wide leaves for bleaching in a chemi-thermomechanical pulping process and used for the studies of critical technologies.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

31. Deferred income (continued)

The Company (continued)

- (3) Pursuant to the “Notice Regarding the Distribution of the 6th Batch of 2007 Energy Conservation and Environmental Protection Project Funds in Line with the Investment Plans of the Central Government Budget Issued by the National Development and Reform Commission” (《國家發改委轉國家發展改革委關於下達2007年第六批資源節約和環境保護項目中央預算內投資計劃的通知》), subsidiary of the Company Jilin Chenming Paper Co., Ltd. Received a special subsidy fund of RMB24,100,000.00 in 2008. Pursuant to the “Notice Regarding Distribution of First Batch of 2007 Energy Conservation and Environmental Protection Project Funds (Songhuajiang Stream Industrial Pollution Treatment Project 2007 First Batch) in Line with the Investment Plan of the Central Government Issued by Development and Reform Commission of Qiqihaer” (《齊齊哈爾市發展和改革委員會關於下達2007年第一批資源節約和環境保護項目(松花江流域工業污染治理項目2007年第一批)中央預算內投資計劃的通知》), subsidiary of the Company Fuyu Chenming Paper Co., Ltd. Received a special subsidy fund of RMB6,500,000.00 in 2008. Pursuant to the “Notice Regarding Budget for Distribution of 2007 Central Government Special Subsidy Funds for Water Pollution Prevention and Treatment in Songhuajiang Stream” (《關於下達2007年松花江流域水污染防治中央專項資金支出預算的通知》) issued by the Financial Department of Jilin Province, subsidiary of the Company Jilin Chenming Paper Co., Ltd. received special subsidy fund of RMB1,750,000.00 in 2008. According to the above relevant documents, the aforementioned funds were used by the Group in the sewage treatment and processing work of Songhuajiang.
- (4) Pursuant to the “Notice Regarding the Plan for Distribution of First Batch of 2008 Environmental Protection Special Subsidy Fund” (《關於下達二零零八年第一批環保專項資金使用計劃的通知》) issued by the Environmental Protection Bureau of Jilin City and Financial Bureau of Jilin City, subsidiary of the Company Jilin Chenming Paper Co., Ltd. received special subsidy fund of RMB1,500,000.00. Such fund was used for the modification of alkaline recycling system.
- (5) Pursuant to “Supplementary Document for Atmospheric Pollution Prevention and Treatment Subsidy Fund” (《大氣污染防治補助資金補貼文件》) issued by the Financial Bureau of Qihe, subsidiary of the Company Shandong Chenming Paper Group Qihe Paperboard Co., Ltd. received special subsidy fund of RMB1,000,000.00 in 2008. Such fund was mainly used for desulphurization work in flue gas.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

31. Deferred income (continued)

The Company (continued)

- (6) Pursuant to the “Notice Regarding Redistribution of 2008 Infrastructure Expenses Budget (Major Recycle Economy and Resources Saving Demonstration Project) under Budget of Central Government” (《關於轉發2008年中央預算內基本建設支出預算(椒環經濟和資源節約重大示範項目)的通知》) issued by Financial Bureau of Yanbian Korean Autonomous Prefecture and the “Notice Regarding Distribution of Third Batch of 2008 Environmental Protection Special Subsidy Fund” issued by the Financial Department of Jilin Province and the Environmental Protection Bureau of Jilin Province, subsidiary of the Company Yanbian Chenming Paper Co. Ltd. received special subsidy grant of RMB4,700,000.00 in 2008. Such fund was primarily used in construction of major demonstration structure for recycle economy and resources conservation.
- (7) Pursuant to the “Notice Regarding Distribution of 2008 Interest Discount Subsidy Fund Project Concerning Citywide Major Industrial Reconfiguration” (《關於下達2008年全市工業重大技術改造項目貼息補助資金計劃的通知》) issued by the Economic Committee of Wuhan City and the Financial Bureau of Wuhan City, subsidiary of the Company Wuhan Chenming Hanyang Paper Co. Ltd. received interest discount financial subsidy of RMB2,000,000.00 in 2008 with respect to technological reconfiguration.

32. Deferred income tax liabilities

The Group

Temporary difference	Taxable temporary difference		Deferred income tax liabilities	
	Closing balance	Opening balance	Closing balance	Opening balance
	RMB	RMB	RMB	RMB
Changes in fair value of consumable biological assets	25,726,183.52	24,415,400.32	6,431,545.79	6,103,850.08

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

33. Share capital

The registered and paid-in share capital of the Company of RMB1 each amounted to RMB2,062,045,941.00 in total. The types and structure of shares are as follows:

a. Changes of shareholdings of the Company during 2008:

	Opening balance (share)	Increase / decrease during the period (share)					Sub-total	Closing balance (share)
		New issue (Note 1)	Lock-up of shareholdings of directors	Expiry of lock-up	Share reform	Others		
Restricted shares outstanding								
State-owned legal person shares	328,573,657	—	—	—	—	(35,570,000)	(35,570,000)	293,003,657
Other domestic shares	10,926,796	—	176,774	(120,101)	—	—	56,673	10,983,469
Including:								
Domestic legal-person shares	—	—	—	—	—	—	—	—
Domestic natural person shares	10,926,796	—	176,774	(120,101)	—	—	56,673	10,983,469
Total number of restricted shares outstanding	339,500,453	—	176,774	(120,101)	—	(35,570,000)	(35,513,327)	303,987,126
Listed tradable shares								
RMB ordinary shares	809,348,003	—	(176,774)	120,101	—	—	(56,673)	809,291,330
Domestic listed foreign shares (B share)	557,497,485	—	—	—	—	—	—	557,497,485
Overseas listed foreign shares (H share)	—	355,700,000	—	—	—	35,570,000	391,270,000	391,270,000
Total listed tradable shares	1,366,845,488	355,700,000	(176,774)	120,101	—	35,570,000	391,213,327	1,758,058,815
Total shares	1,706,345,941	355,700,000	—	—	—	—	355,700,000	2,062,045,941

Note 1: As approved by the Stock Exchanges of Hong Kong Limited, the Company publicly offered 355,700,000 H shares in June 2008.

Note 2: The shares transferred to the NSSF Council and converted into 35,570,000 overseas listed foreign shares (H shares) in connection with the reduction of holdings in state-owned shares by the relevant holders of state-owned shares of the Company.

Increase in share capital in connection with the issuance of new shares mentioned above was reviewed by China Rightson Certified Public Accountants. A capital review report Zhong Rui Yue Hua Yan Zi No. [2008] 2189 (中瑞岳華驗字[2008]第2189號) was published for the certification of the review.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

33. Share capital (continued)

b. Changes of shareholdings of the Company during 2007:

	Opening balance (share)	Increase / decrease during the period (share)						Closing balance (share)
		Conversion from convertible bonds (Note 1)	Lock-up of new shareholdings of directors	Expiry of lock-up	Share reform	Others	Sub-total	
Restricted shares outstanding								
State-owned legal								
person shares	328,573,657	—	—	—	—	—	—	328,573,657
Domestic non-state-owned								
legal person shares	9,517,139	—	—	(9,517,139)	—	—	(9,517,139)	—
Other domestic shares	16,718,345	—	16,400	(5,807,949)	—	—	(5,791,549)	10,926,796
Including:								
Domestic legal-person shares	—	—	—	—	—	—	—	—
Domestic natural person shares	16,718,345	—	16,400	(5,807,949)	—	—	(5,791,549)	10,926,796
Total number of restricted shares outstanding								
	354,809,141	—	16,400	(15,325,088)	—	—	(15,308,688)	339,500,453
Listed tradable shares								
RMB ordinary shares	453,363,529	340,675,786	(16,400)	15,325,088	—	—	355,984,474	809,348,003
Domestic listed foreign shares (B share)	557,497,485	—	—	—	—	—	—	557,497,485
Total listed tradable shares	1,010,861,014	340,675,786	(16,400)	15,325,088	—	—	355,984,474	1,366,845,488
Total shares	1,365,670,155	340,675,786	—	—	—	—	340,675,786	1,706,345,941

The conversion period of Chenming convertible bonds issued by the Company started on 15 March 2005. Pursuant to the approval by the twenty-first meeting of the fourth session of the Board of Directors, the Company early redeemed all the Company's remaining convertible bonds on 14 May 2007. During the reporting period, a total of 340,675,786 shares were converted.

Changes of the share capital as mentioned above were reviewed by China Rightson Certified Public Accountants. A capital review report Zhong Rui Hua Heng Xin Yan Zi No. II [2007] 018 (中瑞華恒信驗字II [2007]第018號) was published for the certification of the review.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

34. Capital reserves

The Group

2008

	Opening balance RMB	Increase for the year RMB	Closing balance RMB
Premium of share capital			
Exercise of conversion rights in convertible bonds of the Company	2,018,215,301.98	—	2,018,215,301.98
Capital contribution from investors	1,754,786,187.93	2,355,491,895.71	4,110,278,083.64
Shares issued by way of capitalization of capital reserves	(737,021,418.15)	—	(737,021,418.15)
Other capital reserves			
Transfer from capital reserves under the original system	463,813,228.85	—	463,813,228.85
Provision for long-term equity investment	237,198,605.60	—	237,198,605.60
Others	1,000,000.00	—	1,000,000.00
Total	3,737,991,906.21	2,355,491,895.71	6,093,483,801.92

Increase in premium of share capital during the year was due to the increase of capital reserves of the Company by RMB2,355,491,895.71 through addition of proceeds of H share issuance after deducting issuing fees and share capital.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

34. Capital reserves (continued)

The Group (continued)

2007

	Opening balance RMB	Increase for the year RMB	Decrease for the year RMB	Closing balance RMB
Premium of share capital				
Exercise of conversion rights in convertible bonds of the Company	334,276,467.95	1,683,938,834.03	—	2,018,215,301.98
Capital contribution from investors	1,754,786,187.93	—	—	1,754,786,187.93
Shares issued by way of capitalization of capital reserves	(737,021,418.15)	—	—	(737,021,418.15)
Other capital reserves				
Equity component separable from the convertible bonds of the Company	195,402,946.14	61,687,883.12	(257,090,829.26)	—
Transfer from capital reserves under the original system	463,813,228.85	—	—	463,813,228.85
Provision for long-term equity investment	237,198,605.60	—	—	237,198,605.60
Others	—	1,000,000.00	—	1,000,000.00
Total	2,248,456,018.32	1,746,626,717.15	(257,090,829.26)	3,737,991,906.21

Increase in premium of share capital of RMB1,426,848,004.77 during the year was mainly due to the conversion of the Company's convertible bonds into RMB ordinary A shares. Increase in premium of share capital of RMB 257,090,829.26 was due to the completion of conversion of equity component in convertible bonds of the Company into shares.

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VII. Notes to the financial statements (continued)

34. Capital reserves (continued)

The Company

2008

	Opening balance RMB	Increase for the year RMB	Decrease for the year RMB	Closing balance RMB
Premium of share capital				
Exercise of conversion rights in convertible bonds of the Company	2,018,215,301.98	—	—	2,018,215,301.98
Capital contribution from investors	1,754,786,187.93	2,355,491,895.71	—	4,110,278,083.64
Shares issued by way of capitalization of capital reserves	(737,021,418.15)	—	—	(737,021,418.15)
Other capital reserves				
Transfer from capital reserves under the original system	778,727,767.93	—	—	778,727,767.93
Others	12,670,520.05	7,797,733.32	(6,452,000.00)	14,016,253.37
Total	3,827,378,359.74	2,363,289,629.03	(6,452,000.00)	6,184,215,988.77

Other reductions during the year in other capital reserves were attributable to the cancellation of subsidiary of the Company Xiangfan Chenming Copperplate Pater Co., Ltd during the year; therefore, investments in such entity in prior years in the form of license rights which caused increase of RMB6,452,000.00 was transferred out of other capital reserves. Increase during the year was attributable to loan extended to a subsidiary of the Group with terms over one year, the interests component of which was included in capital reserves.

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VII. Notes to the financial statements (continued)

34. Capital reserves (continued)

The Company (continued)

2007

	Opening balance RMB	Increase for the year RMB	Decrease for the year RMB	Closing balance RMB
Premium of share capital				
Exercise of conversion rights in convertible bonds of the Company	334,276,467.95	1,683,938,834.03	—	2,018,215,301.98
Capital contribution from investors	1,754,786,187.93	—	—	1,754,786,187.93
Shares issued by way of capitalization of capital reserves	(737,021,418.15)	—	—	(737,021,418.15)
Other capital reserves				
Equity component separable from the convertible bonds of the Company	195,402,946.14	61,687,883.12	(257,090,829.26)	—
Transfer from capital reserves under the original system	778,727,767.93	—	—	778,727,767.93
Others	—	12,670,520.05	—	12,670,520.05
Total	2,326,171,951.80	1,758,297,237.20	(257,090,829.26)	3,827,378,359.74

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VII. Notes to the financial statements (continued)

35. Surplus reserve

The Group

2008

	Statutory surplus reserve RMB
Balance at the beginning of the year	723,742,920.58
Accruals of the year	101,733,929.95
Balance at the end of the year	825,476,850.53

2007

	Statutory surplus reserve RMB
Balance at the beginning of the year	642,691,568.68
Accruals of the year	81,051,351.90
Balance at the end of the year	723,742,920.58

The Company

2008

	Statutory surplus reserve RMB
Balance at the beginning of the year	711,553,338.67
Accruals of the year	101,733,929.95
Balance at the end of the year	813,287,268.62

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

35. Surplus reserve (continued)

The Company (continued)

2007

	Statutory surplus reserve RMB
Balance at the beginning of the year	630,501,986.77
Accrual of the year	81,051,351.90
Balance at the end of the year	711,553,338.67

36. Undistributed profits

The Group

	Report year RMB	Previous year RMB
Undistributed profits at the beginning of the year	2,576,650,349.38	1,894,827,041.81
Add: Net profits of the year	1,075,291,741.53	967,636,172.39
Less: Appropriation of statutory surplus reserves (1)	(101,733,929.95)	(81,051,351.90)
Profits available for distribution to shareholders	3,550,208,160.96	2,781,411,862.30
Less: Dividends payable – cash dividends with respect to last year/prior years approved on the general shareholders' meeting (2)	(273,015,350.56)	(204,761,512.92)
Undistributed profits at the end of the year	3,277,192,810.40	2,576,650,349.38
Including: Cash dividends/profits resolved to be distributed after the balance sheet date (3)	103,102,297.05	273,015,350.56

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VII. Notes to the financial statements (continued)

36. Undistributed profits (continued)

The Company

	Report year RMB	Previous year RMB
Undistributed profits at the beginning of the year	1,509,756,228.39	985,055,574.16
Add: Net profits of the year	1,017,339,299.46	810,513,519.05
Less: Appropriation of statutory surplus reserves (1)	(101,733,929.95)	(81,051,351.90)
Profits available for distribution to shareholders	2,425,361,597.90	1,714,517,741.31
Less: Dividends payable – cash dividends with respect to last year/prior years approved on the general shareholders' meeting (2)	(273,015,350.56)	(204,761,512.92)
Undistributed profits at the end of the year	2,152,346,247.34	1,509,756,228.39
Including: Cash dividends/profits resolved to be distributed after the balance sheet date (3)	103,102,297.05	273,015,350.56

(1) Appropriation of statutory surplus reserves

Pursuant to the Articles, statutory surplus reserves are appropriated as 10% of net profits, subject to a cap of accumulated statutory surplus reserves not exceeding 50% of the registered capital of the Company.

(2) Cash dividends for the year approved on the general shareholders' meeting

Based on 1,706,345,941 shares of RMB1 each in issued capital of the Company, cash dividends of RMB1.6 for every 10 shares was distributed to all shareholders in 2007.

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VII. Notes to the financial statements (continued)

36. Undistributed profits (continued)

(3) Distribution of profits resolved after the balance sheet date

Pursuant to the proposal of the Board, based on 2,062,045,941 shares of RMB1 each issued in 2008, it was proposed to distribute cash bonus of RMB0.5 for every 10 share to all shareholders. The above proposal of bonus distribution is pending approval of the general shareholders' meeting.

(4) Surplus reserves appropriated by subsidiaries

On 31 December 2008, the balance of undistributed profits of the Group comprised surplus reserves appropriated by subsidiaries amounting to RMB310,216,818.12 (31 December 2007: RMB294,492,450.47).

37. Minority Interests

Minority interests of the Group's subsidiaries were as follows:

	Closing balance RMB	Opening balance RMB
Jiangxi Chenming Paper Co., Ltd.	815,713,717.19	752,507,449.34
Wuhan Chenming Hanyang Paper Co. Ltd.	538,016,783.48	530,295,583.65
Chibi Chenming Paper Co., Ltd.	157,339,051.39	172,783,706.32
Shandong Chenming Power Supply Holdings. Co., Ltd.	107,131,506.95	223,314,365.63
Yanbian Chenming Paper Co. Ltd.	59,855,122.25	60,196,511.59
Shandong Grand View Hotel Co., Ltd.	21,533,161.02	33,225,054.35
Shouguang Chenming Art Paper Co., Ltd.	34,455,133.14	37,162,604.18
Others	28,651,287.55	26,039,378.05
Total	1,762,695,762.97	1,835,524,653.11

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VII. Notes to the financial statements (continued)

38. Operating Income

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Principal operations		
Including: Machine-made paper	14,573,920,950.63	13,855,610,458.39
Electricity and steam supply	235,551,601.42	245,149,336.54
Building materials	512,594,168.67	869,909,623.83
Papermaking chemicals	88,639,870.79	92,004,112.10
Hotel income	24,148,863.00	—
Others	8,637,234.46	10,209,545.15
Other business		
Including: Sales of raw materials and semi-finished products	67,340,417.99	80,128,973.80
Installation engineering and machine repair workshop	5,178,594.13	7,309,462.36
Rental income	4,523,895.02	3,319,551.29
Others	9,057,839.66	1,101,386.80
Total	15,529,593,435.77	15,164,742,450.26

(1) The following table sets forth the breakdown of the income from principal operations of paper products by geographical segments:

	Accrued during this year RMB	Accrued during the previous year RMB
PRC	12,632,916,470.61	11,550,360,152.02
United States	49,658,043.08	250,062,700.00
Hong Kong	207,129,713.98	303,260,738.83
Japan	146,670,066.70	334,189,414.51
South Africa	236,460,387.56	292,530,145.09
Other overseas countries	1,301,086,268.70	1,125,207,307.94
Total	14,573,920,950.63	13,855,610,458.39

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VII. Notes to the financial statements (continued)

38. Operating Income (continued)

The Group (continued)

(2) Income from sales to the top 5 customers as a percentage of the total sales income:

	Accrued during this year RMB	Accrued during the previous year RMB
Total income from the top 5 customers	767,668,931.88	763,106,105.69
Percentage	4.94%	5.03%

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Principal operations		
Including: machine-made paper	13,094,562,909.82	12,036,416,273.57
Electricity and steam supply	174,746,161.71	167,012,477.08
Other operations		
Including: Sales of raw materials and semi-finished products	280,625,675.72	343,032,764.09
Others	7,487,527.15	6,127,747.81
Total	13,557,782,274.40	12,552,589,262.55

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VII. Notes to the financial statements (continued)

39. Cost of operations

The Group	Accrued during this year RMB	Accrued during the previous year RMB
Principal operations		
Including: Machine-made paper	11,814,955,646.90	11,040,079,368.04
Electricity and steam supply	199,485,256.28	183,564,081.98
Construction materials	444,273,179.83	727,363,739.74
Papermaking chemicals	36,970,588.86	45,891,476.41
Hotel costs	8,356,343.20	—
Others	3,679,523.24	7,495,335.42
Other operations		
Including: Sales of raw materials and semi-finished products	44,323,831.54	67,980,732.21
Installation engineering and machine repair workshop	3,087,541.74	1,723,814.63
Rental expenses	61,605.68	72,238.81
Others	1,568,823.53	310,687.78
Total	12,556,762,340.80	12,074,481,475.02
The Company		
	Accrued during this year RMB	Accrued during the previous year RMB
Principal operations		
Including: machine-made paper	11,534,107,290.70	10,429,603,365.23
Electricity and steam supply	143,771,971.54	116,062,112.00
Other operations		
Including: Sales of raw materials and semi-finished products	269,069,303.09	341,858,350.99
Others	2,974,132.70	77,560.13
Total	11,949,922,698.03	10,887,601,388.35

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VII. Notes to the financial statements (continued)

40. Tax and levies on operations

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Operating tax	3,036,742.52	498,439.94
Urban maintenances and construction tax	5,661,963.50	10,263,741.95
Educational surcharges	3,883,648.29	7,092,242.91
Total	12,582,354.31	17,854,424.80

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Operating tax	306,581.16	282,690.99

41. Finance costs

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Interest expenses	462,613,466.68	555,690,734.09
Less: interest income	(37,757,767.79)	(11,145,945.64)
Foreign exchange difference	(157,411,894.21)	(173,392,166.56)
Handling charges by financial institutions	19,692,699.37	21,010,428.67
Total	287,136,504.05	392,163,050.56

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VII. Notes to the financial statements (continued)

41. Finance costs (continued)

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Interest expenses	373,230,062.16	452,093,348.72
Less: interest income	(21,454,509.81)	(12,604,855.41)
Foreign exchange difference	(163,932,858.44)	(145,414,343.31)
Handling charges by financial institutions	10,118,999.39	9,809,341.96
Total	197,961,693.30	303,883,491.96

42. Loss on impairment of assets

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Provision of bad debt	(43,734,984.55)	99,866,644.83
Provision of allowance for inventory	127,748,848.59	881,984.43
Provision of impairment on long-term investment	548,538.07	1,450,000.00
Provision of impairment on fixed assets	8,562,932.76	—
Total	93,125,334.87	102,198,629.26

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Provision of bad debt	(29,002,386.79)	2,576,681.68
Provision of allowance for inventory	40,386,319.31	881,984.43
Provision of impairment on long-term investment	548,538.07	1,450,000.00
Total	11,932,470.59	4,908,666.11

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VII. Notes to the financial statements (continued)

43. Profit and loss on changes in fair values

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Biological assets at fair value	918,451.60	24,415,400.31
Financial derivatives at fair value	1,738,200.00	5,955,480.00
Total	2,656,651.60	30,370,880.31

44. Investment income

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Long-term equity investment gains		
Of which: profits distributed on invested entity validated using cost method	85,876.96	—
Losses recognized using equity method	(23,167,629.22)	(9,461,550.75)
Total	(23,081,752.26)	(9,461,550.75)

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Long-term equity investment gains		
Of which: profits distributed on invested entity validated using cost method	168,201,020.17	101,488,000.00
Investment loss from disposal of long-term equity investments	(3,552,717.43)	—
Losses recognized using equity method	(23,167,629.22)	(9,461,550.75)
Gain on entrusted loans	161,487,208.39	130,859,318.51
Total	302,967,881.91	222,885,767.76

There are no significant restrictions on remittance of investment gains back to the Company.

