



Mudan Automobile Shares Company Limited*
牡丹汽車股份有限公司

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




2002

Annual Report

* For identification only

Mudan Automobile Shares Company Limited

Founded in 1998, Mudan Automobile Shares Company Limited (“Mudan Auto” or the “Company”) is one of the largest bus manufacturers in The People’s Republic of China (the “PRC”). The Company’s H shares were listed on the Growth Enterprise Market (“GEM”) of The Stock Exchange of Hong Kong Limited (the “Stock Exchange”) on 18 December 2001. The Company is principally engaged in the manufacturing and sale of a range of light-sized, medium-sized and large-sized buses in the PRC under the brandname “牡丹” and trademark of “”. Headquartered in Jiangsu province with its production plants of over 123,000 square metres, Mudan Auto has an annual production capacity of approximately 20,000 buses. Major markets for Mudan buses include Guangdong province, Liaoning province, Jiangsu province and Shanghai.

Mudan buses are well received by customers. The Company has received numerous awards including “Name-brand Product in the PRC (中國名牌產品)”, “One of the Most Popular Name-brand Products in the PRC (中國暢銷品牌產品之一)”, “The First Recommended City Tourist Bus in the PRC (首屆中國城市旅遊汽車推薦會推薦產品)” and “Designated Name-brand Product in Jiangsu Province (江蘇省重點名牌產品)”.

Mudan Auto’s expertise in strong product development as well as its extensive distribution network, efficient after-sales services and reputable brandname provide a solid foundation for further business expansion. Mudan Automobile’s mission is to become a leading bus manufacturer worldwide. To accomplish this mission, the Company will use its successful experience obtained in the PRC to tap overseas markets and opportunities for a global expansion.

During the year, the Company was awarded “Enterprise of Outstanding After-sales Service and Quality Management” (售後服務管