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VII. Notes to the financial statements (continued)

45. Non-operating income

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Net income on disposal of assets	3,788,007.38	17,433,602.73
Insurance claims	12,888,742.85	7,929,504.36
Income from default penalty and fine	8,733,073.48	94,670.75
Income from debt reconstructing	103,365.66	1,088,135.44
Unpaid debts	7,188,103.61	3,483,335.36
Profit or loss arising from investment costs for acquisition of minority interests by the corporation being less than its share of fair value of identifiable net assets of the invested entity on acquisition	28,209,117.78	24,040,943.45
Profit or loss arising from investment costs for acquisition of a subsidiary by the corporation being less than its share of fair value of identifiable net assets of the invested entity on acquisition (Note VII. 58)	60,519.78	—
Government grants (Note VII. 48)	211,936,111.85	177,377,455.16
Others	1,459,182.43	770,436.42
Total	274,366,224.82	232,218,083.67

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Net income on disposal of assets	1,966,033.29	4,003,506.13
Income from default penalty and fine	8,257,156.10	41,470.75
Unpaid debts	6,453,734.07	2,740,452.41
Government grants (Note VII. 48)	125,334,696.67	40,526,745.00
Others	681,773.53	191,091.91
Total	142,693,393.66	47,503,266.20

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VII. Notes to the financial statements (continued)

46. Non-operating expenses

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Net loss from disposal of assets	5,007,364.04	27,181,945.34
Donation expenses	5,629,166.60	—
Fine payments	70,630.86	81,800.00
Others	1,091,450.14	462,135.81
Total	11,798,611.64	27,725,881.15

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Net loss from disposal of assets	1,388,338.83	10,400,342.17
Fine payments	8,923.91	—
Donation expenses	4,586,626.60	—
Others	—	17,024.09
Total	5,983,889.34	10,417,366.26

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VII. Notes to the financial statements (continued)

47. Income tax expenses

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Income tax expenses for current year	319,575,675.05	314,278,016.08
Deferred income tax expenses	(23,777,818.63)	(43,483,002.81)
Total	295,797,856.42	270,795,013.27

Reconciliation between income tax expenses and accounting profits is set out as follows:

	Accrued during this year RMB	Accrued during the previous year RMB
Profits before tax for the year	1,555,339,310.69	1,489,336,202.56
Income tax calculated at tax rate of 25% (2007: 24%) on the parent company	388,834,827.67	357,440,688.61
Tax deductions from purchase of domestic- manufactured equipment during the year	(38,356,600.64)	(49,706,706.79)
Effect of non-taxable items (excluding temporary differences)	(434,550.00)	(1,428,931.53)
Effect of non-withheld items (excluding temporary differences)	18,427,803.09	12,337,750.71
Effect of unrecognized taxation losses	13,066,243.68	14,450,363.51
Effect of waiver on extraordinary taxation items	(65,397,167.80)	(62,186,221.27)
Effect of different tax rates of subsidiaries	(8,887,432.67)	(1,819,348.17)
Tax credit for the year arising from taxation losses of previously unrecognized deferred tax assets	(11,668,667.20)	(1,904,847.01)
Under-provision of income tax during the previous year	213,400.29	2,023,515.78
Changes on balance of deferred income tax assets at the beginning of the year caused by adjustment of tax rate	—	1,588,749.43
Income tax for the year	295,797,856.42	270,795,013.27

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

VII. Notes to the financial statements (continued)

47. Income tax expenses (continued)

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Income tax expenses for current year	277,468,037.20	215,688,385.76
Deferred tax expenses	(6,089,292.08)	(18,474,278.30)
Total	271,378,745.12	197,214,107.46

Reconciliation between income tax expenses and accounting profits is set out as follows:

	Accrued during this year RMB	Accrued during the previous year RMB
Profit before tax for the year	1,288,718,044.58	1,007,727,626.51
Income tax calculated at tax rate of 25% (2007: 24%) on the parent company	322,179,511.15	241,854,630.36
Tax deductions from purchase of domestic- manufactured equipment during the year	(26,945,499.64)	(36,586,979.70)
Effect of non-taxable items (excluding temporary differences)	(36,420,014.73)	(22,086,347.82)
Effect of non-withheld items (excluding temporary differences)	12,564,748.34	2,843,145.52
Changes on balance of deferred income tax assets at the beginning of the year caused by adjustment of tax rate	—	1,599,446.72
Effect of different tax rates of branch companies	—	9,590,212.38
Income tax for the year	271,378,745.12	197,214,107.46

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VII. Notes to the financial statements (continued)

48. Government grants

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Government grants received in relation to assets		
Financial support fund	57,823,238.62	40,000.00
Total	57,823,238.62	40,000.00
Government grants received in relation to income		
Reversal of value-added tax (note 1)	33,851,926.78	75,372,967.36
Financial support fund (note 2)	176,259,321.68	97,104,487.80
Total	210,111,248.46	172,477,455.16
Government grants accounted for in profit or loss account of the current period	211,936,111.85	177,377,455.16
Government grants accounted for in deferred income	56,828,375.23	830,000.00

Note 1: Reversal of value-added tax was the value-added tax levied on products of the subsidiaries of the Company primarily made of the three remains and shoddy wood subject to the value-added tax benefit of levy-first-refund-immediately mainly in accordance with Cai Shui [2006] No 102 promulgated by the State Administration of Taxation in August 2006.

Note 2: Financial support fund was the financial incentive fund and other support fund granted by the local governments to support the development of the Company and its subsidiaries.

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VII. Notes to the financial statements (continued)

48. Government grants (continued)

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Government grants received in relation to assets Financial support fund	5,643,238.62	—
Government grants received in relation to income Financial support fund	125,229,000.00	40,526,745.00
Government grants accounted for in profit or loss account of the current period	125,334,696.67	40,526,745.00
Government grants accounted for in deferred income	5,537,541.95	—

49. Earnings per share

Net profits for the period attributable to ordinary shareholders for the purpose of calculating earnings per share are as follows:

	Accrued during this year RMB	Accrued during the previous year RMB
Net profits for the period attributable to ordinary shareholders	1,075,291,741.53	967,636,172.39

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VII. Notes to the financial statements (continued)

49. Earnings per share (continued)

Net profits for the period attributable to ordinary shareholders for the purpose of calculating diluted earnings per share are as follows:

	Accrued during this year RMB	Accrued during the previous year RMB
Net profits for the period attributable to ordinary shareholders	1,075,291,741.53	967,636,172.39
Interests on dilutive potential ordinary shares for the period recognized as expenses attributable to ordinary shareholders after deducting the effect of income tax	N/A	46,653,405.07
Effect of income tax attributable to ordinary shareholders	N/A	(11,198,124.23)
Total	N/A	1,003,091,453.23

For the purpose of calculating earnings per share, the denominator, being the weighted average of outstanding ordinary shares, is calculated as follows:

	Accrued during this year RMB	Accrued during the previous year RMB
Number of outstanding ordinary shares at the beginning of the year	1,706,345,941.00	1,365,670,155.00
Add: number of weighted ordinary shares issued during the period	191,456,010.93	246,109,034.73
Less: number of weighted ordinary shares repurchased during the period	—	—
Number of outstanding weighted ordinary shares at the end of the year	1,897,801,951.93	1,611,779,189.73

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VII. Notes to the financial statements (continued)

49. Earnings per share (continued)

For the purpose of calculating diluted earnings per share, the number of outstanding weighted average ordinary shares is calculated as follows:

	Accrued during this year RMB	Accrued during the previous year RMB
Number of weighted average ordinary shares for the purpose of calculating basic earnings per share	1,897,801,951.93	1,611,779,189.73
Add: number of weighted average ordinary shares increased assuming dilutive potential ordinary shares were converted into issued ordinary shares	N/A	94,668,092.54
Of which: number of weighted ordinary shares increased on conversion of convertible corporate bonds	N/A	94,668,092.54
Number of weighted average ordinary shares for the purpose of calculating diluted earnings per share	N/A	1,706,447,282.27

Earnings per share

	Accrued during this year RMB	Accrued during the previous year RMB
Calculated based on net profits attributable to shareholders of parent company:		
Basic earnings per share	0.57	0.60
Diluted earnings per share	N/A	0.59

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VII. Notes to the financial statements (continued)

50. Net profit after deducting extraordinary gains and losses

	Accrued during this year RMB	Accrued during the previous year RMB
Net profits	1,259,541,454.27	1,218,541,189.29
Add: items of extraordinary gains and losses		
Gains and losses generated from held for trading financial instatement	(1,738,200.00)	(5,955,480.00)
Reversal of impairment provision on receivables tested for impairment on individual basis	(39,718,405.84)	—
Net gains and losses from disposal of non-current assets	1,219,356.66	9,748,342.61
Government grants accounted for in profit and loss account of the current period	(178,084,185.07)	(102,004,487.80)
Net gains and losses from debt restructuring	(103,365.66)	(1,088,135.44)
Profit or loss arising from investment costs for acquisition of minority interests by the corporation being less than its share of fair value of identifiable net assets of the invested entity on acquisition	(28,209,117.78)	(24,040,943.45)
Profit or loss arising from investment costs for acquisition of a subsidiary by the corporation being less than its share of fair value of identifiable net assets of the invested entity on acquisition	(60,519.78)	—
Non-operating net gains and losses other than the above items	(23,477,854.77)	(11,734,011.08)
Add: effect of extraordinary gains and losses on income tax	34,679,297.41	21,695,055.51
Net profits after deducting extraordinary gains and losses	1,024,048,459.44	1,105,161,529.64
Of which: net profits attributable to shareholders		
of parent company	854,268,917.39	878,418,573.66
Net profits attributable to minority interests	169,779,542.05	226,742,955.98

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VII. Notes to the financial statements (continued)

51. Cash and cash equivalents

The Group

	At the end of the year RMB	At the beginning of the year RMB
Cash	2,687,579,159.85	613,826,456.62
Of which: Treasury cash	1,341,632.42	2,688,459.77
Bank deposits repayable on demand	2,686,237,527.43	611,137,996.85
Balance of cash and cash equivalents	2,687,579,159.85	613,826,456.62

The Company

	At the end of the year RMB	At the beginning of the year RMB
Cash	2,080,005,634.40	235,957,551.29
Of which: Treasury cash	30,527.86	124,896.69
Bank deposits repayable on demand	2,079,975,106.54	235,832,654.60
Balance of cash and cash equivalents	2,080,005,634.40	235,957,551.29

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VII. Notes to the financial statements (continued)

52. Supplementary information on cash flow statements

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Reconciliation of net profits as cash flows from operating activities		
Net profits	1,259,541,454.27	1,218,541,189.29
Add: provision for impairment of assets	93,125,334.87	102,198,629.26
Depreciation of fixed assets	1,123,298,624.07	1,008,525,601.52
Depreciation of real estate held for investment	1,738,256.04	1,692,178.63
Intangible assets amortized	24,785,007.19	21,011,320.41
Amortisation of long-term expenses to be amortized	10,479,070.22	13,580,649.59
Investment gains	23,081,752.26	9,461,550.75
Net losses from disposal of fixed assets	1,219,356.66	9,748,342.61
Financial expenses	289,644,850.83	349,485,068.77
Decrease in stock (minus: increase)	(1,971,610,816.00)	(286,774,248.96)
Decrease in consumable biological assets (minus: increase)	(205,255,558.95)	(48,230,037.74)
Losses from change in fair value (minus: gains)	(2,656,651.60)	(30,370,880.31)
Decrease in deferred income tax assets (minus: increase)	(24,105,514.34)	(65,231,585.59)
Increase in deferred income tax debt (minus: decrease)	327,695.71	6,103,850.08
Profit or loss arising from investment costs for acquisition of minority interests by the corporation being less than its share of fair value of identifiable net assets of the invested entity on acquisition	(28,209,426.61)	(24,040,943.45)
Profit or loss arising from investment costs for acquisition of a subsidiary by the corporation being less than its share of fair value of identifiable net assets of the invested entity on acquisition	(60,519.78)	—

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VII. Notes to the financial statements (continued)

52. Supplementary information on cash flow statements (continued)

The Group (continued)

	Accrued during this year RMB	Accrued during the previous year RMB
Decrease in operating receivables (minus: increase)	631,971,826.80	(909,649,696.33)
Increase in operating payables (minus: decrease)	706,826,061.40	(51,787,863.52)
Net cash flows from operating activities	1,934,140,803.04	1,324,263,125.01
Major investments and financing activities not involving cash settlements		
Capital converted from debt	—	1,815,151,440.06
Net change in cash and cash equivalents		
Cash balance at the end of the year	2,687,579,159.85	613,826,456.62
Less: cash balance at the beginning of the year	613,826,456.62	784,320,395.18
Net increase in cash and cash equivalents	2,073,752,703.23	(170,493,938.56)

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VII. Notes to the financial statements (continued)

52. Supplementary information on cash flow statements (continued)

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Reconciliation of net profits as cash flows from operating activities		
Net profits	1,017,339,299.46	810,513,519.05
Add: provision of impaired assets	11,932,470.59	4,908,666.11
Depreciation of fixed assets	636,865,171.67	597,047,915.21
Depreciation of real estate held for investment	1,738,256.04	1,692,178.63
Intangible assets amortized	9,192,696.46	8,535,125.98
Investment gains	(302,967,881.91)	(222,885,767.76)
Net losses from disposal of fixed assets	(577,694.46)	6,396,836.04
Financial expenses	202,715,131.70	285,151,322.33
Decrease in stock (minus: increase)	(1,095,688,644.28)	45,452,211.35
Decrease in deferred income tax assets (minus: increase)	(6,089,292.08)	(34,129,708.29)
Decrease in operating receivables (minus: increase)	(331,577,867.42)	(67,328,339.67)
Increase in operating payables (minus: decrease)	418,589,550.86	116,327,723.65
Net cash flows from operating activities	561,471,196.63	1,551,681,682.63
Major investments and financing activities not involving cash settlements		
Capital converted from debt	—	2,050,071,904.63
Net change in cash and cash equivalents		
Cash balance at the end of the year	2,080,005,634.40	235,957,551.29
Less: cash balance at the beginning of the year	235,957,551.29	431,939,246.80
Net increase in cash and cash equivalents	1,844,048,083.11	(195,981,695.51)

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VII. Notes to the financial statements (continued)

53. Other cash received relating to operating activities

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Finance support fund	176,259,321.68	102,004,487.80
Interest income	37,757,767.79	11,145,945.64
Income on default penalty and fine	8,733,073.48	—
Other income	14,347,616.45	4,934,611.53
Total	237,097,779.40	118,085,044.97

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Finance support fund	125,229,000.00	40,526,745.00
Interest income	21,454,509.81	12,604,855.41
Repayments from subsidiaries	—	479,183,735.05
Income on default penalty and fine	8,257,156.10	—
Other income	8,481,240.92	6,976,521.20
Total	163,421,906.83	539,291,856.66

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VII. Notes to the financial statements (continued)

54. Other cash paid relating to operating activities

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Traffic expense	544,627,054.10	607,302,287.15
Hospitality expense	49,202,638.95	54,713,994.20
Rental expense	13,671,142.45	16,277,434.12
Travel expense	25,301,977.30	28,816,771.37
Office expense	12,761,302.18	15,213,790.85
Waste disposal expense	36,129,966.97	34,316,255.04
Insurance premium	23,239,270.90	19,504,157.26
Water and electricity expense	10,939,864.29	6,289,640.37
Repair expense	14,261,254.87	9,803,453.16
Advertising expense	2,112,057.69	2,806,430.72
Intermediary service expense	14,835,125.30	24,439,184.16
Quality compensation	2,773,156.98	27,709,692.63
Others	38,246,593.27	30,778,762.51
Total	788,101,405.25	877,971,853.54

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VII. Notes to the financial statements (continued)

54. Other cash paid relating to operating activities (continued)

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Traffic expense	248,702,474.08	269,118,918.26
Hospitality expense	31,582,129.33	37,863,687.39
Rental expense	2,851,015.68	4,715,600.85
Travel expense	19,203,629.01	21,006,486.39
Office expense	8,896,573.46	9,111,985.81
Waste disposal expense	11,570,374.63	11,808,733.56
Insurance premium	13,395,430.47	12,627,457.96
Water and electricity expense	1,652,643.85	1,388,764.66
Repair expense	4,177,890.34	3,336,530.15
Advertising expense	313,230.54	2,657,864.72
Intermediary service expense	12,186,981.90	22,345,609.23
Quality compensation	2,476,371.23	26,367,387.93
Payments to subsidiaries	131,773,856.61	—
Research and development expense	10,731,981.19	5,681,395.78
Others	11,691,023.10	41,982,850.20
Total	511,205,605.42	470,013,272.89

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VII. Notes to the financial statements (continued)

55. Cash received relating to other investment activities

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Special subsidy funds received	57,823,238.62	—

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Special subsidy funds received	5,643,238.62	—

56. Other cash received in relation to financing activities

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Decrease in restricted bank deposits during the year	50,557,068.28	—

57. Other cash paid in relation to financing activities

The Group

	Accrued during this year RMB	Accrued during the previous year RMB
Increase in restricted bank deposits during the period	39,043,580.93	84,845,990.79
Cash paid for redemption of convertible bonds by the Company	—	577,766.86
Guarantee expense for convertible bonds	—	3,722,552.40
Total	39,043,580.93	89,146,310.05

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VII. Notes to the financial statements (continued)

57. Other cash paid in relation to financing activities (continued)

The Company

	Accrued during this year RMB	Accrued during the previous year RMB
Increase in restricted bank deposits during the period	—	112,991,173.39
Cash paid for redemption of convertible bonds by the Company	—	577,766.86
Guarantee expense for convertible bonds	—	3,722,552.40
Total	—	117,291,492.65

58. Merger of entities

The Group as a party in merger of non-jointly controlled entities:

In 2008, the overview mergers of non-jointly controlled entities of the Group are set out below:

(1) Shouguang Runsheng Waste Collection Co., Ltd.

(a) Overview of the acquired entity:

During the year, subsidiary of the Company Shouguang Chenming Modern Logistic Co., Ltd. acquired 100% of equity interests in Shouguang Runsheng Waste Collection Co., Ltd. for a consideration of RMB1,000,000.00. As of 31 December 2008, such consideration had not been paid.

The above acquired subsidiary had fair value basically consistent with its carrying amount, specifics are as follows:

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VII. Notes to the financial statements (continued)

58. Merger of entities (continued)

(1) Shouguang Runsheng Waste Collection Co., Ltd. (continued)

(b) Important financial information of the acquired entity:

Items	Carrying amount on the acquisition date RMB
Identifiable assets	
Current assets	20,086,539.98
Non-current assets	458,779.80
Sub-total	20,545,319.78
Identifiable liabilities	
Current liabilities	19,484,800.00
Sub-total	19,484,800.00
Total net assets	1,060,519.78
Less: consideration of acquisition	1,000,000.00
Discount on acquisition	60,519.78
	Amount RMB
Cash and cash equivalents used as consideration of merger	—
Less: cash and cash equivalents held by the merged subsidiary	505,574.07
Acquired cash and cash equivalents received by the subsidiary	(505,574.07)

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VII. Notes to the financial statements (continued)

58. Merger of entities (continued)

(2) Wuxi Songling Paper Co., Ltd.

(a) Overview of the acquired entity:

In June 2008, subsidiary of the Company Fuyu Chenming Paper Co., Ltd. acquired the assets and liabilities of Wuxi Songling Paper Co., Ltd. for nil consideration.

The above acquisition was classified as acquisition of assets and business operations, the difference between the consideration paid by the Group and the carrying amount was included in non-current assets of the Group.

(b) Important financial information of the acquired entity:

Project	Carrying amount on the acquisition date RMB
Identifiable assets	
Current assets	42,541.96
Non-current assets	5,224,429.76
Sub-total	5,266,971.72
Identifiable liabilities	
Current liabilities	5,266,971.72
Sub-total	5,266,971.72
	Amount RMB
Cash and cash equivalents used as consideration of merger	—
Less: cash and cash equivalents held by the merged subsidiary	39,780.38
Acquired cash and cash equivalents received by the subsidiary	(39,780.38)

The acquisition date is the date when the acquiring entity obtains actual control of the acquired entity, which is the date on which the ownership of net assets and control of decisions in business operations of the acquired entity are transferred to the acquiring entity.

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VII. Notes to the financial statements (continued)

59. Disposal of subsidiaries

Upon approval by shareholders' general meeting of Xiangfan Chenming Copperplate Paper Co., Ltd (hereinafter referred to as "Xiangfan Chenming"), the Group cancelled its subsidiary Xiangfan Chenming during the year. Xiangfan Bailan Group Co., Ltd., a minority shareholder of Xiangfan Chenming, was allocated ownership of the then existing plants and copperplate paper machines of Xiangfan Chenming and assumed liabilities thereof. The Company and Wuhan Chenming Hanyang Paper Holdings Co., Ltd., a subsidiary of the Company, gave up their respective claims on the debts of Xiangfan Chenming.

As the cleaning up of assets and liabilities in Xiangfan Chenming was completed at the date of cancellation, therefore it was not including in the scope of consolidation in the combined balance sheet of the Group as of 31 December 2008; however, the operating results of such entity prior to cancellation were reflected in the combined income statement for 2008. The operating results of the cancelled subsidiary during the period from 1 January 2008 up to the date of cancellation are set out as follows:

	Period from 1 January 2008 up to date of cancellation RMB
Non-operating income	3,847,724.51
Provision for impairment of assets	(6,766,933.91)
Net profits	(2,919,209.40)

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VII. Notes to the financial statements (continued)

60. Segment reporting

Apart from machine made-paper business income from business segments and geographical segments of the Group accounted for less than 10% of all respective segment income. Information on related segments of the Group is summarized below.

Segment result

	Accrued during this year RMB	Accrued during the previous year RMB
Segment result	1,606,436,083.27	1,234,994,916.80
Unallocated corporate expenses	(213,411,044.10)	(33,283,195.76)
Unallocated corporate income	207,308,263.05	454,386,000.00
Investment gains	(23,081,752.26)	(9,461,550.75)
Profit and loss on change in fair value	2,656,651.60	30,370,880.31
Finance expense	(287,136,504.05)	(392,163,050.56)
Non-operating income	274,366,224.82	232,218,083.67
Non-operating expenses	(11,798,611.64)	(27,725,881.15)
Profits before tax	1,555,339,310.69	1,489,336,202.56
Income tax	(295,797,856.42)	(270,795,013.27)
Net profits	1,259,541,454.27	1,218,541,189.29

Segment assets

	Accrued during this year RMB	Accrued during the previous year RMB
Segment assets	22,940,152,881.56	20,712,446,123.40
Non-allocated assets	3,359,342,863.45	1,298,662,133.89
Total assets	26,299,495,745.01	22,011,108,257.29

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VII. Notes to the financial statements (continued)

60. Segment reporting (continued)

Segment liabilities

	Accrued during this year RMB	Accrued during the previous year RMB
Segment liabilities	3,433,285,494.11	1,975,867,134.27
Non-allocated liabilities	8,844,435,585.94	9,454,681,458.06
Total liabilities	12,277,721,080.05	11,430,548,592.33

VIII. Related party relations and transactions

(1) Save for subsidiaries set out in note VI, information on the first major shareholder is set as follows

Name of related party	Place of incorporation	Principal operations	Relation with the Company	Economic nature or type	Legal representative
Shouguang Chenming Holdings Co., Ltd	Shouguang City	Investments in papermaking, electricity, coal, forestry projects	The first major shareholder	Limited liability company	Chen Hongguo

Shouguang Chenming Holdings Co., Ltd (hereafter referred to as "Shouguang Chenming Holdings") was established on 30 December 2005 by Shouguang SASAC which contributed its state-owned shares to set up the Company. The China Securities Regulatory Commission finally approved the change in the holder of state-owned Shares of Chenming Paper and the change in nature of its equity interests arising from the establishment of Shouguang Chenming Holdings on 14 August 2006 (Guo Zi Chan Quan [2005] No. 1539) . Since then, the first major shareholder of the Company was changed from State-owned Assets Supervision and Administration Commission of Shouguang City to Shouguang Chenming Holdings .

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VIII. Related party relations and transactions (continued)

- (2) Other related parties which entered into transactions with the Group but without controlling relation are as follows

	Organization Code	Related party relation
Shouguang Liben Paper Making Co., Ltd.	61358854-8	Associated corporation
Qingzhou Chenming Denaturation Amylum Co., Ltd.	16937769-8	Associated corporation
Arjo Wiggins Chenming Specialty Paper Co., Ltd.	78233868-9	Associated corporation

- (3) Major related transactions entered into between the Company and related parties during the year are as follows

- (a) Sale and purchase

Details of sales and purchases of goods to and from related parties by the Company are as follows:

	Accrued during this year		Accrued during the previous year	
	Amount RMB	Percentage %	Amount RMB	Percentage %
Sales - subsidiaries of the Company	1,001,223,140.56	95.89	1,062,798,846.87	99.29
- associated corporations of the Company	42,959,570.88	4.11	7,579,571.34	0.71
	1,044,182,711.44	100.00	1,070,378,418.21	100.00
Purchases - subsidiaries of the Company	6,581,078,483.39	100.00	5,520,741,792.55	100.00
	6,581,078,483.39	100.00	5,520,741,792.55	100.00

The Company sells and purchases to and from related parties at prices negotiated between both parties.

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VIII. Related party relations and transactions (continued)

(3) Major related transactions entered into between the Company and related parties during the year are as follows (Continued)

(b) Lending and borrowing

Details of lending and borrowing between the Company and related parties are as follows:

Name of subsidiaries	Annual rate %	Amount incurred during this year RMB	Balance for this year RMB	Proportion		Amount incurred during the previous year RMB	Remaining the previous year RMB	Proportion %
				%	%			
Jilin Chenming Paper Co., Ltd.	6.723 (1,150,000,000.00)	80,000,000.00	80,000,000.00	4.11	510,000,000.00	1,230,000,000.00	49.42	
Shandong Chenming Panels Co., Ltd.	5.000 (40,000,000.00)	37,000,000.00	37,000,000.00	1.90	(34,000,000.00)	77,000,000.00	3.09	
Wuhan Chenming Hanyang Paper Co., Ltd.	5.022-6.723 (30,000,000.00)	550,000,000.00	550,000,000.00	28.25	(120,000,000.00)	580,000,000.00	23.30	
Wuhan Chenming Qianneng Electric Power Co., Shandong Chenming Paper	6.723 (20,000,000.00)	35,000,000.00	35,000,000.00	1.80	—	55,000,000.00	2.21	
Group Qihe Paperboard Co., Ltd.	6.723 (120,000,000.00)	—	—	—	107,000,000.00	120,000,000.00	4.82	
Jiangxi Chenming Paper Co., Ltd.	6.723-7.830 400,000,000.00	700,000,000.00	700,000,000.00	35.95	(10,000,000.00)	300,000,000.00	12.05	
Heze Chenming Panels Co., Ltd.	5.022-6.723 15,000,000.00	71,000,000.00	71,000,000.00	3.65	31,000,000.00	56,000,000.00	2.25	
Hailaer Chenming Paper Co., Ltd	5.022-6.723 (10,000,000.00)	19,000,000.00	19,000,000.00	0.98	29,000,000.00	29,000,000.00	1.17	
Qihe Chenming Panels Co., Ltd	5.022-6.723 (7,000,000.00)	15,000,000.00	15,000,000.00	0.77	22,000,000.00	22,000,000.00	0.88	
Juancheng Chenming Panels Co., Ltd.	5.022-6.723 20,000,000.00	40,000,000.00	40,000,000.00	2.05	20,000,000.00	20,000,000.00	0.81	
Shandong Chenming Grand View Hotel Co., Ltd.	5.022-6.723 110,000,000.00	110,000,000.00	110,000,000.00	5.65	—	—	—	
Shouguang Chenming Art Paper Co., Ltd.	6.723 290,000,000.00	290,000,000.00	290,000,000.00	14.89	—	—	—	
Total	(542,000,000.00)	1,947,000,000.00	1,947,000,000.00	100.00	555,000,000.00	2,489,000,000.00	100.00	

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VIII. Related party relations and transactions (continued)

(3) Major related transactions entered into between the Company and related parties during the year are as follows (Continued)

(c) Balance of credit and debt

Item	Closing balance RMB	Opening balance RMB
Accounts receivable – between subsidiaries of the Company	525,597,011.45	178,881,249.80
– between associated corporations of the Company	10,744,498.96	—
Total	536,341,510.41	178,881,249.80
Other receivables – between subsidiaries of the Company	840,005,604.20	627,427,338.67
– between associated corporations of the Company	14,678,824.86	14,824,065.87
Total	854,684,429.06	642,251,404.54
Prepayments – between subsidiaries of the Company	270,455,992.44	14,186,653.54
Accounts payable – between subsidiaries of the Company	826,483,624.07	562,460,992.26
– between associated corporations of the Company	—	176,409.70
Total	826,483,624.07	562,637,401.96
Other payables – between subsidiaries of the Company	109,518,990.30	138,875,798.30
Dividends receivable – between subsidiaries of the Company	164,874,997.10	42,933,862.14
Bills payable – between subsidiaries of the Company	3,260,000.00	—

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VIII. Related party relations and transactions (continued)

(d) Senior executive's remuneration

	Accrued during this year RMB'000	Accrued during the previous year RMB'000
Senior executive's remuneration	7,989.20	8,888.02

Senior executives include the Company's directors, supervisors, general managers, deputy general managers, secretary of the board of directors and financial officers.

(e) Guarantee provided for subsidiaries

As at 31 December 2008, guarantee provided for subsidiaries by the Company to secure lending is as follows:

Name of Subsidiaries	Amount under guarantee RMB
Jiangxi Chenming Paper Co., Ltd.	345,000,000.00
Jilin Chenming Paper Co., Ltd.	268,795,150.00
Wuhan Chenming Hanyang Paper Co., Ltd.	43,417,300.00
Zhanjiang Chenming Paper Pulp Co., Ltd.	106,834,600.00
Heze Chenming Panels Co., Ltd.	20,047,300.00
Total	784,094,350.00

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IX. Financial instruments and risk management

Major financial instruments of the Group include borrowings, receivables and accounts payables, etc. Detailed descriptions of these financial instruments are set out in Note 7. Below are the risks associated with such financial instruments and the risk management policies adopted by the Group to mitigate such risks. The management of the Group manages and monitors such risk exposures to ensure such risks are contained within a prescribed scope.

1. Objective and measures of risk management

The Group engages in risk management with the aim of achieving an appropriate balance between risk and return, where the negative effects of risks against the Group's operating results are minimized, in order to maximize the benefits of shareholders and other stakeholders. Based on such objective in risk management, the underlying strategy of the Group's risk management is to ascertain and analyze all types of risks exposures of the Group, establish appropriate risk tolerance thresholds, carry out risk management procedures and perform risk monitoring on all kinds of risks in a timely and reliable manner, thus containing risk exposures within a prescribed scope.

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IX. Financial instruments and risk management (continued)

1. Objective and measures of risk management (continued)

1.1. Market risks

1.1.1 Foreign exchange risk

Foreign exchange risk represents risks of loss incurred as a result of changes in exchange rate. The Group is mainly exposed to foreign exchange risks in connection with USD; except for certain subsidiaries of the Company which effect purchases and sales in USD, all the business activities of the remaining principal operations of the Group are settled with Renminbi. On 31 December 2008, except for the USD balances in assets and liabilities, odd monies in EUR and balances in HKD as set out below, all the balances of assets and liabilities of the Group were denominated in Renminbi. The foreign exchange risk arising from assets and liabilities in such foreign currency balances could affect the operating results of the Group.

	Closing balance RMB	Opening balance RMB
Cash and cash equivalents	151,424,949.93	130,538,941.51
Other bank balances and cash	3,127,711.98	—
Accounts receivables	383,790,184.17	760,734,927.92
Accounts payable	(451,290,912.64)	(259,852,046.39)
Other receivables	2,537,036.67	—
Other payables	—	(5,947,322.49)
Short-term borrowings	(58,773,955.58)	(542,239,343.22)
Long-term borrowings due within one year	(638,077,940.62)	(466,541,847.91)
Long-term borrowings	(583,558,787.92)	(2,045,502,626.41)
Total	(1,190,821,714.01)	(2,428,809,316.99)

The Group closely monitors changes in foreign exchange rates as to their effects to the Group's exposure in foreign exchange risk. Currently, the Group has not adopted other policies to circumvent foreign exchange risks.

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IX. Financial instruments and risk management (continued)

1. Objective and measures of risk management (continued)

1.1. Market risks (continued)

1.1.2 Interest rate risk – risk in change of liquidity positions

The risk that changes in interest rate lead to changes in cash flow of the financial instruments of the Group is mainly associated with floating-rate bank borrowings (details set out in Note VII.30). The Group's policy is to maintain these borrowings in floating rates, so as to eliminate fair value risks arising from changes in interest rate.

1.2 Credit risk

On 31 December 2008, the most significant credit risk exposure that might incur financial losses on the Group was mainly attributable to a contractual counterparty's failure to perform its obligations, the effects of which could lead to losses in financial assets of the Group and financial guarantee undertaken by the Group, specific details are set out as follows:

The carrying amount of financial assets recognized in the combined balance sheet: in respect of financial instruments carried at fair value, the carrying amount reflects the risk exposure; however, such amount does not represent the maximum credit exposure which changes in line with future changes in fair value.

In order to mitigate credit risk, the Group established a committee to be responsible for determining credit limits, approving credit applications and carrying out other monitoring procedures to ensure necessary actions are taken to collect debts as they fall due. Besides, the Group reassesses the collectability of each amount receivable on an individual basis at each balance sheet date, in order to ensure sufficient provision is allocated for amounts that are not recoverable. As such, the management of the Group believes the credit risk assumed by the Group has been significantly reduced.

The Group places its liquidity funds in banks with higher credit ratings; therefore, the credit risk with respect to liquidity funds is low.

Since the Group's risk exposures are distributed among various contractual parties and various customers, the Group has not significant concentration risk.

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IX. Financial instruments and risk management (continued)

1. Objective and measures of risk management (continued)

1.3 Liquidity risk

In managing liquidity risk, the Group maintains cash and cash equivalent at a level deemed sufficient by the management and carry out monitoring, in order to satisfy the operating needs of the Group and lower the effects of fluctuations in cash flows. The management of the Group monitors the utilization of bank borrowings and makes sure the related borrowing agreements are complied with.

The primary source of funding for the Group is bank borrowings. On 31 December 2008, the Group had outstanding bank facilities of RMB13,854,080,000.

Maturity analysis of financial assets and financial liabilities of the Group at undiscounted remaining contractual obligations are set out as follows:

	1 to 3 months RMB	3 to 12 months RMB	1 to 5 years RMB	Over 5 years RMB	Total RMB
Bank balances and cash	2,853,418,128.07	—	—	—	2,853,418,128.07
Bills receivable	731,953,547.10	242,056,241.14	—	—	974,009,788.24
Accounts receivable	1,154,591,244.89	597,818,104.28	—	—	1,752,409,349.17
Other receivable	90,041,676.35	45,847,936.58	—	—	135,889,612.93
Debts	(1,021,445,495.13)	(1,778,277,523.63)	(4,234,899,487.09)	(236,472,560.60)	(7,271,095,066.45)
Bills payable	(167,536,872.23)	(200,090,689.91)	—	—	(367,627,562.14)
Accounts payable	(2,217,100,498.83)	(425,207,687.07)	—	—	(2,642,308,185.90)
Other payables	(49,527,882.03)	(296,698,360.03)	—	—	(346,226,242.06)
Short-term debentures payable	—	(1,998,800,000.00)	—	—	(1,998,800,000.00)
Dividends payable	(36,089.31)	—	—	—	(36,089.31)
Total	1,374,357,758.88	(3,813,351,978.64)	(4,234,899,487.09)	(236,472,560.60)	(6,910,366,267.45)

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IX. Financial instruments and risk management (continued)

2. Sensitivity analysis

The Group adopts sensitivity analysis techniques to analyze the possible effects of rational and probable changes in risk variables to profit and loss for the current period or to the beneficial interests. Since risk variables seldom change on a stand-alone basis, while the correlation between variables has significant influence to the ultimate amount of change effected by the change in a single risk variable; therefore, the below analysis is based on the assumption that the changes in each variable occurred separately.

2.1 Foreign exchange risk

Holding all other variables constant, the effects of probable and rational changes in exchange rate to the profit and loss for the period and after-tax consequences of interests are set out below:

Item	Change in exchange rate %	Current year		Previous year	
		Effects on		Effects on	
		Effects on net profits RMB '000	shareholders' interests RMB '000	Effects on net profits RMB '000	shareholders' interests RMB '000
US dollar	Appreciate 5% relative to Renminbi	(49,345)	(49,345)	(87,228)	(87,228)
US dollar	Depreciate 5% relative to Renminbi	49,345	49,345	87,228	87,228

The possible occurrence of rational changes in exchange rates of Hong Kong dollar and Euro has relatively small influence on profit and loss for the current period and pre-tax consequences of interests.

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IX. Financial instruments and risk management (continued)

2. Sensitivity analysis (continued)

2.2 Sensitivity analysis of interest rate risk

Sensitivity analysis of interest rate risk is based on the below assumptions:

- Changes in market rate affects the interest income or expense of floating-rate financial instruments;
- Change in fair value of derivative financial instruments and other financial assets and liabilities are calculated using discounted cash flow method at market rate at the balance sheet date.

Based on the above assumptions, holding all other variables constant, the effect of possible occurrence of rational changes in interest rate to the profit and loss for the period and after-tax consequences of interests are set out below:

Item	Change in interest rate %	Current year		Previous year	
		Effects on net profits RMB '000	Effects on shareholders' interests RMB '000	Effects on net profits RMB '000	Effects on shareholders' interests RMB '000
Floating-rate borrowings	Increased by 1%	(38,720)	(38,720)	(44,809)	(44,809)
Floating-rate borrowings	Decreased by 1%	38,720	38,720	44,809	44,809

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X. Commitment

(1) Capital commitments

	Closing balance RMB	Opening balance RMB
Contracted but not yet recognized in the financial statements		
- Commitments in relation to acquisition and construction of long-term assets	291,332,151.32	362,388,255.96

(2) Operating lease commitments

Until the balance sheet date, the Group entered into irrevocable operating lease contracts with non-group companies as follows:

	Closing balance RMB	Opening balance RMB
Minimum lease payments under irrevocable operating leases		
The first year after balance sheet date	49,278,297.28	15,744,593.37
The second year to fifth year after balance sheet date	27,355,917.46	26,274,043.94
The sixth year after balance sheet date and thereafter	56,189,228.75	38,077,285.14
Total	132,823,443.49	80,095,922.45

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XI. Non-adjustment matters included in post balance sheet events

1. Profit distribution proposal

On 8 April 2009, the twelfth meeting of the fifth session of the Board of the Company approved the profit distribution proposal for 2008. It is proposed that based on 2,062,045,941 shares in total at the end of the 2008, RMB0.5 cash bonus per 10 shares (tax included) will be distributed to all shareholders out of undistributed profit, in total amounting to RMB103,102,297.05 of profit distribution.

2. Issuance of medium-term notes proposal

The twelfth meeting of the fifth session of the Board of the Company approved the proposal concerning issuance of medium-term notes. It was approved that medium-term notes of total principal amount not exceeding RMB2.3 billion may be issued in tranche with terms ranging from three to five years. The proceeds from issuance of medium-term notes would be used to supplement the working capital of the Company and repay bank borrowings. The interest rate of the medium-term notes issued would be determined according to the market conditions prevailing at the time of issue, but in no event higher than the best rate for bank loans quoted by the People's Bank of China for the corresponding period. There is no guarantee provided by the Company on the medium-term notes issued.

3. Repurchase of H shares proposal

The twelfth meeting of the fifth session of the Board of the Company approved the proposal concerning the granting of a general mandate to the Board for repurchase of a portion of H shares of the Company. The Board proposes to the shareholders' meeting that the Board and Mr. Chen Hongguo, the chairman of the Board, authorized by, and on behalf of, the Board, be authorized to repurchase a portion of H shares not exceeding 10% of the aggregate nominal value of H shares in issue of the Company as at the time of passing of the relevant resolution at the shareholders' meeting.

The above proposals are pending for approval at the shareholders' meeting of the Company.

XII. Approval of the financial statements

These financial statements were approved by the Board of Directors of the Company on 8 April 2009.

XI PRC Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with Accounting Standards for Business Enterprises

SUPPLEMENTARY INFORMATION PROVIDED BY THE MANAGEMENT FOR 2008

1. DIFFERENCES BETWEEN FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH INTERNATIONAL FINANCIAL REPORTING STANDARDS AND FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH RELEVANT CHINA ACCOUNTING STANDARDS

This reconditioning of differences between the financial statements prepared domestically and overseas was prepared by Shandong Chenming Paper Holdings Limited in accordance with the relevant requirements of the "Compilation Rules for Information Disclosures by Companies that Offer Securities to the Public (No. 15) - General Requirements for Financial Reports" (as amended in 2007) issued by the China Securities Regulatory Commission.

The financial statements of the Group for 2008 were prepared in accordance with the PRC Accounting Standards of Business Enterprises (ASBEs) which set out net profits and net assets of RMB1,259,541,454.27 and RMB14,021,774,664.96 respectively. These figures are different from those reported in the financial statements prepared in accordance with the International Financial Reporting Standards in the following material aspects:

	31 December 2008 Net assets RMB	For the year 2008 Net profit RMB
Amount presented per IFRS	13,656,968,902.24	1,294,998,937.34
Special fund for treasury bond received and special accounts payable	344,948,245.89	(32,490,567.06)
Capitalization of foreign exchange gains and losses on project loans	19,857,516.83	(2,966,916.01)
Amount presented per PRC ASBES	14,021,774,664.96	1,259,541,454.27

The reason of such differences is as follows:

In years prior to 2006, according to the principles of the PRC Accounting Standards of Business Enterprises (ASBEs), the Group will receive special fund for treasury bond received and special accounts payable related to construction of relevant fixed assets which are included in capital reserve. However; according to IAS, the Group will account for special fund for treasury bond received and special accounts payable under deferred income and be amortized by installments over the useful lives of fixed assets

The above differences were all incurred in years prior to 2006, the management believes such differences in accounting principles will gradually be eliminated in future years.

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2. RETURN ON NET ASSETS AND EARNINGS PER SHARE ON FULLY DILUTED AND WEIGHTED AVERAGE BASIS

This calculation of return on net assets and earnings per share was prepared by Shandong Chenming Paper Holdings Limited (hereinafter referred to as the "Company") in accordance with the relevant requirements of the spare "Compilation Rules for Information Disclosures by Companies that Offer Securities to the Public (No. 09) – Calculations and disclosures for the return on net assets and earnings per share" (as amended in 2007) issued by the China Securities Regulatory Commission.

Profits during the reporting period	Calculated in accordance with the net profits attributable to holders of the ordinary shares in the company	Calculated in accordance with the net profits attributable to holders of ordinary shares in the Company, after deducting extraordinary gains and losses
Return on net assets		
Fully diluted basis	8.77%	6.97%
Weighted average basis	10.24%	8.13%
Earnings per share		
Basis earnings per share	0.57	0.45
Diluted earnings per share	N/A	N/A

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3. ANALYSIS ON CHANGES OF ITEMS IN THE FINANCIAL STATEMENTS

The following analysis on changes of items in the financial statements was prepared by Shandong Chenming Paper Holdings Limited in accordance with the relevant requirements of the "Compilation Rules for Information Disclosures by Companies that Offer Securities to the Public (No. 15) - General Requirements for Financial Reports" (as amended in 2007) issued by the China Securities Regulatory Commission.

Items in balance sheet	2008 RMB	2007 RMB	Range of change %	Reason for the difference
Bank balances and cash	2,853,418,128.07	740,621,843.91	285	(1)
Financial assets held for trading	—	5,955,480.00	(100)	(2)
Bills receivable	974,009,788.24	1,676,684,054.95	(42)	(3)
Accounts receivable	1,752,409,349.17	1,660,020,696.84	6	(4)
Inventories	3,397,792,930.38	1,744,492,612.36	95	(5)
Other current assets	151,993,045.95	—	100	(14)
Fixed assets	14,213,441,758.08	13,243,156,039.93	7	(6)
Projects under construction	431,379,272.50	904,753,634.02	(52)	(6)
Intangible assets	1,277,076,588.53	822,301,826.32	55	(7)
Long-term expenses				
to be amortized	37,227,730.36	56,513,234.75	(34)	(8)
Consumable biological assets	301,212,691.14	92,159,871.29	227	(9)
Short-term borrowings	1,516,945,042.67	3,594,000,057.28	(58)	(10)
Bills payable	367,627,562.14	130,056,316.74	183	(11)
Accounts payable	2,642,308,185.90	1,656,706,980.62	59	(12)
Advance receipts	101,693,578.57	170,286,629.21	(40)	(13)
Tax payables	49,965,982.34	102,444,450.86	(51)	(14)
Non-current liabilities due				
within one year	1,038,125,240.62	667,746,417.91	55	(15)
Other current liabilities	1,941,874,444.43	506,212,916.67	284	(16)
Long-term borrowings	4,019,250,823.86	4,056,194,662.35	(1)	(17)
Deferred income	56,828,375.23	830,000.00	6,747	(18)
Share capital	2,062,045,941.00	1,706,345,941.00	21	(19)
Capital reserves	6,093,483,801.92	3,737,991,906.21	63	(20)

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3. ANALYSIS ON CHANGES OF ITEMS IN THE FINANCIAL STATEMENTS (continued)

Items in income statement	2008 RMB	2007 RMB	Range of change %	Reason for the difference
Operating income	15,529,593,435.77	15,164,742,450.26	2	(21)
Operating expenses	12,556,762,340.80	12,074,481,475.02	4	(22)
Tax and added tax on principal operations	12,582,354.31	17,854,424.80	(30)	
Selling expenses	705,595,565.95	783,289,341.85	(10)	(23)
Administrative expenses	561,194,537.62	530,820,858.29	6	(24)
Finance expenses	287,136,504.05	392,163,050.56	(27)	(25)
Losses from impairment of assets	93,125,334.87	102,198,629.26	(9)	(26)
Investment gains	(23,081,752.26)	(9,461,550.75)	144	(27)
Non-operating income	274,366,224.82	232,218,083.67	18	(28)

- (1) Bank balances and cash of the Group as at 31 December 2008 increased by 285% over 31 December 2007, mainly due to the issuance of H-shares of the Group in June 2008, raising proceeds and receipt of interests.
- (2) Financial assets held for trading for the year reduced by RMB5,955,480.00, due to the future pooling foreign exchange contracts entered into in 2007 by subsidiary Jiangxi Chenming Paper Co., Ltd expiring successively during the year.
- (3) Bills receivable for the year decreased by 42%, primarily due to the Group making sales on credit more frequently and requiring repayments from sales contractors within a credit period, in a way gradually reducing settlement by bills receivable and causing the balance to shrink significantly.
- (4) Accounts receivable for the year increased by 6%, mainly due to the increase in income for the year.
- (5) Stock increased by 95% during the year, primarily due to the drop in market price of paper products and slump in demand resulted by the financial crisis during the year, leading to period-on-period declines in sales of all four quarters. In view of this, the management had allocated sufficient provision for the drop in price of stock.
- (6) Fixed assets increased by 7% during the year, projects under construction reduced by 52%, mainly because: a. a 120,000-tonne coated paper project, construction work in Grand View Hotel and a 98,000-tonne waste paper de-inking project were transferred to fixed assets; b. Fuyu Chenming Paper Co., Ltd., a subsidiary of the Company, acquired the entire fixed assets of 黑龍江斯達紙業有限公司(Heilongjiang Xida Paper Company Limited) and 黑龍江造紙廠(Heilongjiang Paper Plant), therefore increasing amounts in fixed assets.

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3. ANALYSIS ON CHANGES OF ITEMS IN THE FINANCIAL STATEMENTS (Continued)

- (7) Intangible assets increased by 55% during the year, mainly due to subsidiary Zhanjiang Chenming Paper Pulp Co., Ltd. commenced preparation work for construction during the year, which increased land use rights.
- (8) Long-term expenses to be amortized reduced by 34% during the year, primarily attributable to the completion of assets acquisition by subsidiary Fuyu Chenming Paper Co., Ltd. during the year, where the payments on land and equipment leases originally required to be paid were reduced.
- (9) Consumable biological assets increased by 227% during the year, mainly due to purchase, growing and fair value change of forestry by subsidiaries of the Company, i.e. Zhanjiang Chenming Arboriculture Co., Ltd., Yangjiang Chenming Arboriculture Co., Ltd., Nanchang Chenming Arboriculture Co., Ltd. and Huanggang Chenming Arboriculture Co., Ltd.
- (10) Short-term borrowings were reduced by 58%, mainly because of repayment of a portion of short-term borrowings falling due, since sales of paper products in the first half of 2008 was favorable and the Company had adequate liquidity due to customers making timely payments; as a result, the growth of amount in borrowings was lowered.
- (11) Bills payable increased by 183% during the year, mainly because the Group expanded the usage of payable bills instruments in 2008, where an increased number of bills payable were used to settle purchases of raw materials and equipment.
- (12) Accounts payable increased by 59%, primarily attributable to the Group's extension of payment period on external purchases in view of the impact of the financial crisis.
- (13) Advance receipts for the year dropped by 40%, mainly because overseas sales dropped during the year under the effects of the financial crisis, which caused the advance receipts by the Group's subsidiary Chenming (HK) to reduce compared with last year.
- (14) Tax payables dropped by 51% and other current assets increased by 100% during the year, mainly because certain subsidiaries of the Group paid income tax in advance, which formed credit balances in income tax. Meanwhile, subsidiary Jilin Chenming Paper Co., Ltd. enjoyed the policy of input tax deduction on acquisition of fixed assets creating a larger amount of input tax credits. The balances of income tax paid in advance and not yet credited input tax deduction were reclassified to other current assets at the end of the year.

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3. ANALYSIS ON CHANGES OF ITEMS IN THE FINANCIAL STATEMENTS (Continued)

- (15) Non-current liabilities due within one year increased by 55% during the year, mainly because a portion of the Group's long-term liabilities were falling due in a short period, therefore transferred to 'current liabilities due within one year'.
- (16) Short-term debentures payable increased by 284% during the year. Short-term debentures issued by subsidiary Jiangxi Chenming matured in September 2007 and the Group issued RMB1.9 billion short-term debentures in 2008.
- (17) Long-term borrowings reduced by 1%, primarily attributable to the transfer of a portion of long-term borrowings due in 2009 into "non-current liabilities due within one year" and early repayment of a portion of borrowings.
- (18) Deferred income increased by 6,747% during the year, mainly because the Group received substantial grants from the government with respect to its assets during the year.
- (19) Share capital increased by 21% during the year, mainly because the Company issued 355,700,000 H-shares in June 2008 which increased share capital.
- (20) Capital reserves increased by 63% for the year, primarily because the Company received proceeds in connection with the issuance of H-shares, such amount net of issuance expenses was credited into capital reserves.
- (21) Operating income increased by 2% during the year, mainly due to a rise in average sales price during the year.
- (22) Operating costs rose by 4% during the year, mainly because the average purchase price of raw materials increased as well as higher average cost per unit during the year.
- (23) Sales expenses for the year reduced by 10%, mainly because sales volume decreased in the fourth quarter under the impact of financial crisis, allowing more room for lowering of transportation expenses.

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3. ANALYSIS ON CHANGES OF ITEMS IN THE FINANCIAL STATEMENTS (Continued)

- (24) Administrative expenses increased by 6% during the year, mainly due to loss from production interruption arising from suspension of panel production lines because of the impact of the financial crisis.
- (25) Finance costs decreased by 27% during the year, mainly because the Group issued H-shares in June 2008, the proceeds collected therefrom increased interests income, while the Group reduced short-term borrowings and repaid certain long-term borrowings during the year; and no provision for interest of the convertible bonds was made, thus reducing interest expenses in 2008.
- (26) Losses from impairment of assets during the year was reduced by 9%, primarily due to the Group's receipt of goods payment by 順德星辰(Shunde Xingchen) which was recognized as impaired during the year, therefore, the Group reversed a bad debt fully provided for in the previous year.
- (27) Investment losses for the year increased by 144%, mainly due to the exacerbation of losses in associated corporations during the year.
- (28) Non-operating income increased by 18% during the year, primarily attributable to the increase in government grants and negative goodwill arising from purchase of minority interests during the year.

The supplementary information provided by the management was signed by the responsible personnel of Shandong Chenming Paper Holdings Limited as shown below on 8 April 2009:

Head of Corporation: Chen Hongguo

Chief Financial Officer: Liu Junwu

Head of finance section: Wang Chunfang

8 April 2009

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Deloitte.

德勤

TO THE SHAREHOLDERS OF SHANDONG CHENMING PAPER HOLDINGS LIMITED

山東晨鳴紙業集團股份有限公司

(established in the People's Republic of China with limited liability)

We have audited the consolidated financial statements of Shandong Chenming Paper Holdings Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") set out on pages 281 to 355, which comprise the consolidated balance sheet as at 31 December 2008, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility for the consolidated financial statements

The directors of the Company are responsible for the preparation and the true and fair presentation of these consolidated financial statements in accordance with the International Financial Reporting Standards issued by the International Accounting Standards Board and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the consolidated financial statements are free from material misstatement.

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An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Group as at 31 December 2008 and of the Group's profit and cash flows for the year then ended in accordance with the International Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Deloitte Touche Tohmatsu
Certified Public Accountants
Hong Kong
8 April 2009

XII Independent Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with International Financial Reporting Standard

Consolidated Income Statement

For the year ended 31 December 2008

	NOTES	2008 RMB'000	2007 RMB'000
Revenue	6	15,430,910	14,878,875
Cost of sales		(12,472,911)	(11,845,624)
Gross profit		2,957,999	3,033,251
Other income	7	500,511	462,316
Share of results of associates		(23,168)	(9,462)
Distribution expenses		(705,596)	(783,289)
Administrative expenses		(542,680)	(653,232)
Gain on change in fair value of derivative financial instruments		1,738	5,955
Gain on change in fair value less estimated point-of-sale cost of biological assets		918	24,415
Impairment loss on property, plant and equipment	14	(8,563)	—
Allowance for inventory		(127,749)	(882)
Finance costs	8	(462,613)	(555,693)
Profit before tax	9	1,590,797	1,523,379
Income tax expense	11	(295,798)	(270,795)
Profit for the year		1,294,999	1,252,584
Attributable to:			
Equity holders of the Company		1,102,288	994,013
Minority interests		192,711	258,571
		1,294,999	1,252,584
Dividends	12	273,015	204,760
		2008	2007
Earnings per share	13		
– Basic		RMB 0.58	RMB 0.62
– Diluted		N/A	RMB 0.60

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Consolidated Balance Sheet

At 31 December 2008

	NOTES	2008 RMB'000	2007 RMB'000
Non-current assets			
Property, plant and equipment	14	14,641,475	14,147,218
Prepaid lease payments - non-current portion	15	1,225,356	791,740
Investment property	16	28,165	29,903
Interests in associates	17	66,822	69,890
Available-for-sale investments	18	25,851	26,400
Goodwill	19	20,284	20,284
Biological assets	20	301,213	92,160
Deferred tax assets	30	127,916	103,362
		16,437,082	15,280,957
Current assets			
Inventories	21	3,397,793	1,744,493
Trade and other receivables	22	3,449,740	4,106,882
Prepaid lease payments - current portion	15	42,209	34,817
Derivative financial instruments	23	—	5,955
Income tax recoverable		27,088	—
Restricted bank deposits	24	165,839	126,795
Bank balances and cash	24	2,687,579	613,826
		9,770,248	6,632,768
Current liabilities			
Trade and other payables	25	3,670,671	2,485,607
Borrowings - amount due within one year	26	2,555,070	4,261,746
Short-term debentures	27	1,941,874	506,213
Provision	28	17,987	17,987
Income tax payable		9,374	95,829
Dividend payable		36	36
Deferred income - current portion	29	21,598	32,682
Derivative financial instruments	23	199	—
		8,216,809	7,400,100
Net current assets (liabilities)		1,553,439	(767,332)
Total assets less current liabilities		17,990,521	14,513,625

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	NOTES	2008 RMB'000	2007 RMB'000
Non-current liabilities			
Borrowings - amount due after one year	26	4,019,251	4,056,195
Deferred income - non-current portion	29	307,869	271,030
Deferred tax liabilities	30	6,432	6,104
		4,333,552	4,333,329
Net assets			
		13,656,969	10,180,296
Capital and reserves			
Share capital	31	2,062,046	1,706,346
Reserves		9,850,146	6,664,805
Equity attributable to equity holders of the Company		11,912,192	8,371,151
Minority interests		1,744,777	1,809,145
Total equity			
		13,656,969	10,180,296

The consolidated financial statements on pages 281 to 355 were approved and authorised for issue by the Board of Directors on 8 April 2009 and are signed on its behalf by:

DIRECTOR

DIRECTOR

XII Independent Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with International Financial Reporting Standard

Consolidated Statement of Changes in Equity

For the year ended 31 December 2008

	Attributable to equity holders of the Company									
	Share capital	Capital reserve	Convertible loan notes equity reserve	Statutory surplus reserve	Discretionary surplus reserve	Translation reserve	Retained earnings	Total	Minority interests	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
		(note a)		(note b)	(note b)					
At 1 January 2007	1,365,670	1,446,227	424,802	642,575	117	(2)	1,872,996	5,752,385	1,703,564	7,455,949
Exchange differences arising on translation of foreign operation and net income recognised directly in equity	—	—	—	—	—	306	—	306	—	306
Profit for the year	—	—	—	—	—	—	994,013	994,013	258,571	1,252,584
Total recognised income and expense for the year	—	—	—	—	—	306	994,013	994,319	258,571	1,252,890
Shares issued upon conversion of convertible loan notes	340,676	1,913,207	(424,676)	—	—	—	—	1,829,207	—	1,829,207
Dividends recognised as distribution	—	—	—	—	—	—	(204,760)	(204,760)	—	(204,760)
Redemption of convertible loan notes	—	126	(126)	—	—	—	—	—	—	—
Transfer of reserves	—	—	—	81,051	—	—	(81,051)	—	—	—
Transfer of reserve upon recognition of deferred income (note c)	—	32,682	—	—	—	—	(32,682)	—	—	—
Contributions from minority shareholders	—	—	—	—	—	—	—	—	37,554	37,554
Distributions made by subsidiaries to minority shareholders	—	—	—	—	—	—	—	—	(139,553)	(139,553)
Decrease in minority interests as a result of increase in interest in subsidiaries	—	—	—	—	—	—	—	—	(50,991)	(50,991)
At 31 December 2007	1,706,346	3,392,242	—	723,626	117	304	2,548,516	8,371,151	1,809,145	10,180,296

XII Independent Auditors' Report and Financial Statements and Notes thereto Prepared in Accordance with International Financial Reporting Standard

	Attributable to equity holders of the Company									
	Share capital	Convertible loan notes	Statutory surplus reserve	Discretionary surplus reserve	Translation reserve	Retained earnings	Total	Minority interests	Total	
	RMB'000	RMB'000 (note a)	RMB'000 (note b)	RMB'000 (note b)	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Exchange differences arising on translation of foreign operation and net income recognised directly in equity	—	—	—	—	—	576	—	576	—	576
Profit for the year	—	—	—	—	—	1,102,288	1,102,288	192,711	1,294,999	1,294,999
Total recognised income and expense for the year	—	—	—	—	—	576	1,102,288	1,102,864	192,711	1,295,575
Issue of shares by way of placing and public offering (Note 31)	355,700	2,355,492	—	—	—	—	2,711,192	—	2,711,192	2,711,192
Dividends recognised as distribution	—	—	—	—	—	(273,015)	(273,015)	—	(273,015)	(273,015)
Transfer of reserves	—	—	—	101,734	—	(101,734)	—	—	—	—
Transfer of reserve upon recognition of deferred income (note c)	—	18,061	—	—	—	(18,061)	—	—	—	—
Distributions made by subsidiaries to minority shareholders	—	—	—	—	—	—	—	(142,484)	(142,484)	(142,484)
Decrease in minority interests as a result of increase in interest in subsidiaries	—	—	—	—	—	—	—	(114,595)	(114,595)	(114,595)
At 31 December 2008	2,062,046	5,765,795	—	825,360	117	880	3,257,994	11,912,192	1,744,777	13,656,969

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Notes:

- a. Capital reserve comprises surplus between the fair value of the net assets and the nominal value of shares issued when the Company was converted from a state-owned enterprise to a joint stock limited company, premium of shares issued, transfers from convertible loan notes equity reserve upon exercise and redemption of convertible loan notes, capital surplus arising from capital injection from minority shareholders, transfers from accumulated profits for those government grants recognised in the income statement under International Financial Reporting Standards but are not distributable in accordance with the legal requirement in the People's Republic of China (the "PRC"). The capital reserve can only be used for conversion into share capital.
- b. In accordance with the relevant PRC Company Laws and regulations and the Articles of Association of the Company and other PRC group entities, the Company and other PRC group entities are required to appropriate 10% of their profit after taxation reported in their statutory financial statements prepared under the PRC General Accepted Accounting Principle to the statutory surplus reserve. The appropriation to statutory surplus reserve may cease if the balance of the statutory surplus reserve has reached 50% of the registered capital of the Company and other PRC group entities. After the appropriation of the statutory surplus reserve, appropriation of discretionary surplus reserve can be made upon approval by the shareholders in shareholders' meeting.

Both surplus reserves can be used to make up prior year losses, if any, and can be applied in conversion into capital by means of capitalisation issue. However, when converting the statutory surplus reserve of the Company and other group entities into share capital, the balance of such reserve remaining unconverted must not be less than 25% of the registered capital of the relevant PRC entity.

- c. The Group obtained government grants in relation to the construction of property, plant and equipment of the Group from the local municipal governments. The grants were recorded as deferred income in the consolidated balance sheet and credited to the consolidated income statement on a straight-line basis over the expected useful lives of the related assets. In accordance with the terms of the grants, the relevant amounts were transferred from retained earnings to capital reserve during the year as it cannot be distributed before winding up.

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Consolidated Cash Flow Statement

For the year ended 31 December 2008

	NOTES	2008 RMB'000	2007 RMB'000
Operating activities			
Profit before tax		1,590,797	1,523,379
Adjustments for:			
Share of results of associates		23,168	9,462
Interest income		(37,758)	(11,146)
Finance costs		462,613	555,693
Depreciation of property, plant and equipment		1,118,083	923,309
Depreciation of investment properties		1,738	1,693
Release of lease payment charge		20,379	34,592
Release of government grants		(32,068)	(32,682)
Loss on disposal of property, plant and equipment		1,219	9,749
Impairment loss on property, plant and equipment		8,563	—
(Reverse of) allowances for bad and doubtful debts		(43,735)	99,868
Allowances for inventories		127,749	882
Impairment of available-for-sale investments		549	910
Impairment of interest in associates		—	540
Dividend income from available-for-sale investment		(86)	—
Gain on change in fair value of derivative financial instruments		(1,738)	(5,955)
Gain on change in fair value less estimated point-of-sale cost of biological assets		(918)	(24,415)
Net exchange (gain) loss		(172,969)	5,111
Discount on acquisition of additional interests in subsidiaries		(28,209)	(24,041)
Discount on acquisition of interests in subsidiaries	36	(61)	—
Operating cash flows before movements in working capital		3,037,316	3,066,949
Increase in inventories		(1,971,611)	(286,775)
Increase in biological assets		(205,256)	(48,231)
Decrease (increase) in trade and other receivables		631,972	(847,362)
Increase (decrease) in trade and other payables		837,080	(44,760)
Cash generated from operations		2,329,501	1,839,821
Income tax paid		(433,118)	(276,783)
Interest received		37,758	11,146
Net cash from operating activities		1,934,141	1,574,184

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NOTES	2008 RMB'000	2007 RMB'000
Investing activities		
Purchase of property, plant and equipment	(1,064,904)	(784,153)
Increase in prepaid lease payments	(477,895)	(151,786)
Additional cost incurred in investment property	—	(994)
Acquisition of additional interests in subsidiaries from minority shareholders of subsidiaries	(10)	(87,326)
Investment in associates	(20,100)	—
Purchase of available-for-sale investments	—	(21,400)
Increase in restricted bank deposits	(39,044)	(84,846)
Proceeds on disposal of property, plant and equipment	604	15,746
Government grants received	57,823	—
Dividend income received from available-for-sale investments	86	—
Net cash inflow arising from acquisition of subsidiaries	546	—
Net cash used in investing activities	(1,542,894)	(1,114,759)
Financing activities		
Net proceeds on issuance of new shares	2,711,192	—
New borrowings raised	6,002,052	8,076,267
Borrowings repaid	(7,546,631)	(6,334,110)
Proceeds from issuance of short-term debentures	1,900,000	500,000
Expense incurred in connection with the issuance of short-term debentures	(7,600)	(3,035)
Repayment of short-term debentures	(500,000)	(2,000,000)
Redemption of convertible loan notes	—	(578)
Interest paid	(443,404)	(556,281)
Dividends paid	(273,015)	(205,424)
Dividends paid to minority shareholders of subsidiaries	(142,484)	(139,553)
Capital contribution by minority shareholders of subsidiaries	—	37,554
Net cash from (used in) financing activities	1,700,110	(625,160)
Net increase (decrease) in cash and cash equivalents	2,091,357	(165,735)
Cash and cash equivalents at 1 January	613,826	784,320
Effect of exchange rate changes on cash and cash equivalents	(17,604)	(4,759)
Cash and cash equivalents at 31 December, represented by	2,687,579	613,826
Analysis of the balances of cash and cash equivalents:		
Bank balances and cash	2,687,579	613,826

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Notes to the Financial Statements

For the year ended 31 December 2008

1. GENERAL

Shandong Chenming Paper Holdings Limited (the "Company") is a joint stock company established in the PRC in May 1993. The Company's B Shares and A Shares have been listed on the Shenzhen Stock Exchange since 1997 and 2000 respectively, and its H shares have been listed on the Main Board of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") since June 2008. Its registered office is located at No. 595 Shengcheng Road, Shouguang City, Shandong Province, the PRC.

The ultimate holding company of the Company is State-owned Assets Supervision and Administration Commission of Shouguang City (壽光市國有資產管理局) and the parent company of the Company is Shouguang Chenming Holdings Co., Ltd., which is also established in the PRC.

The consolidated financial statements are presented in Renminbi ("RMB"), which is also the functional currency of the Company and its major group entities.

The Company and its subsidiaries (collectively referred to as the "Group") are principally engaged in manufacture and sale of paper products, construction materials, chemical products, sale of electricity and steam. The activities of principal subsidiaries are set out in Note 38.

2. APPLICATION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRSs")

In the current year, the Group has applied, the following amendments and interpretations ("new IFRSs"), issued by the International Accounting Standard Board ("IASB") which are or have become effective:

IAS 39 & IFRS 7 (Amendments)	Reclassification of Financial Assets
IFRIC 11	IFRS 2: Group and Treasury Share Transactions
IFRIC 12	Service Concession Arrangements
IFRIC 14	IAS19 - The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction

The adoption of these new IFRSs had no material effect on how the results and financial position for the current or prior accounting periods have been prepared and presented. Accordingly, no prior period adjustment has been required.

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2. APPLICATION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRSs") (continued)

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

IFRSs (Amendments)	Improvements to IFRSs ¹
IAS 1 (Revised)	Preparation of Financial Statements ²
IAS 23 (Revised)	Borrowing Costs ²
IAS 27 (Revised)	Consolidated and Separate Financial Statements ³
IAS 32 & 1 (Amendments)	Puttable Financial Instruments and Obligations Arising on Liquidation ²
IAS 39 (Amendment)	Eligible Hedged Items ³
IFRS 1 & IAS 27 (Amendments)	Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate ²
IFRS 2 (Amendment)	Vesting Conditions and Cancellations ²
IFRS 3 (Revised)	Business Combinations ³
IFRS 7 (Amendment)	Improving Disclosures about Financial Instruments ²
IFRS 8	Operating Segments ²
IFRIC 9 & IAS 39 (Amendments)	Embedded Derivatives ⁴
IFRIC 13	Customer Loyalty Programmes ⁵
IFRIC 15	Agreements for the Construction of Real Estate ²
IFRIC 16	Hedges of a Net Investment in a Foreign Operation ⁶
IFRIC 17	Distributions of Non-cash Assets to Owners ³
IFRIC 18	Transfers of Assets from Customers ⁷

¹ Effective for annual periods beginning on or after 1 January 2009 except the amendments to IFRS 5, effective for annual period beginning on or after 1 July 2009

² Effective for annual periods beginning on or after 1 January 2009

³ Effective for annual periods beginning on or after 1 July 2009

⁴ Effective for annual periods ending on or after 30 June 2009

⁵ Effective for annual periods ending on or after 1 July 2008

⁶ Effective for annual periods beginning on or after 1 October 2008

⁷ Effective for transfers on or after 1 July 2009

The adoption of IFRS 3 (Revised) may affect the Group's accounting for business combination for which the acquisition date is on or after 1 January 2010. IAS 27 (Revised) will affect the accounting treatment for changes in the Group'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 financial positions of the Group.

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3. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared on the historical cost basis, except for certain financial instruments and biological assets, which are measured at fair values, as explained in the accounting policies set out below.

The consolidated financial statements have been prepared in accordance with IFRSs issued by the IASB. In addition, the consolidated financial statements include applicable disclosures required by the Rules Governing the Listing of Securities on the Stock Exchange and by the Hong Kong Companies Ordinance.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Minority interests in the net assets of consolidated subsidiaries are presented separately from the Group's equity therein. Minority interests in the net assets consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

Business combinations

The acquisition of businesses is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 *Business Combinations* are recognised at their fair values at the acquisition date.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Business combinations (continued)

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

Acquisition of additional interests in subsidiaries

Discount arising on acquisition of additional interest in subsidiaries, representing the excess of the carrying value of the net assets attributable to the additional interest in the subsidiaries over the cost of the acquisition, is recognised, after reassessment, immediately in profit or loss.

Goodwill arising on acquisition of additional interest in subsidiaries, representing the excess of the cost of the acquisition over the carrying value of the net assets attributable to the additional interest in the subsidiaries, is presented separately on the balance sheet and is carried at cost less any accumulated impairment losses.

Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill is allocated to each of the relevant cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the acquisition. A cash-generating unit to which goodwill has been allocated is tested for impairment annually, and whenever there is an indication that the unit may be impaired. For goodwill arising on an acquisition in a financial year, the cash-generating unit to which goodwill has been allocated is tested for impairment before the end of that financial year. When the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated to reduce the carrying amount of any goodwill allocated to the unit first, and then to other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. Any impairment loss for goodwill is recognised directly in the consolidated income statement. An impairment loss recognised for goodwill is not reversed in subsequent periods.

On subsequent disposal of the relevant cash-generating unit, the attributable amount of goodwill capitalised is included in the determination of the amount of profit or loss on disposal.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Interests in associates

An associate is an entity over which the Group has significant influence and that is neither a subsidiary nor an interest in a joint venture.

The results and assets and liabilities of associates are incorporated in these consolidated financial statements using the equity method of accounting. Under the equity method, investments in associates are carried in the consolidated balance sheet at cost as adjusted for post-acquisition changes in the Group's share of the net assets of the associates, less any identified impairment loss. When the Group's share of losses of an associate equals or exceeds its interest in that associate (which includes any long-term interest, that, in substance, form part of the Group's net investments in the associate), the Group discontinues recognising its share of further losses. An additional share of losses is provided for and a liability is recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that associates.

Any excess of the cost of acquisition over the Group's share of the net fair value of identifiable assets, liabilities and contingent liabilities of the associate recognised at the date of acquisition is recognised as goodwill. The goodwill is included within the carrying amount of the investment and is assessed for impairment as part of the investment.

Any excess of the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition, after reassessment, is recognised immediately in profit or loss.

Where a group entity transacts with an associate of the Group, profits and losses are eliminated to the extent of the Group's interest in the relevant associate.

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods sold and services provided in the normal course of business, net of discounts and sales related taxes.

Revenue from sale of goods is recognised when goods are delivered and title has passed.

Revenue from sale of electricity are recognised when electricity are generated and transmitted to the power grid operated by the local electric power company.

Revenue from sale of steam is recorded based upon output delivered at rates specified under contract terms.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Revenue recognition (continued)

Interest income from a financial asset is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Group as lessor

Rental income from operating leases is recognised in the consolidated income statement on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised as an expense on a straight-line basis over the lease term.

The Group as lessee

Rentals payable under operating leases are charged to profit or loss on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are recognised as a reduction of rental expense over the lease term on a straight-line basis.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Foreign currencies

In preparing the financial statements of each individual group entity, transactions in currencies other than the functional currency of that entity (foreign currencies) are recorded in the respective functional currency at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are recognised in profit or loss in the period in which they arise.

For the purposes of presenting the consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated into the presentation currency of the Group (i.e. RMB) at the rate of exchange prevailing at the balance sheet date, and their income and expenses are translated at the average exchange rates for the year, unless exchange rates fluctuate significantly during the period, in which case, the exchange rates prevailing at the dates of transactions are used. Exchange differences arising, if any, are recognised as a separate component of equity (the translation reserve). Such exchange differences are recognised in profit or loss in the period in which the foreign operation is disposed of.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, are capitalised as part of the cost of those assets. Capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

All other borrowing costs are recognised in profit or loss for the period in which they are incurred.

Government grants

Government grants are recognised as income over the periods necessary to match them with the related costs. Government grants related to depreciable assets are presented as deferred income and are released to income over the useful lives of the assets. Other government grants, including value-added tax refunds and expansion grants are recognised as income when they are unconditional and the group entity is entitled to receive.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Retirement benefit costs

Payments to state-managed retirement benefit schemes are charged as an expense when employees have rendered service entitling them to the contribution.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax base used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited to profit or loss, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority to the same group entity and the group entity intends to settle its current tax assets and liabilities on a net basis.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Research and development expenditure

Expenditures on research activities is recognised as an expense in the period in which it is incurred.

An internally-generated intangible asset arising from development expenditure is recognised only if it is anticipated that the development costs incurred on a clearly-defined project will be recovered through future commercial activity. The resultant asset is amortised on a straight-line basis over its useful life, and carried at cost less subsequent accumulated amortisation and any accumulated impairment losses.

The amount initially recognised for internally-generated intangible asset is the sum of the expenditure incurred from the date when the intangible asset first meets the recognition criteria. Where no internally-generated intangible asset can be recognised, development expenditure is charged to profit or loss in the period in which it is incurred.

Subsequent to initial recognition, internally-generated intangible asset is reported at cost less accumulated amortisation and accumulated impairment losses.

Property, plant and equipment

Property, plant and equipment including buildings held for use in the production or supply of goods or services, or for administrative purposes other than construction in progress, are stated at cost less subsequent accumulated depreciation and accumulated impairment losses.

Depreciation is provided to write off the cost of item of property, plant and equipment other than construction in progress over their estimated useful lives and, after taking into account of their estimated residual value, using the straight-line method.

Construction in progress includes property, plant and equipment in the course of construction for production or for its own use purposes. Construction in progress is carried at cost less any recognised impairment loss. Construction in progress is classified to the appropriate category of property, plant and equipment when completed and ready for intended use. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the consolidated income statement in the year in which the item is derecognised.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Investment properties

Investment properties are properties held to earn rentals and/or for capital appreciation.

On initial recognition, investment properties are measured at cost, including any directly attributable expenditure. Subsequent to initial recognition, investment properties are stated at cost less subsequent accumulated depreciation and any accumulated impairment losses. Depreciation is charged as to write off the cost of investment properties over their estimated useful lives and after taking into account of their estimated residual value, using straight-line method.

An investment property is derecognised upon disposal or when the investment property is permanently withdrawn from use and no future economic benefits are expected from its disposals. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the consolidated income statement in the year in which the item is derecognised.

Impairment of tangible assets other than goodwill (see accounting policy in respect of goodwill arising from acquisition of additional interests in subsidiaries above)

At each balance sheet date, the Group reviews the carrying amounts of its tangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the greater of net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. Impairment losses are recognised as an expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised as income immediately.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials and, where applicable, direct labor costs and those overheads that have been incurred in bringing the inventories to their present location and condition. Cost is calculated using the weighted average method. Net realisable value represents the estimated selling price less all estimated costs to completion and costs to be incurred in marketing, selling and distribution.

Biological assets

Biological assets, which represent immature timber, are initially and subsequently measured at each balance sheet date at their fair value less estimated point-of-sale costs at the point of harvest (costs to sell). All changes in fair value are recognised in profit or loss in the period in which they arise.

The fair values of biological assets are determined using the discounted value of the expected delivered market price for estimated timber volumes less cost of delivery and estimated maintenance costs up to when the timber becomes usable. The discount rate used is the applicable pre-tax weighted average cost of capital of the business unit.

Cost of delivery includes all costs associated with getting the harvested agricultural produce to the market, being harvesting, loading, transport and allocated overheads.

During the planting period, the amortisation charge provided for the prepaid lease payments in respect of the leasehold land on which plantations are located is capitalised as part of the costs of the biological assets. Biological assets are generally felled at the optimum age when ready for intended use. At the time the tree is felled, it is taken out of biological assets (non-current assets) and accounted for under inventory (current assets).

Financial instruments

Financial assets and financial liabilities are recognised on the balance sheet when a group entity becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial assets

The Group's financial assets are classified into one of the three categories, including financial assets at fair value through profit or loss ("FVTPL"), loans and receivables and available-for-sale investments. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period. Interest income is recognised on an effective interest basis for debt instruments.

Financial assets at fair value through profit or loss

Financial assets at FVTPL has two subcategories, including financial assets held for trading and those designated at FVTPL on initial recognition. A financial asset other than a financial asset held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial asset forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 permits the entire combined contract (asset or liability) to be designated as at FVTPL.

At each balance sheet date subsequent to initial recognition, financial assets at FVTPL are measured at fair value, with changes in fair value recognised directly in profit or loss in the period in which they arise.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial assets (continued)

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. At the balance sheet date subsequent to initial recognition, loans and receivables (including trade and other receivables, restricted bank deposits and, bank balances and cash) are carried at amortised cost using the effective interest method, less any identified impairment losses (see the accounting policy on impairment loss on financial assets below).

Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated or not classified as financial assets at FVTPL, loans and receivables or held-to-maturity investments.

Available-for-sale equity investments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments, they are measured at cost less any identified impairment losses at each balance sheet date subsequent to initial recognition (see the accounting policy on impairment loss on financial assets below).

Impairment of financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the financial assets have been affected.

For an available-for-sale equity investment, a significant or prolonged decline in the fair value of that investment below its cost is considered to be objective evidence of impairment.

For all other financial assets, objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organisation.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial assets (continued)

Impairment of financial assets (continued)

For financial assets carried at amortised cost, an impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.

For financial assets carried at cost, the amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment loss will not be reversed in subsequent periods.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade and other receivables, where the carrying amount is reduced through the use of an allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss. When a trade and other receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited to profit or loss.

For financial assets measured at amortised cost, if, in a subsequent period, the amount of impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment losses was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial liabilities and equity

Financial liabilities and equity instruments issued by the Group are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument.

An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities. The Group's financial liabilities are generally classified into financial liabilities at FVTPL and other financial liabilities.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Interest expense is recognised on an effective interest basis.

Financial liabilities at fair value through profit or loss

Financial liabilities at FVTPL has two subcategories, including financial liabilities held for trading and those designated at FVTPL on initial recognition. A financial liability other than a financial liability held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial liability forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 permits the entire combined contract (asset or liability) to be designated as at FVTPL.

At each balance sheet date subsequent to initial recognition, financial liability at FVTPL are measured at fair value, with changes in fair value recognised directly in profit or loss in the period in which they arise.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial liabilities and equity (continued)

Derivative financial instruments

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each balance sheet date. The resulting gain or loss is recognised in profit or loss immediately.

Other financial liabilities

Other financial liabilities including borrowings, short-term debentures, trade and other payables and dividend payable are subsequently measured at amortised cost, using the effective interest method.

Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the assets expire or, the financial assets are transferred and the Group and the Company has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised directly in equity is recognised in profit or loss. If the Group retains substantially all the risks and rewards of ownership of a transferred assets, the Group continues to recognise the financial assets and recognise a collateralised borrowing for proceeds received.

Financial liabilities are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, and it is probable that the Group will be required to settle that obligation. Provisions are measured at the directors' best estimate of the expenditure required to settle the obligation at the balance sheet date, and are discounted to present value where the effect is material.

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4. CRITICAL ACCOUNTING JUDGMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

Critical judgments in applying the Group's accounting policies

In the application of the Group's accounting policies, which are described in Note 3, management has made the following judgments that have the most significant effect on the amounts recognised in the consolidated financial statements.

Timing of transfer of constructions in progress to property, plant and equipment for its intended use

In determining the timing when the construction in progress, especially for large-scale paper manufacturing plant and machinery, is transferred to qualifying asset ready for its intended use requires the Group to determine whether substantially all the activities necessary to bring the qualifying asset to the condition ready for its intended use are completed and related direct expenditure are included in the cost of the qualifying asset. The determination requires the use of management's judgment and experience.

Key sources of estimation uncertainty

The Group makes estimates and assumptions concerning the future. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets in the next financial year are discussed below.

Depreciation of property, plant and equipment

Property, plant and equipment are depreciated on a straight-line basis over their estimated useful lives, after taking into account the estimated residual value. The Group assesses annually the residual value and the useful life of the property, plant and equipment and if the expectation differs from the original estimates, such differences from the original estimates will impact the depreciation charges in the year in which the estimates change.

Impairment of property, plant and equipment

The Group assesses annually whether property, plant and equipment have any indication of impairment in accordance with the accounting policy. The recoverable amounts of property, plant and equipment have been determined based on the higher of value-in-use calculations and fair value less cost to sell. These calculations require the use of judgment and estimates. Where the actual future cash flows are less than expected, a material impairment loss may arise.

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4. CRITICAL ACCOUNTING JUDGMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY (continued)

Key sources of estimation uncertainty (continued)

Impairment of goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires the Group to estimate the future cash flows expected to arise from the cash generating unit and a suitable discount rate in order to calculate the present value. Where the actual future cash flows are less than expected, a material impairment loss may arise. Details of the recoverable amount calculation are disclosed in Note 19.

Allowance for bad and doubtful debts

The Group makes allowances for bad and doubtful debts based on an assessment of the recoverability of trade and other receivables. Allowances are applied to trade and other receivables where events or changes in circumstances indicate that the balances may not be collectable. The identification of bad and doubtful debts requires the use of judgment and estimates. Where the expectation is different from the original estimate, such difference will impact carrying value of trade and other receivables and doubtful debts expenses in the year in which such estimate has been changed.

Allowance for inventory

The Group makes allowance for inventories based on an assessment of the net realizable value of inventories. Allowances are applied to inventories where events or changes in circumstances indicate that the net realisable value is lower than the cost of inventories. The identification of obsolete inventories requires the use of judgment and estimates on the conditions and usefulness of the inventories. Where the expectation is different from the original estimate, such difference will impact carrying value of inventories in the year in which such estimate has been changed.

Deferred tax assets

The Group assesses annually whether to recognise the deferred tax assets. Where there are sufficient taxable profits or temporary differences available in the future, a deferred tax asset will be recognized. The determination requires the use of management's judgments and experience.

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5. CAPITAL RISK MANAGEMENT AND FINANCIAL INSTRUMENTS

a. Capital risk management

In order to maintain a strong credit rating and healthy capital ratios, the Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to shareholders and supporting its business through the optimisation of the debt and equity balance.

The capital structure of the Group consists of debt, which includes the borrowings disclosed in Note 26, trade and other payables in Note 25, short-term debentures in Note 27 and equity attributable to equity holders of the Company, comprising issued capital, reserves and retained earnings.

The management of the Group reviews the capital structure on a quarterly basis. As a part of this review, the management considers the cost of capital and the risks associated with each class of capital. Based on recommendations of the management, the Group will balance its overall capital structure through the payment of dividends, new borrowings, new share issues and the issue of short-term debentures.

b. Financial risk management objectives and policies

Categories and fair value of financial instruments

The carrying amounts of each of the following categories of financial assets and financial liabilities at the balance sheet date are set out as follows:

	2008 RMB'000	2007 RMB'000
Financial assets		
Available-for-sale financial assets	25,851	26,400
Loans and receivables	5,840,632	4,273,488
Financial assets designated as fair value through profit and loss	—	5,955
Financial liabilities		
Financial liabilities stated at amortised cost	12,032,281	11,074,034
Financial liabilities designated as fair value through profit and loss	199	—

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5. CAPITAL RISK MANAGEMENT AND FINANCIAL INSTRUMENTS (continued)

b. Financial risk management objectives and policies (continued)

Categories and fair value of financial instruments (continued)

The major financial instruments of the Group include available-for-sale investments, trade and other receivables, restricted bank deposits, bank balances and cash, derivative financial instruments, trade and other payables, borrowings, short-term debentures and dividend payable. Details of these financial instruments are disclosed in respective notes. The risks associated with these financial instruments are set out below. The management managers and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

Currency risk

Foreign currency risk is the risk that the value of a financial instrument will fluctuate because of changes in foreign exchange rates. The functional currency of the Company and its major subsidiaries is RMB as the primary economic environment in which the Company and majority of other group entities operate is the PRC, however, certain borrowings, bank balances, trade receivables and payables of the Group are denominated in foreign currencies and the Group also entered into certain foreign exchange forward contracts denominated in USD, therefore, the Group is exposed to foreign currency risk.

Approximately 13% (2007: 15%) of the sales of the Group for the year are denominated in currencies other than the functional currency of the Company and other group entities making the sale.

Approximately 22% (2007: 21%) of the purchases of the Group for the year are denominated in currencies other than the functional currency of the Company and other group entities making the purchase.

The major currency of amounts denominated in a currency other than the functional currency of the Group is USD and the monetary assets and liabilities of the Group denominated in USD as at each balance sheet date is as follows:

	2008 RMB'000	2007 RMB'000
Trade and other receivables	386,327	897,211
Bank balances	151,425	130,540
Restricted bank deposits	3,128	—
Trade and other payables	(451,291)	(274,894)
Borrowings	(1,280,411)	(3,054,284)

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5. CAPITAL RISK MANAGEMENT AND FINANCIAL INSTRUMENTS (continued)

b. Financial risk management objectives and policies (continued)

Currency risk (continued)

The Group currently does not have a foreign currency hedging policy. However, management monitors foreign exchange exposure and will consider hedging significant foreign currency exposure should the need arise.

The following table demonstrates the sensitivity of the Group to a reasonably possible change in the RMB spot and forward exchange rate against USD, with all other variables held constant. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at each balance sheet date for the change in foreign currency rates:

	Possible change in exchange rate 5%	
	2008 RMB'000	2007 RMB'000
Increase (decrease) in profit after tax		
- if RMB weaken against foreign currency	(49,345)	(87,228)
- if RMB strengthen against foreign currency	49,345	87,228

In addition, the Group is also exposed to currency risk in respect of foreign currency forward contracts. The notional amount of outstanding foreign exchange forward contracts, which are not designated as cash flow hedges, committed by the Group as at 31 December 2008 is USD3,000,000 (2007: USD34,000,000). If RMB weakens against USD by 5% (RMB strengthens against USD by 5%), the profit for the year will decrease (increase) by RMB1,025,000 (2007: RMB11,950,000) while all other variables are held constant.

Interest rate risk

Fair value interest rate risk

The fair value interest rate risk of the Group relates primarily to fixed-rate bank deposits, borrowings, and short-term debentures. The fixed-rate bank borrowings and short-term debentures are mainly due within one year in which the fair value interest rate risk is considered to be minimal. The Group currently does not have an interest rate hedging policy. However, the management monitors interest rate exposure and will consider hedging significant interest rate exposure should the need arise.

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5. CAPITAL RISK MANAGEMENT AND FINANCIAL INSTRUMENTS (continued)

b. Financial risk management objectives and policies (continued)

Interest rate risk (continued)

Cash flow interest rate risk

The cash flow interest rate risk of the Group relates primarily to variable-rate bank borrowings and other borrowings from International Finance Corporation (“IFC”), a minority shareholder of a subsidiary.

The following tables demonstrate the sensitivity of the Group to a reasonably possible change in the interest rate of the variable-rate bank borrowings and other borrowings from IFC, with all other variables in particular foreign currency rates, remain constant and assuming the amount of liability outstanding at the balance sheet date was outstanding for the whole year. 100 basis points (“bp”) is the sensitivity rate used when reporting cash flow interest rate risk internally to key management personnel and represents management’s assessment of the reasonably possible change in interest rates.

	100 bp increase		100 bp decrease	
	2008 RMB'000	2007 RMB'000	2008 RMB'000	2007 RMB'000
(Decrease) increase in profit for the year	(38,720)	(44,809)	38,720	44,809

Price risk

The Group is exposed to equity price risk through its investment in equity securities with carrying value of RMB25,851,000 (2007: RMB26,400,000) as at 31 December 2008 which was classified as available-for-sale investment at the balance sheet date. Sensitivity analysis for price risk is not presented as the available-for-sale financial assets as at 31 December 2008 are made up of unlisted equity securities which are measured at cost less impairment.

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5. CAPITAL RISK MANAGEMENT AND FINANCIAL INSTRUMENTS (continued)

b. Financial risk management objectives and policies (continued)

Credit risk

The credit risk of the Group is primarily attributable to its trade and other receivables. At the balance sheet date, the maximum exposure to credit risk of which will cause a financial loss to the Group due to failure to discharge an obligation by the counterparties or debtors is the carrying amount of the respective recognised financial assets stated in the consolidated balance sheet.

In order to minimise the credit risk, the management of the Group has delegated a team responsible for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual trade debts at each balance sheet date to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the directors of the Company consider that the credit risk of the Group is significantly reduced.

No single customer accounted for more than 10% of the total revenue and trade receivable balance of the Group during the year, in this regard, the directors of the Company consider that the Group have no significant concentration of credit risk, with exposure spread over a large number of counterparties and customers.

Liquidity risk

The Group relies on bank borrowings and issuance of short-term debentures as a significant source of liquidity. In the management of the liquidity risk, the Group monitors and maintains a level of cash and cash equivalents deemed adequate by the management to finance the Group's operations and mitigate the effects of fluctuations in cash flows. The management monitors the utilisation of bank borrowings and ensures compliance with the loan covenant throughout the year.

The following tables detail the remaining contractual maturity for non-derivative financial liabilities of the Group. The tables have been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Group can be required to pay. The table includes both interest and principal cash flows.

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5. CAPITAL RISK MANAGEMENT AND FINANCIAL INSTRUMENTS (continued)

b. Financial risk management objectives and policies (continued)

Liquidity risk (continued)

	Weighted Average effective interest rate %	On demand RMB'000	1-3 months RMB'000	3-6 months RMB'000	6-12 months RMB'000	1-2 years RMB'000	2-5 years RMB'000	Total		Total carrying amount RMB'000
								More than 5 years RMB'000	undiscounted cash flows RMB'000	
At 31 December 2008										
Non-derivative financial liabilities										
Borrowings										
- fixed-rate	4.68	—	754,221	443,648	34,915	30,444	426,877	171,700	1,861,805	1,662,476
- variable-rate	4.97	—	267,224	506,320	793,395	532,719	3,244,859	64,773	5,409,290	4,911,845
Short-term debentures	5.20	—	—	736,400	1,262,400	—	—	—	1,998,800	1,941,874
Trade and other payables	—	246,404	2,400,575	666,463	202,608	—	—	—	3,516,050	3,516,050
Dividend payable	—	36	—	—	—	—	—	—	36	36

	Weighted Average effective interest rate %	On demand RMB'000	1-3 months RMB'000	3-6 months RMB'000	6-12 months RMB'000	1-2 years RMB'000	2-5 years RMB'000	Total		Total carrying amount RMB'000
								More than 5 years RMB'000	undiscounted cash flows RMB'000	
At 31 December 2007										
Non-derivative financial liabilities										
Borrowings										
- fixed-rate	6.87	—	991,881	1,105,932	191,136	27,187	333,525	102,603	2,752,264	2,641,696
- variable-rate	6.54	—	806,698	305,543	1,253,697	1,786,748	1,796,872	799,039	6,748,597	5,676,245
Short-term debentures	4.03	—	—	—	520,235	—	—	—	520,235	506,213
Trade and other payables	—	651,629	820,386	201,615	576,214	—	—	—	2,249,844	2,249,844
Dividend payable	—	36	—	—	—	—	—	—	36	36

Notes:

- (1) The derivative financial instruments will be settled on a net payment/receipt is expected as at the balance sheet date, therefore, no cash flow is expected.
- (2) The contractual payments in respect of variable-rate bank and other loans are calculated based on the outstanding market rates as at the balance sheet date.

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5. CAPITAL RISK MANAGEMENT AND FINANCIAL INSTRUMENTS (continued)

b. Financial risk management objectives and policies (continued)

Fair value

The fair value of financial assets and financial liabilities are determined as follows:

- The fair value of other financial assets and financial liabilities (excluding derivative financial instruments) are determined in accordance with generally accepted pricing models based on discounted cash flow analysis or using prices from observable current market transactions; and
- The fair value of derivative financial instruments, are calculated using quoted prices. Where such prices are not available, the fair value of the non-option derivative is estimated using discounted cash flow analysis and the applicable yield curve.

Except as detailed in the following table, the directors of the Company consider that the carrying amounts of financial assets and financial liabilities recorded at amortised cost in the financial statements approximate their fair values:

	2008		2007	
	Carrying value RMB'000	Fair value RMB'000	Carrying value RMB'000	Fair value RMB'000
Borrowings - fixed rate	1,662,476	1,711,480	2,641,696	2,614,372

6. REVENUE

	2008 RMB'000	2007 RMB'000
Sale of paper products	14,561,339	13,837,756
Sale of construction materials	512,594	869,910
Sale of chemical products	88,640	92,004
Sale of electricity and steam	235,552	68,996
Others	32,785	10,209
	15,430,910	14,878,875

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7. OTHER INCOME

	2008 RMB'000	2007 RMB'000
Government grants:		
Expansion grants (note a)	178,084	102,005
Value-added tax refund (note b)	33,852	75,373
	211,936	177,378
Interest income	37,758	11,146
Net exchange gain	157,412	173,392
Net gain from sales of raw materials	21,798	63,662
Insurance compensation	12,889	7,930
Discount on acquisition of additional interests in subsidiaries (note c)	28,209	24,041
Discount on acquisition of a business (Note 36)	61	—
Payable write off	7,188	3,483
Penalty income	8,733	95
Others	14,527	1,189
	500,511	462,316

Notes:

- (a) The Group received government grants from the local municipal governments in relation to the encouragement of the development and advancement of the business of the Group. According to the relevant government grant documents, the grants are the general and unconditional subsidies for the business operations of the Group.
- (b) Pursuant to various circulars issued by the State Administration of Taxation and local government authorities, the Group is entitled to receive various types of refund on value-added tax as it has used certain designated materials in its production.
- (c) Pursuant to the transfer agreement dated 24 December 2007 entered into between the ultimate holding company of the Company, State-owned Assets Supervision and Administration Commission of Shouguang City (壽光市國有資產管理局) and the People's Government of Shouguang City (壽光市人民政府), as vendors and the Company as purchaser, the Company agreed to acquire 35.71% equity interest of a then 51% owned subsidiary, Shandong Chenming Power Supply Holdings Co., Ltd., at a consideration of RMB86,376,000. The transaction was completed in January 2008. A discount on acquisition of equity interest amounted to approximately RMB28,204,000 was recognised, after reassessment, immediately in profit or loss for the year ended 31 December 2008.

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7. OTHER INCOME (continued)

Notes: (continued)

Pursuant to the transfer agreement dated 4 April 2008 entered into between Zhang Bangji, the independent third party, as vendor and Jilin Chenming Paper Co., Ltd., a wholly-owned subsidiary of the Company ("Jilin Chenming"), as purchaser, Jilin Chenming agreed to acquire 1% equity interest of a then 99% owned subsidiary, Jilin Chenming Waste Collection Co., Ltd., a subsidiary of the Company at a cash consideration of RMB10,000. A discount on acquisition of equity interest amounted to approximately RMB5,000 was recognised, after reassessment, immediately in profit or loss for the year ended 31 December 2008.

Pursuant to the transfer agreement dated 8 October 2006 entered into between Jiangxi Paper Industry Co., Ltd, an independent third party, as vendor and the Company as purchaser, the Company agreed to acquire 3.846% equity interest of a then 47.154% owned subsidiary, Jiangxi Chenming Paper Co., Ltd ("Jiangxi Chenming"), over which, the Group already has control before the acquisition, at a consideration of RMB26,000,000. The transaction completed on 5 March 2007 upon getting the approval from the government authorities of Jiangxi Province. A discount on acquisition of interest amounted to approximately RMB22,839,000 was recognised, after reassessment, immediately in profit or loss for the year ended 31 December 2007.

Pursuant to the transfer agreement dated 1 May 2007 entered into among Wu Xiangqiang, an independent third parties and Hou Huancai, a director of the Company, as vendors and the Company as purchaser, the Company agreed to acquire 0.053% equity interest of a 99.947% then owned subsidiary, Shandong Chenming Paper Group Qihe Paperboard Co., Ltd from Wu Xiangqiang and Hou Huancai at a total consideration of RMB200,000. A discount on acquisition of interest amounted to approximately RMB257,000 was recognised, after reassessment, immediately in profit or loss for the year ended 31 December 2007.

Pursuant to the transfer agreement dated 9 May 2007 entered into between Liu Chunshan, an independent third party, as vendor and Shandong Chenming Panels Co., Ltd. ("Shandong Chenming Panels"), a subsidiary of the Company, as purchaser, Shandong Chenming Panels agreed to acquire 10% equity interest of a then 90% owned subsidiary, Shouguang Chenming Floor Board Co., Ltd at a consideration of RMB50,000. A discount on acquisition of interest amounted to approximately RMB498,000 was recognised, after reassessment, immediately in profit or loss for the year ended 31 December 2007.

Pursuant to the transfer agreement dated 10 May 2007 entered into between ten independent third parties, as vendor and Shandong Chenming Power Supply Holdings Co., Ltd, a subsidiary of the Company, as purchaser, Shandong Chenming Power Supply Holdings Co., Ltd agreed to acquire 10% equity interest in a then 90% owned subsidiary, Shouguang Chenming Cements Co., Ltd at a consideration of RMB700,000. A discount on acquisition of interest amounted to approximately RMB447,000 was recognised, after reassessment, immediately in profit or loss for the year ended 31 December 2007.

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8. FINANCE COSTS

	2008 RMB'000	2007 RMB'000
Interest expenses on:		
Bank borrowings		
- wholly repayable within five years	307,780	354,035
- not wholly repayable within five years	74,334	66,239
Convertible loan notes	—	46,653
Short-term debentures	55,812	60,685
Other borrowings		
- wholly repayable within five years	33,806	20,507
- not wholly repayable within five years	14,933	38,044
	486,665	586,163
Less: Amount capitalised under construction in progress	(24,052)	(30,470)
	462,613	555,693

Note: Borrowing costs capitalised during the year arose on the general borrowing pool and are calculated by applying a capitalisation rate of 6.72% (2007: 6.20%) to expenditure on property, plant and equipment.

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9. PROFIT BEFORE TAX

	2008 RMB'000	2007 RMB'000
Profit before taxation has been arrived at after charging (crediting):		
Wages and salaries	474,186	427,848
Staff welfare	119,450	41,466
Retirement benefit scheme contribution	58,229	55,345
Discretionary performance bonus	39	20,236
Total staff costs (including directors' emoluments)	651,904	544,895
Gross rental income from investment properties	(2,484)	(2,484)
Less: Direct operating expenses from investment properties that generated rental income during the period	446	446
Net rental income from investment properties	(2,038)	(2,038)
(Reversal of) allowance for bad and doubtful debts	(43,735)	99,868
Allowance for inventories	127,749	882
Auditors' remuneration	5,608	4,200
Cost of inventories recognised as an expenses	12,308,235	11,785,623
Release of lease payment charge	20,379	34,592
Depreciation of property, plant and equipment	1,118,083	923,309
Depreciation of investment properties	1,738	1,693
Impairment loss on property, plant and equipment	8,563	—
Impairment of interest in associates	—	540
Impairment of available-for-sale investment	549	910
Loss on disposal/write off of property, plant and equipment	1,219	9,749
Minimum operating lease payment in respect of property, plant and equipment	14,446	34,817
Repairs and maintenance expenditure on property, plant and equipment	256,701	245,530
Research and development costs	11,830	6,226
Dividend income from available-for-sale investments	(86)	—

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10. REMUNERATION OF DIRECTORS AND EMPLOYEES

(a) Directors' emoluments

Directors' emoluments paid to the directors of the Company for the year were as follows:

	2008 RMB'000	2007 RMB'000
Independent non-executive directors		
- Fees	260	250
Non-executive directors		
- Fees	120	150
Executive directors		
- Fees		
- Retirement benefits scheme contributions	154	128
- Other emoluments	4,287	8,011
	4,821	8,539

	2008 RMB'000	2007 RMB'000
Independent non-executive directors		
Diao Yuntao	40	50
Wang Zhihua	40	50
Zhou Chengjuan	40	50
Lau Yingkit	100	50
Wang Yumei	40	50
	260	250
Non-executive directors		
Gan Zhihe	40	50
Zhao Wei	40	50
Cao Chunyu	40	50
	120	150

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10. REMUNERATION OF DIRECTORS AND EMPLOYEES (continued)

(a) Directors' emoluments (continued)

	2008 RMB'000	2007 RMB'000
Executive directors		
Chen Hongguo	1,468	2,017
Yin Tongyuan	983	1,517
Li Feng	616	1,017
Xing Fangtong	221	917
Wu Bingyu	299	817
Hou Huancai	562	917
Zhou Shaohua	292	722
Liu Chengzhen (resigned on 29 April 2007)	—	61
Guo Xiucheng (resigned on 29 April 2007)	—	154
	4,441	8,139

(b) Employees

All of the five highest paid individuals of the Group during the year are directors of the Company.

During the year, no emoluments were paid by the Group to the directors of the Company and the five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office. None of the directors waived any emoluments during the year.

11. INCOME TAX EXPENSE

	2008 RMB'000	2007 RMB'000
Income tax charge comprises:		
Current income tax		
- charge for the year	319,362	313,844
- under provision in prior years	213	2,024
	319,575	315,868
Deferred tax credit (Note 30)	(23,777)	(45,073)
Charge for the year	295,798	270,795

On 26 June 2008, the Hong Kong Legislative Council passed the Revenue Bill 2008 which reduced corporate profits tax rate from 17.5% to 16.5% effective from the year of assessment 2008/2009. Therefore, Hong Kong Profits Tax is calculated at 16.5% (2007: 17.5%) of the estimated assessable profit for the year.

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11. INCOME TAX EXPENSE (continued)

PRC Enterprise Income Tax of the Group mainly comprises income tax of the Company and its subsidiaries which are calculated at rates applicable to the relevant companies for both years.

On 16 March 2007, the PRC promulgated the Law of the PRC on Enterprise Income Tax (the "New Law") by Order No. 63 of the President of the PRC. On 6 December 2007, the State Council of the PRC issued Implementation Regulation of the New Law. Under the New Law and the Implementation Regulation, the statutory Enterprise Income Tax rate is changed from 33% to 25%. The Enterprise Income Tax rate of 25% is applied to the group entities for the year ended 31 December 2008 (2007: 33%) except for certain group entities which are entitled to various concessionary tax rates.

Since the Company is a foreign investment enterprise established and operated in China's Coasted Economic Free Zone in Shandong, the income tax rate of 25% is applicable to the Company immediately on 1 January 2008 under the New Law (2007: 24%).

Pursuant to the approval of State Administration of Taxation and according to the related regulations in respect of preferential tax benefit for west development (西部大開發) issued by PRC Ministry of Foreign Trade and Economic Cooperation, for Hailaer Chenming Paper Co., Ltd. and Yanbian Chenming Paper Co., Ltd., subsidiaries of the Company, the applicable income tax rate is 15% from 2001 to 2010.

Pursuant to the approval of the local government in the year of 2002 and according to regulations issued by State of Council and State Administration of Taxation, which is applicable to foreign investment enterprise, the applicable income tax rate of Shandong Chenming Xinli Power Co., Ltd., a subsidiary of the Company, is 15%. On 26 December 2007, the State Council of the PRC issued Circular of the State Council on the Implementation of Transitional Preferential Policies for the New Law and the applicable tax rate for foreign investment enterprise is gradually phased in to the new tax rate of 25% during the five-year transitional period at a tax rate of 18%, 20%, 22%, 24% and 25% in year 2008, 2009, 2010, 2011 and 2012 respectively, therefore, the applicable tax rate for 2008 is 18% (2007: 15%).

Pursuant to the approval of the Wuhan State Tax Bureau, Wuhan Chenming Hanyang Paper Holdings Co., Ltd., a subsidiary of the Company, was changed to a foreign investment enterprise in April 2005, is exempted from paying PRC income tax for two years starting from the first profit-making year followed by a 50% reduction in income tax rate in the following three years. The year 2005 is the first profit-making year of the subsidiary. The subsidiary entitles 50% reduction in income tax rate in 2008 and the applicable income tax rate is 9% (2007: 7.5%).

Jiangxi Chenming Paper Co., Ltd. ("Jiangxi Chenming") is a foreign investment enterprise established in the PRC. Pursuant to the enterprise income tax laws applicable to foreign investment enterprise, Jiangxi Chenming is exempted from paying PRC income tax for two years starting from the first profit-making year followed by a 50% reduction in income tax rate in the following three years. The years of 2007 and 2008 are the first and second profit-making year of Jiangxi Chenming under the PRC income tax rule and accordingly, income tax have been exempted.

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11. INCOME TAX EXPENSE (continued)

	2008 RMB'000	2007 RMB'000
Profit before tax	1,590,797	1,523,379
Tax at the applicable income tax rate of 25% (2007: 24%)	397,699	365,611
Effect of tax incentives	(38,357)	(49,707)
Tax effect of income not taxable	(9,298)	(9,599)
Tax effect of expenses not deductible	18,428	12,338
Tax effect of tax losses not recognised	13,066	14,450
Effect of tax exemptions granted to certain subsidiaries	(65,397)	(62,186)
Effect of different tax rates of certain subsidiaries	(8,887)	(231)
Tax effect of utilisation of tax losses previously not recognised	(11,669)	(1,905)
Underprovision in prior years	213	2,024
Income tax expense for the year	295,798	270,795

12. DIVIDENDS

	2008 RMB'000	2007 RMB'000
Dividend declared and paid during the year for:		
- 2007 (RMB0.16 per share)	273,015	—
- 2006 (RMB0.12 per share)	—	204,760
	273,015	204,760

The final dividend in respect of the year ended 31 December 2008 of RMB0.05 cents (2007: RMB0.16 cents) per share (equivalent to approximately RMB103,102,000 (2007: RMB273,015,000)) on 2,062,046,000 shares (2007: 1,706,346,000 shares) has been proposed by the directors and is subject to approval by the shareholders in the forthcoming annual general meeting.

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13. EARNINGS PER SHARE

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

Earnings

	2008 RMB'000	2007 RMB'000
Earnings for the purpose of basic earnings per share (profit for the year attributable to equity holders of the Company)	1,102,288	994,013
Effect of dilutive potential shares:		
Interest on convertible loan notes (net of tax)	N/A	35,451
Earnings for the purpose of diluted earnings per share	N/A	1,029,464

Number of shares

	2008 '000	2007 '000
Weighted average number of shares for the purposes of basic earnings per share	1,897,802	1,611,779
Effect of dilutive potential shares:		
Convertible loan notes	N/A	94,668
Weighted average number of shares for the purpose of diluted earnings per share	N/A	1,706,447

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14. PROPERTY, PLANT AND EQUIPMENT

	Buildings	Plant and machinery	Furniture, fixtures and equipment	Motor vehicles	Construction in progress	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
COST						
At 1 January 2007	2,258,498	10,166,586	338,586	118,595	4,032,210	16,914,475
Additions	23,501	57,255	28,080	21,990	1,368,122	1,498,948
Transfers	638,061	4,039,965	8,078	145	(4,686,249)	—
Transfers to investments properties	(37,298)	—	—	—	—	(37,298)
Disposals/write offs	(10,823)	(22,495)	(2,121)	(19,481)	—	(54,920)
At 31 December 2007	2,871,939	14,241,311	372,623	121,249	714,083	18,321,205
Value-added tax refund on domestically manufactured plant and machinery	—	(13,916)	—	—	—	(13,916)
Acquisition of a business	—	—	10	—	—	10
Additions	80,040	72,451	22,592	18,292	1,463,395	1,656,770
Transfers	410,304	1,388,700	132,346	7,772	(1,939,122)	—
Disposals/write offs	(21,964)	(31,658)	(2,281)	(11,028)	—	(66,931)
At 31 December 2008	3,340,319	15,656,888	525,290	136,285	238,356	19,897,138
DEPRECIATION AND IMPAIRMENT						
At 1 January 2007	385,650	2,679,423	175,482	46,244	—	3,286,799
Provided for the year	86,998	790,112	32,902	13,297	—	923,309
Transfers to investments properties	(6,696)	—	—	—	—	(6,696)
Eliminated on disposal/write off	(5,489)	(15,242)	(1,221)	(7,473)	—	(29,425)
At 31 December 2007	460,463	3,454,293	207,163	52,068	—	4,173,987
Provided for the year	105,937	984,276	18,985	8,885	—	1,118,083
Impairment for the year	—	7,924	232	407	—	8,563
Eliminated on disposal/write off	(12,280)	(24,719)	(1,959)	(6,012)	—	(44,970)
At 31 December 2008	554,120	4,421,774	224,421	55,348	—	5,255,663
CARRYING AMOUNTS						
At 31 December 2007	2,411,476	10,787,018	165,460	69,181	714,083	14,147,218
At 31 December 2008	2,786,199	11,235,114	300,869	80,937	238,356	14,641,475

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14. PROPERTY, PLANT AND EQUIPMENT (continued)

At the balance sheet date, the Group has pledged plant and machinery and buildings having a carrying amount of approximately RMB1,144,235,000 (2007: RMB1,205,081,000) to secure the loan facilities granted to the Group by certain banks and IFC.

The Group has certain buildings with carrying amounts of approximately RMB242,268,000 (2007: RMB253,657,000), which have not yet obtained any title certificates as at the date of this report. The directors of the Company are of the opinion that the Group is not required to incur additional cost in obtaining the title certificates for these buildings in the PRC.

The above items of property, plant and equipment, other than construction in progress, are depreciated over their estimated useful lives, after taking into account their estimated residual value, on a straight line basis:

Buildings	20 - 40 years
Plant and machinery	8 - 20 years
Furniture, fixtures and equipment	5 years
Motor vehicles	5 - 8 years

According to the No. [2006]111 regulation respect of preferential VAT benefit for foreign-investment entities issued by State Administration of Taxation (國稅發[2006]111號《國家稅務總局國家發展和改革委員會關於印發《外商投資項目採購國產設備退稅管理試行辦法》的通知》) the Group received approximately RMB13,916,000 value-added tax ("VAT") refund for purchasing machinery manufactured in the PRC during the year ended 31 December 2008.

During the year ended 31 December 2008, Xiangfan Chenming Copperplate Paper Co., Ltd., a subsidiary of the Company, was deregistered. The directors of the Company conducted a review of the assets held by this subsidiary and considered that the recoverable amounts of the relevant assets, which have been determined on the basis of their fair value less cost to sell, were estimated to be less than their carrying amounts, impairment losses of approximately RMB6,767,000 was recognised during the year ended 31 December 2008.

During the year ended 31 December 2008, the directors identified that one production line of the Group will not be used in near future as its product quality is not up to standard, an impairment of approximately RMB1,796,000 was recognised for this product line.

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15. PREPAID LEASE PAYMENTS

	2008 RMB'000	2007 RMB'000
Prepaid lease payments related to		
Land use rights	1,267,565	811,560
Production facilities	—	14,997
	1,267,565	826,557
Analysed for reporting purposes as:		
Non-current portion	1,225,356	791,740
Current portion	42,209	34,817
	1,267,565	826,557

At the balance sheet date, the Group has pledged the land use rights having carrying value of approximately RMB74,654,000 (2007: RMB76,256,000) to secure the loan facilities granted to the Group.

The Group have certain land use rights with carrying amount of approximately RMB147,503,000 (2007: RMB92,099,000), which has not yet obtained the land use rights certificates as at the date of this report. The lease payments for land use rights without certificates are amortised over a period from 40 to 50 years from the date of signing the lease agreement. The directors of the Company are of the opinion that the Group is not required to incur additional cost in obtaining the land use rights certificates for these land use rights in the PRC. With reference to the lease term of other land use rights with similar usage, the directors of the Company are of the opinion that the amortisation basis is reasonable.

The lease terms of the land use rights held by the Group are between 40 and 50 years. The payment of production facilities represents prepaid rentals for production facilities leased.

During the year ended 31 December 2008, prepaid lease payment with carrying amount of RMB2,879,000 has been capitalized into biological assets.

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16. INVESTMENT PROPERTIES

	RMB'000
<hr/>	
COST	
At 1 January 2007	—
Transfer from property, plant and equipment	37,298
Additions	994
<hr/>	
At 31 December 2007 and 31 December 2008	38,292
<hr/>	
DEPRECIATION	
At 1 January 2007	—
Transfer from property, plant and equipment	6,696
Provided for the year	1,693
<hr/>	
At 31 December 2007	8,389
Provided for the year	1,738
<hr/>	
At 31 December 2008	10,127
<hr/>	
CARRYING AMOUNTS	
At 31 December 2008	28,165
<hr/>	
At 31 December 2007	29,903
<hr/>	

The fair value of the Group's investment properties at 31 December 2008 was RMB38,884,000 (2007: RMB35,732,000). The fair value have been determined by the directors of the Company and no valuation has been performed by independent qualified professional valuers. The valuation performed by the directors of the Company was arrived at by reference to recent market prices for similar properties in the same locations and conditions.

The above investment properties are situated in the PRC, held under medium-term lease and depreciated on a straight-line basis over 20 years. The properties are leased out to independent third parties since 2007.

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17. INTERESTS IN ASSOCIATES

	2008 RMB'000	2007 RMB'000
Cost of unlisted investment	100,190	80,090
Share of post-acquisition losses, net of dividend received	(32,828)	(9,660)
Less: Impairment	(540)	(540)
	66,822	69,890

Details of the Group's associates as at the balance sheet date are as follows:

Name of company	Place of establishment/ operation	Proportion of nominal value of registered capital held by the Group		Principal activities
		2008	2007	
壽光麗奔製紙有限公司 (Shouguang Liben Paper Making Co., Ltd.)	PRC	26.40%	26.40%	Manufacture of paper
青州市晨鳴變性淀粉有限責任公司 (Qingzhou Chenming Denaturation Amylum Co., Ltd.)	PRC	30.00%	30.00%	Production of denaturated amyllum
阿爾諾維根斯晨鳴特种紙有限公司 (Arjo Wiggins Chenming Specialty Paper Co., Ltd.)	PRC	30.00%	30.00%	Manufacture of paper

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17. INTERESTS IN ASSOCIATES (continued)

The summarised financial information in respect of the Group's associates is set out below:

	2008 RMB'000	2007 RMB'000
Total assets	618,885	556,556
Total liabilities	386,117	319,481
Net assets	232,768	237,075
Group's share of net assets of associates	66,822	69,890
Revenue	272,381	98,041
Loss for the year	(79,033)	(31,925)
Group's share of loss of associates for the year	(23,168)	(9,462)

18. AVAILABLE-FOR-SALE INVESTMENTS

	2008 RMB'000	2007 RMB'000
Unlisted equity securities, at cost	28,652	28,652
Less: impairment	(2,801)	(2,252)
Carrying value at the balance sheet date	25,851	26,400

Available-for-sale investments comprise unlisted equity investments in certain companies established in the PRC, in which the Group holds less than 20% of their paid-up capital. They are measured at cost less impairment at each balance sheet date because the range of reasonable fair value estimates is so significant that the directors of the Company are of the opinion that their fair values cannot be measured reliably.

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19. GOODWILL

The goodwill of the Group arose from the acquisition of the remaining equity interest hold by minority shareholders of subsidiaries.

During the year ended 31 December 2008, the management of the Group assessed the recoverable amounts of goodwill to determine if there was any impairment of goodwill of the cash generating units ("CGUs") by reference to the CGUs' value in use.

The recoverable amounts of the CGUs are determined based on value in use calculations which uses cash flow projections derived from the financial budgets for the next five years prepared by the management using the discount rate of 5.47% (2007: 9.54%) per annum which reflect the current market assessment of the time value of money and the risks specific to the CGUs and using steady growth rates range from 5% to 10% (2007: range from 10% to 15%) per annum. The growth rates are based on the industry growth forecast and do not exceed the average long-term growth rate for the relevant industry.

Management believes that any reasonably possible change in any of these assumptions would not cause the aggregate carrying amount to exceed the aggregate recoverable amount of goodwill.

20. BIOLOGICAL ASSETS

	2008 RMB'000	2007 RMB'000
CARRYING AMOUNT		
At beginning of the year	92,160	19,514
Plantation expenditure incurred	208,135	48,231
Gain on change in fair value less estimated point-of-sale cost of biological assets	918	24,415
At end of the year	301,213	92,160

Biological assets represent immature trees in the plantation forest purchased since end of 2006 to be grown for lumber for own use.

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20. BIOLOGICAL ASSETS (continued)

The biological assets are stated at their fair values less estimated point-of-sale costs. The fair value has been arrived at based on a valuation carried out by Jones Lang LaSalle Sallmanns which has appropriate qualifications and recent experiences in the valuation of similar assets. The valuation, which conforms to International Valuation Standards, is determined using the discounted value of the expected delivered market price for estimated timber volumes less cost of delivery and estimated maintenance costs up to when the timber becomes usable. The discount rate used is the applicable pre-tax weighted average cost of capital of the Group. Accordingly, gain on change in fair value less estimated point-of-sale cost of biological assets amounted to RMB918,000 (2007: RMB24,415,000) has been recognised and credited to the consolidated income statement for the year ended 31 December 2008.

21. INVENTORIES

	2008 RMB'000	2007 RMB'000
Raw materials	1,579,741	1,113,790
Work in progress	73,197	72,508
Finished goods		
Paper products	1,632,059	489,379
Construction materials	110,937	35,475
Chemical materials	1,859	33,341
	3,397,793	1,744,493

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22. TRADE AND OTHER RECEIVABLES

	2008 RMB'000	2007 RMB'000
Trade receivables	1,919,637	1,879,327
Less: Impairment	(167,228)	(219,306)
	1,752,409	1,660,021
Other receivables	312,341	255,568
Less: Impairment	(51,546)	(59,406)
	260,795	196,162
Bills receivable	974,010	1,676,684
Advance to suppliers, deposits and prepayments	462,526	574,015
Trade and other receivables	3,449,740	4,106,882

Trade receivables

The Group allows an average credit period of 90 days to its trade customers, except for certain customers with credit period more than 90 days. The following is an aged analysis of trade receivables net of impairment at the reporting date:

	2008 RMB'000	2007 RMB'000
0 - 90 days	1,365,834	1,295,048
91 - 180 days	240,387	265,222
181 - 365 days	104,987	54,812
1 - 2 years	27,306	40,301
2 - 3 years	13,895	4,638
	1,752,409	1,660,021

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22. TRADE AND OTHER RECEIVABLES (continued)

Trade receivables (continued)

The following is an aged analysis of bill receivable at the report date:

	2008 RMB'000	2007 RMB'000
0 - 90 days	802,843	1,243,096
91 - 180 days	171,167	433,588
	974,010	1,676,684

Before accepting any new customer, the Group goes through internal credit assessment procedure to assess the potential customer's credit quality and defines credit limits by customer.

Aging of amounts past due but not impaired trade receivables:

	2008 RMB'000	2007 RMB'000
0 - 90 days	224,355	63,605
91 - 180 days	11,627	15,388
181 - 365 days	104,987	54,812
1 - 2 years	27,306	40,301
2 - 3 years	13,895	4,638
Total	382,170	178,744

Included in trade receivables balance of the Group is a debtor with amount of RMB92,563,000 (2007: RMB119,458,000) as at 31 December 2008, which is individually determined to be impaired. As the debtor has delayed payment on several occasions, the Group lodged lawsuit against the debtor and a building with estimated value amounting to RMB15,844,000 was pledged to the Group. The Group has provided impairment of RMB48,799,000 (2007: RMB88,518,000) as at 31 December 2008, after taking into account the subsequent settlement received from this debtors and the fair value of the building pledged to the Group.

The Group has provided full impairment on certain receivables past due over 3 years based on past experience of which receivables that are past due beyond 3 years are generally not recoverable. Other than the recognised impairment losses, no allowance has been made to the remaining past due trade receivables as the Group is satisfied with the subsequent settlement from and the credit quality of these customers and the Group considers that these balances are not impaired. The directors of the Company are of the opinion that the credit quality of the trade receivable balances that are neither past due or impaired at each balance sheet date is of good quality.

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22. TRADE AND OTHER RECEIVABLES (continued)

Aging of amounts past due but not impaired trade receivables: (continued)

Except for the building pledged to the Group as disclosed above, no other collateral was held by the Group as the balance sheet date.

Other receivables

Other receivables are non-trade nature balances due from third parties and they are unsecured, interest-free and repayable on demand.

Included in other receivables balance of the Group is a consideration of RMB86,376,000 which is acquisition of minority interest of Shandong Chenming Power Supply Holdings Co., Ltd. at 31 December 2007.

Movement in the impairment on trade receivables

	2008 RMB'000	2007 RMB'000
Balance at beginning of the year	219,306	155,979
Impairment losses recognised on receivables	15,072	145,118
Amounts recovered during the year	(56,577)	(47,779)
Write off	(10,573)	(34,012)
Balance at end of the year	167,228	219,306

Movement in the impairment on other receivables

	2008 RMB'000	2007 RMB'000
Balance at beginning of the year	59,406	56,877
Impairment losses recognised on receivables	10,259	45,649
Amounts recovered during the year	(12,489)	(43,120)
Write off	(5,630)	—
Balance at end of the year	51,546	59,406

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23. DERIVATIVE FINANCIAL INSTRUMENTS

	2008 RMB'000	2007 RMB'000
Foreign currency forward contracts	(199)	5,955

At 31 December 2008 and 2007, the outstanding foreign exchange forward contracts committed by the Group are as follows:

2008

Notional amount	Maturity	Exchange rates RMB/USD	RMB'000
Sell USD 3,000,000	22 January 2009	6.7687	20,306

2007

Notional amount	Maturity	Exchange rates RMB/USD	RMB'000
Sell USD 3,000,000	22-25 March 2008	7.2304	21,691
Sell USD 3,000,000	24 April 2008	7.5344	22,603
Sell USD 4,000,000	20-25 August 2008	7.1062	28,425
Sell USD 4,000,000	22-25 September 2008	7.0760	28,304
Sell USD 4,000,000	20-24 October 2008	7.0496	28,198
Sell USD 3,000,000	24 January 2008	7.4296	22,289
Sell USD 2,000,000	17 March 2008	7.2775	14,555
Sell USD 2,000,000	15 April 2008	7.2446	14,489
Sell USD 2,000,000	15 May 2008	7.2106	14,421
Sell USD 3,000,000	23 May 2008	7.1656	21,497
Sell USD 2,000,000	15 July 2008	7.1393	14,279
Sell USD 2,000,000	15 August 2008	7.1031	14,206
			244,957

The total fair value of the Group's currency derivatives financial liabilities as at 31 December 2008 are estimated to be approximately RMB199,000 (2007: derivatives financial assets of RMB5,955,000), which are based on fair value provided by counter parties which are financial institutions. As the currency derivatives are not designated as cash flow hedges, the change in fair values amounting to RMB1,738,000 (2007: RMB5,955,000) has been credited to the consolidated income statement for the year.

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24. RESTRICTED BANK DEPOSITS/BANK BALANCES AND CASH

Restricted bank deposits represent the bank deposits pledged to banks to secure certain bills facilities granted to the Group by certain banks amounting to RMB165,839,000 (2007: RMB126,795,000) and are therefore classified as current assets. The restricted bank deposits carry fixed interest rate of 0.36% (2007: 0.72%) per annum as at 31 December 2008. The pledged bank deposits will be released upon the settlement of relevant bill facilities.

Bank balances and cash held by the Group include bank balances and short-term deposits with an original maturity of three months to six months, which carry interests at market rates which ranging from 0.36% to 3.33% (2007: 0.72% to 4.14%) per annum as at 31 December 2008.

25. TRADE AND OTHER PAYABLES

	2008 RMB'000	2007 RMB'000
Trade payables aged:		
0 - 90 days	2,001,600	1,078,946
91 - 180 days	275,863	235,542
181 - 365 days	216,240	218,859
1 - 2 years	98,420	88,004
2 - 3 years	17,648	19,819
Over 3 years	32,537	15,537
Trade payables	2,642,308	1,656,707
Bills payable aged:		
0-90 days	252,629	127,316
91-180 days	114,999	2,740
Bills payable	367,628	130,056
Other payables	506,114	463,081
Advances received from customers	101,694	170,287
Accrued charges	52,927	65,476
	3,670,671	2,485,607

The average credit period on purchases of goods is 90 days.

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26. BORROWINGS

	2008 RMB'000	2007 RMB'000
Bank loans		
Secured	1,356,920	1,514,813
Unsecured	4,703,656	6,266,583
	6,060,576	7,781,396
Other loans		
Secured, from IFC	214,153	272,705
Unsecured	299,592	263,840
	513,745	536,545
	6,574,321	8,317,941
Bank and other loans are repayable:		
Within one year	2,555,070	4,261,746
In the second year	365,446	1,617,931
In the third to fifth year inclusive	3,502,164	1,864,543
More than five years	151,641	573,721
	6,574,321	8,317,941
Less: Amount due within one year shown under current liabilities	(2,555,070)	(4,261,746)
Amount due after one year	4,019,251	4,056,195

Details of the terms of the Group's borrowings are set out below:

	Maturity date	Effective interest rate per annum		Carrying amount	
		2008 %	2007 %	2008 RMB'000	2007 RMB'000
Fixed-rate borrowings	2009 to 2013	4.68	6.87	1,662,476	2,641,696
Floating-rate borrowings	2009 to 2023	4.97	6.54	4,911,845	5,676,245
Total borrowings				6,574,321	8,317,941

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27. SHORT-TERM DEBENTURES

- (a) Pursuant to a circular [2007] No. 289 issued by the People's Bank of China in 2007, Jiangxi Chenming issued a debenture with face value of RMB500,000,000 on 11 September 2007. The debenture is unsecured, interest bearing at 4.03% per annum, and repayable one year after the issue date. The debenture was fully repaid in 2008.
- (b) Pursuant to a circular [2007] No. 427 issued by the People's Bank of China in 2007, the Company issued two debentures to third party debenture holders with face value of RMB700,000,000 and RMB1,200,000,000 on 6 June 2008 and 29 August 2008 respectively. The debentures are unsecured, bear interest at 5.2% per annum and will be repayable one year after the issue date.

28. PROVISION

The amount represents that provision made in relation to a claim from one of its contractors about the dispute in payment of the construction work performed for a production plant of the Group in 2004. Full provision has been made by the Group in respect of the claim and the claim is still in progress up to the date of this report.

29. DEFERRED INCOME

	2008 RMB'000	2007 RMB'000
At beginning of the year	303,712	336,394
Grants obtained	57,823	—
Released to income	(32,068)	(32,682)
At end of the year	329,467	303,712
Analysed for the reporting purpose as:		
Current portion	21,598	32,682
Non-current portion	307,869	271,030
Total	329,467	303,712

Government grants obtained during the year are in relation to the construction of property, plant and equipment of the Group from the local municipal governments.

The grants were recorded as deferred income in the balance sheet and credited to the income statement on a straight-line basis over the expected useful lives of the related assets. In accordance with the terms of the grants, the amount attributable to the Group of approximately RMB18,061,000 (2007: RMB32,682,000) were transferred from retained earnings to capital reserve during the year as the relevant amount cannot be distributed before winding up.

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30. DEFERRED TAXATION

The following are the major deferred tax liabilities recognised and movements thereon during the current and prior years:

	Impairment loss on assets RMB'000	Convertible loan notes RMB'000	Deferred income RMB'000	Salaries and wages accruals RMB'000	Tax losses RMB'000	Biological assets RMB'000	Others RMB'000	Total RMB'000
At 1 January 2007	48,027	(25,258)	—	10,512	1,367	—	3,481	38,129
Effect on change in tax rate	2,001	(1,052)	—	438	57	—	145	1,589
Credit (charge) to income for the year	26,033	12,254	—	7,329	344	(6,104)	3,628	43,484
Credit to equity for the year	—	14,056	—	—	—	—	—	14,056
At 31 December 2007	76,061	—	—	18,279	1,768	(6,104)	7,254	97,258
Acquisition of subsidiaries	449	—	—	—	—	—	—	449
(Charge) credit to income for the year	(3,477)	—	8,522	4,476	9,279	(328)	5,305	23,777
At 31 December 2008	73,033	—	8,522	22,755	11,047	(6,432)	12,559	121,484

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30. DEFERRED TAXATION (continued)

For the purpose of balance sheet presentation, certain deferred tax assets and liabilities have been offset. The following is the analysis of the deferred tax balances for financial reporting purposes:

	2008 RMB'000	2007 RMB'000
Deferred tax assets	127,916	103,362
Deferred tax liabilities	(6,432)	(6,104)
	121,484	97,258

At the balance sheet date, the Group has unused tax losses of RMB216,222,000 (2007: RMB183,814,000) available for offset against future profits.

Deferred tax assets are recognised for tax losses carried forward to the extent that the realisation of the related tax benefit through the future taxable profits is probable. A deferred tax asset has been recognised in respect of RMB44,188,000 (2007: RMB7,073,000) of tax losses arising from PRC Enterprise Income Tax.

The Group did not recognise deferred income tax assets in respect of the remaining tax losses amounting to RMB172,034,000 (2007: RMB176,741,000) as the future profit stream of the subsidiaries are uncertain. The remaining tax losses arising from PRC Enterprise Income Tax can be carried forward to offset against future taxable income in year 2009 to 2013.

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31. SHARE CAPITAL

	Number of shares '000	Restricted A Shares '000	Type of shares			Total RMB'000
			A Shares '000	B Shares '000	H Shares '000	
At 1 January 2007	1,365,670	354,809	453,364	557,497	—	1,365,670
Shares issued upon conversion of convertible loan notes	340,676	—	340,676	—	—	340,676
Transfer of restricted A Shares held by PRC legal persons to A shares	—	(9,517)	9,517	—	—	—
Transfer of A shares held by directors, supervisors and senior management to restricted A Shares	—	17	(17)	—	—	—
Transfer of restricted A Shares held by directors, supervisors and senior management to A shares	—	(5,808)	5,808	—	—	—
At 31 December 2007	1,706,346	339,501	809,348	557,497	—	1,706,346
Issue of H Shares (note a)	355,700	—	—	—	355,700	355,700
Transfer of A Shares to H shares (note b)	—	(35,570)	—	—	35,570	—
Transfer of A shares held by directors, supervisors and senior management to restricted A Shares(note c)	—	177	(177)	—	—	—
Transfer of restricted A Shares held by directors, supervisors and senior management to A Shares (note d)	—	(120)	120	—	—	—
At 31 December 2008	2,062,046	303,988	809,291	557,497	391,270	2,062,046

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31. SHARE CAPITAL (continued)

Notes:

- (a) On 18 June 2008, 355,700,000 H Shares of the Company of RMB1.00 each were issued at HK\$9.00 per share for cash by way of an international offering and a public offering on the Stock Exchange.
- (b) In accordance with relevant approval document regarding the listing of shares of the company outside the PRC, Shouguang Chenming Holdings Co.,Ltd., the parent company of the Company is required to transfer 35,570,000 A Shares to 中華人民共和國全國社會保障基金理事會The National Social Security Fund Council of the PRC ("NSSF Council") upon the listing of H Shares of the Company on the Stock Exchange, and all the shares held by NSSF Council were converted into H Shares on an one-for-one basis.
- (c) During the year ended 31 December 2008, acquired 176,774 A Shares from the public, as the transfer of entity's shares held by the directors and key management of an entity are restricted under the relevant requirement of the Shenzhen Stock Exchange, these shares were reclassified from A Shares to Restricted A shares accordingly.
- (d) Lock-up period for certain restricted A Shares held by certain directors and key management of the Company was expired during the period, 120,000 restricted A Shares were reclassified from Restricted A Shares to A Shares.
- (e) All shares rank pari passu in all other material aspects.

32. COMMITMENTS

	2008 RMB'000	2007 RMB'000
Contracted but not provided for acquisition of property, plant and equipment	291,332	362,388

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33. LEASE COMMITMENTS

The Group as lessee

At the balance sheet date, the Group had commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

	Rented premises RMB'000	Rented land for plantation RMB'000	Total RMB'000
Year ended 31 December 2008			
Within one year	10,567	38,710	49,277
In the second to fifth year inclusive	17,367	9,989	27,356
After five years	39	56,151	56,190
	27,973	104,850	132,823
Year ended 31 December 2007			
Within one year	9,113	6,632	15,745
In the second to fifth year inclusive	17,351	8,924	26,275
After five years	1,718	36,358	38,076
	28,182	51,914	80,096

Leases are negotiated for an average term of six years and rentals are fixed at the date of signing of lease agreements.

The Group as lessor

The Group's investment properties are held for rental purposes. The properties are expected to generate rental yields of 12.04% (2007: 8.31%) on an ongoing basis. All of the properties held have committed tenants for an average term of one year.

At the balance sheet date, the Group had contracted with tenants for the following future minimum lease payments:

	2008 RMB'000	2007 RMB'000
Within one year	1,436	1,407
In the second year	—	1,561
	1,436	2,968

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34. RELATED PARTY TRANSACTIONS

- (a) Besides the acquisition of additional equity interest of Shandong Chenming Power Supply Holdings Co., Ltd. as disclosed in Note 7(c), the Group has entered into the following significant transactions with its related parties during the year:

	2008 RMB'000	2007 RMB'000
<i>Associates:</i>		
Electricity charges received	22,742	7,332
Utility charges received	10,312	—
Miscellaneous service charges received	9,755	248
Rental received	150	—
<i>Minority shareholders of subsidiaries:</i>		
Sales of finished products	202,545	313,993
Technology consultancy fee paid	1,625	1,500
Interest paid	14,933	22,054
Minimum operating lease payment in respect of property, plant and equipment	6,960	7,166

Other than the above transactions, the Group also settled or received on behalf of certain related parties during the year and the unsettled balance is included in the balance with the respective related parties as at the balance sheet date.

- (b) Balances with related parties (included in respective items on the balance sheet)

	2008 RMB'000	2007 RMB'000
<i>Associates:</i>		
Other receivables	14,679	14,824
Trade receivables	10,744	—
Trade payables	—	176
<i>Minority shareholders of subsidiaries:</i>		
Trade receivable	18,354	—
Other loans from IFC	214,153	272,705

All the amounts due from (to) associates and minority shareholders of subsidiaries are unsecured, interest-free and expected to be recovered/repaid within one year from the balance sheet date, except for part of the loans from IFC, which are repayable after one year from the balance sheet date.

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34. RELATED PARTY TRANSACTIONS (continued)

(c) Material transactions and balances with other stated-owned enterprises in the PRC

The Group operates in an economic environment currently predominated by enterprises directly or indirectly owned or controlled by the PRC government (hereinafter collectively referred to as "State-owned Enterprises"). During the year, the Group had material transactions with some of these State-owned Enterprises in its ordinary and usual course of business. In establishing its pricing strategies and approval process for its products, the Group does not differentiate whether the counter-party is a State-owned Enterprise or not. While the directors of the Company consider the State-owned Enterprises are independent third parties so far as the Group's business transactions with them are concerned, for the purpose of this report, the Group has identified the nature and quantified the amounts of its significant transactions with State-owned Enterprises during the year as follows:

(i) Material transactions

	2008 RMB'000	2007 RMB'000
Sales	5,098,665	3,859,814
Purchases	468,331	837,689
Construction works expenses paid	18,354	81,846

(ii) Material balances

	2008 RMB'000	2007 RMB'000
Bank balances and deposits	2,484,732	512,856
Trade and other receivables	823,004	994,266
Trade and other payables	552,004	279,712
Borrowings	6,284,920	7,985,080

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34. RELATED PARTY TRANSACTIONS (continued)

(d) Compensation of key management personnel

The remuneration of directors and other members of senior management during the year was as follows:

	2008 RMB'000	2007 RMB'000
Short-term employee benefits		
- Directors	4,667	8,411
- Other senior management	3,322	5,420
Subtotal	7,989	13,831
Post-employment benefits		
- Directors	154	128
- Other senior management	327	269
Subtotal	481	397
Total	8,470	14,228

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35. SEGMENT INFORMATION

(a) Business segments

For management purposes, the Group is currently divided into the following operating division: paper products, construction materials, chemical products, electricity and steam and others.

The manufacture and sales of paper products accounted for over 90% of the segment revenue, results and assets of the Group during the year. Accordingly, no individual business segment analysis is presented and the consolidated segment information is presented as follow:

An analysis of the Group's revenue and contribution by business segment during the year is as follows:

	2008 RMB'000	2007 RMB'000
Segment result	2,080,026	1,637,062
Unallocated corporate expenses	(213,412)	(33,284)
Unallocated corporate income	207,308	454,386
Share of result of associates	(23,168)	(9,462)
Gain on change in fair value of derivative financial instruments	1,738	5,955
Gain on change in fair value less estimated point-of-sale cost of biological assets	918	24,415
Finance costs	(462,613)	(555,693)
Profit before tax	1,590,797	1,523,379
Income tax expenses	(295,798)	(270,795)
Profit for the year	1,294,999	1,252,584

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35. SEGMENT INFORMATION (continued)

(a) Business segments (continued)

An analysis of the Group's total assets and liabilities by business segment is as follows:

BALANCE SHEET

	2008 RMB'000	2007 RMB'000
ASSETS		
Segment assets	22,847,987	20,615,064
Unallocated corporate assets	3,359,343	1,298,661
Consolidated total assets	26,207,330	21,913,725
LIABILITIES		
Segment liabilities	3,705,925	2,278,749
Unallocated corporate liabilities	8,844,436	9,454,680
Consolidated total liabilities	12,550,361	11,733,429

OTHER INFORMATION

	2008 RMB'000	2007 RMB'000
Capital additions	2,134,665	1,498,948
Depreciation of property, plant and equipment	1,118,083	923,309
Depreciation of investment properties	1,738	1,693
Release of lease payment charge	20,379	34,592
Impairment of property, plant and equipment	8,563	—
(Reverse of) allowance for bad and doubtful debts	(43,735)	99,868
Loss on disposal of property, plant and equipment	1,219	9,749
Allowance for inventories	127,749	882
Impairment of available-for-sale investment	549	910

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35. SEGMENT INFORMATION (continued)

(b) Geographical segment

The Group's operations are located in the PRC only and sales are made to customers in the PRC and overseas.

The following table provides an analysis of the Group's revenue by geographical market that are based on location of customers.

	2008 RMB'000	2007 RMB'000
PRC	13,502,030	12,573,625
South Africa	236,460	292,530
Hong Kong	207,130	303,261
Japan	146,670	334,189
United States	49,658	250,063
Others	1,288,962	1,125,207
	15,430,910	14,878,875

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36. ACQUISITION OF SUBSIDIARIES

(a) Acquisition of a business

In December 2008, Shouguang Chenming Modern Logistic Co., Ltd., a subsidiary of the Company, which is engaged in goods transportation, acquired the assets and liabilities in relation to the business of reclamation of waste paper in Shouguang City from Shouguang Runsheng Waste Collection Co., Ltd at a cash consideration of RMB1,000,000, which has not yet been paid as at year ended 31 December 2008. The fair value of assets and liabilities, the amounts of which are approximately to the carrying values immediate before acquisition, acquired is set out as follows:

	RMB'000
Property, plant and equipment	10
Deferred tax assets	449
Inventories	2,113
Trade and other receivables	17,468
Cash and cash equivalents	506
Trade and other payables	(19,485)
	1,061
Discount on acquisition	(61)
Total consideration, satisfied by payable and included in other payables	1,000
Net cash inflow arising on acquisition:	
Cash consideration paid	—
Cash and cash equivalents acquired	506
	506

The business acquired contributed a loss of RMB6,561,000 to the Group for the period between the date of acquisition and the balance sheet date. No revenue was contributed to the Group during the period as its revenue solely comes from the Group before the acquisition.

If the above acquisitions had been completed on 1 January 2008, the group revenue for the year ended 31 December 2008 would have been RMB15,430,910,000 and profit for the year ended 31 December 2008 would have been by RMB1,289,149,000. The proforma information is for illustrative purposes only and is not necessarily an indicative revenue and results of operations of the Group that actually would have been achieved had the acquisition been completed on 1 January 2008, nor is it intended to be a projection of future results.

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36. ACQUISITION OF SUBSIDIARIES (continued)

(b) Acquisition of assets

In June 2008, Fuyu Chenming Paper Co., Ltd., a subsidiary of the Company, which is engaged in manufacture of paper, acquired the assets and liabilities in relation to the business of trading of paper in Wuxi City from Wuxi Songling Paper Co., Ltd. at a cash consideration of RMB Nil. The abovementioned transaction is the business of assets acquisition. The difference between the consideration of the acquisition and the carrying value is recognized as the cost of property, plant and equipment. The fair value of assets and liabilities, the amounts of which are approximately to the carrying value immediate before acquisition, acquired is set out as follows:

	RMB'000
Property, plant and equipment	3,856
Prepaid lease payments	1,368
Trade and other receivables	3
Cash and cash equivalents	40
Trade and other payables	(5,267)
	—
Total consideration paid	—
Net cash inflow arising on acquisition:	
Cash consideration paid	—
Cash and cash equivalents acquired	40
	40

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37. POST BALANCE SHEET EVENTS

The following events occurred subsequent to 31 December 2008:

- (1) To reduce the finance costs of the Company and optimize its financing structure, the Board resolved to issue medium-term notes of not more than RMB 2.3 billion due to the interest rate of medium-term notes being lower than the best lending rate for a loan of same term offered by the banks with the benefits of a flexible issuing mechanism, high transparency and low issuing cost and risks. The proceeds from issuance of medium-term notes will be used to fund working capital and repay bank borrowings.

The term of medium-term notes is three to five years, and there is no guarantee provided by the Company. The interest rate is to be determined according to the market conditions prevailing at the time of issue, but in no event higher than the best rate for bank loans quoted by the People's Bank of China for the corresponding period.

- (2) The resolution regarding the grant of a general mandate to the Board to repurchase H shares of the Company was considered and approved by the Board. This resolution is pending for the approval at a shareholders' meeting.

That the Board and Mr. Chen Hongguo, the chairman of the Board (the "Chairman"), authorized by, and on behalf of, the Board, be authorized to repurchase H Shares under a general mandate. And the aggregate nominal amount of which shall not exceed 10% of the aggregate nominal value of H Shares in issue of the Company as at the time of passing of the relevant resolution at a shareholders' meeting.

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38. PARTICULARS OF SUBSIDIARIES

Name of company	Place of incorporation/ registration and operation	Issued and fully paid/ paid-in capital	Attributable equity interest held by the Company at 31 December 2008				Principal activity
			Directly held		Indirectly held		
			2008	2007	2008	2007	
山東晨鳴熱電股份有限公司 (Shandong Chenming Power Supply Holdings Co., Ltd.)	PRC	RMB99,553,061	86.71%	51.00%	—	—	Investment holding
武漢晨鳴漢陽紙業股份有限公司 (note) (Wuhan Chenming Hanyang Paper Holdings Co., Ltd.)	PRC	RMB211,367,000	50.93%	50.93%	—	—	Manufacture of paper
海拉爾晨鳴紙業有限責任公司 (Hailaer Chenming Paper Co., Ltd.)	PRC	RMB16,000,000	75.00%	75.00%	—	—	Manufacture of paper
山東晨鳴紙業集團齊河 板紙有限責任公司 (Shandong Chenming Paper Group Qihe Paperboard Co., Ltd.)	PRC	RMB376,200,000	100.00%	100.00%	—	—	Manufacture of paper
赤壁晨鳴紙業有限公司 (Chibi Chenming Paper Co., Ltd.)	PRC	RMB177,419,400	20.00%	20.00%	31.00%	31.00%	Manufacture of paper
延邊晨鳴紙業有限責任公司 (Yanbian Chenming Paper Co., Ltd.)	PRC	RMB81,633,000	76.73%	76.73%	—	—	Manufacture of paper pulp and chemical products
壽光市晨鳴天園林業有限責任公司 (Shouguang Chenming Tianyuan Arboriculture Co., Ltd.)	PRC	RMB10,586,700	68.00%	68.00%	—	—	Arboriculture of tree
江西晨鳴紙業有限責任公司 (note) (Jiangxi Chenming Paper Co., Ltd.)	PRC	USD172,000,000	51.00%	51.00%	—	—	Manufacture of paper
鄧城晨鳴板材有限公司 (Juancheng Chenming Panels Co., Ltd.)	PRC	RMB15,000,000	100.00%	100.00%	—	—	Manufacture of paper

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38. PARTICULARS OF SUBSIDIARIES (continued)

Name of company	Place of incorporation/ registration and operation	Issued and fully paid/ paid-in capital	Attributable equity interest held by the Company at 31 December 2008				Principal activity
			Directly held		Indirectly held		
			2008	2007	2008	2007	
山東御景大酒店有限公司 (note) (Shandong Grand View Hotel Co., Ltd.)	PRC	USD13,905,700	70.00%	70.00%	—	—	Development of a hotel project
吉林晨鳴紙業有限責任公司 (Jilin Chenming Paper Co., Ltd.)	PRC	RMB1,500,000,000	100.00%	100.00%	—	—	Manufacture of paper
湛江晨鳴漿紙有限公司 (Zhanjiang Chenming Paper Pulp Co., Ltd.)	PRC	RMB500,000,000	100.00%	100.00%	—	—	Production of paper pulp
晨鳴(香港)有限公司 (Chenming (HK) Limited)	Hong Kong	USD100,000	100.00%	100.00%	—	—	Trading of paper
壽光晨鳴現代物流有限公司 (Shouguang Chenming Modern Logistic Co., Ltd.)	PRC	RMB10,000,000	100.00%	100.00%	—	—	Goods transportation
富裕晨鳴紙業有限責任公司 (Fuyu Chenming Paper Co., Ltd.)	PRC	RMB208,000,000	100.00%	100.00%	—	—	Manufacture of paper
壽光晨鳴美術紙有限公司 (note) (Shouguang Chenming Art Paper Co., Ltd.)	PRC	RMB20,000,000	75.00%	75.00%	—	—	Manufacture of paper
黃岡林業發展有限責任公司 (Huanggang Chenming Arboriculture Co., Ltd.)	PRC	RMB10,000,000	100.00%	—	—	—	Arboriculture of tree
黃岡晨鳴漿紙有限公司 (Huanggang Chenming Paper Pulp Co., Ltd.)	PRC	RMB20,000,000	100.00%	—	—	—	Production of paper pulp
咸寧晨鳴林業發展有限責任公司 (Xianning Chenming Arboriculture Co., Ltd.)	PRC	RMB10,000,000	100.00%	—	—	—	Arboriculture of tree

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38. PARTICULARS OF SUBSIDIARIES (continued)

Name of company	Place of incorporation/ registration and operation	Issued and fully paid/ paid-in capital	Attributable equity interest held by the Company at 31 December 2008				Principal activity
			Directly held		Indirectly held		
			2008	2007	2008	2007	
山東晨鳴新力熱電有限公司 (note) (Shandong Chenming Xinli Power Co., Ltd.)	PRC	USD11,800,000	—	—	51.00%	51.00%	Generation of electricity
武漢晨鳴乾能熱電有限責任公司 (Wuhan Chenming Qianneng Electric Power Co., Ltd.)	PRC	RMB88,235,000	—	—	51.00%	51.00%	Generation of electricity
壽光市晨鳴水泥有限公司 (Shouguan Chenming Cement Co., Ltd.)	PRC	RMB7,000,000	—	—	100.00%	100.00%	Manufacture of cement
山東晨鳴板材有限責任公司 (Shandong Chenming Panels Co., Ltd.)	PRC	RMB30,000,000	—	—	100.00%	100.00%	Manufacture of decorating materials
武漢晨建新型牆體材料有限公司 (Wuhan Chenjian New-style Wall Materials Co., Ltd.)	PRC	RMB10,000,000	—	—	51.00%	51.00%	Manufacture of construction materials
齊河晨鳴廢舊物質收購有限公司 (Qihe Chenming Waste Collection Co., Ltd.)	PRC	RMB500,000	—	—	98.00%	98.00%	Collection, processing and sale of waste paper and paper products
菏澤晨鳴板材有限責任公司 (Heze Chenming Panels Co., Ltd.)	PRC	RMB30,000,000	—	—	67.00%	67.00%	Manufacture of decorating materials
齊河晨鳴板材有限公司 (Qihe Chenming Panels Co., Ltd.)	PRC	RMB40,820,000	—	—	100.00%	100.00%	Manufacture of decorating materials
壽光晨鳴地板有限責任公司 (Shouguang Chenming Floor Board Co., Ltd.)	PRC	RMB500,000	—	—	100.00%	100.00%	Manufacture of floor board

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38. PARTICULARS OF SUBSIDIARIES (continued)

Name of company	Place of incorporation/ registration and operation	Issued and fully paid/ paid-in capital	Attributable equity interest held by the Company at 31 December 2008				Principal activity
			Directly held		Indirectly held		
			2008	2007	2008	2007	
吉林晨鳴廢舊物資回收有限公司 (Jilin Chenming Waste Collection Co., Ltd.)	PRC	RMB1,000,000	—	—	100.00%	99.00%	Collection of waste paper and paper products
湛江晨鳴林業發展有限公司 (Zhanjiang Chenming Arboriculture Co., Ltd.)	PRC	RMB1,000,000	—	—	100.00%	100.00%	Arboriculture of tree
陽江晨鳴林業發展有限公司 (Yangjiang Chenming Arboriculture Co., Ltd.)	PRC	RMB1,000,000	—	—	100.00%	100.00%	Arboriculture of tree
吉林市晨鳴機械制造有限公司 (Jilin Chenming Machinery Manufacturing Co., Ltd.)	PRC	RMB600,000	—	—	100.00%	100.00%	Not yet commenced business
南昌晨鳴林業發展有限公司 (Nanchang Chenming Arboriculture Co., Ltd.)	PRC	RMB1,000,000	—	—	100.00%	100.00%	Arboriculture of tree
無錫松嶺紙業有限公司 (Wuxi Songling Paper Co., Ltd.)	PRC	RMB5,010,000	—	—	100.00%	—	Trading of paper
壽光潤生廢紙回收有限責任公司 (Shouguang Runsheng Waste Collection Co., Ltd.)	PRC	RMB1,000,000	—	—	100.00%	—	Reclamation of waste paper

Note: Except for these subsidiaries, which are Sino-foreign equity joint venture companies, all subsidiaries of the Company established in the PRC are PRC limited liability companies.

None of the subsidiaries had issued any debt securities at the year ended 31 December 2008 or at any time during the year.

XIII Documents Available for Inspection

1. They include the financial statements which is signed and sealed by the legal representative, financial controller and head of the financial department of the Company.
2. They include the original copy of the auditors' report which is sealed by the accounting firm and signed by the certified public accountant.
3. They include the original copies of all of the documents and announcements of the Company which have been disclosed in the designated newspaper and website as approved by China Securities Regulatory Commission during the reporting period.

Shandong Chenming Paper Holdings Limited

8 April 2009



山東晨鳴紙業集團股份有限公司
SHANDONG CHENMING PAPER HOLDINGS LIMITED*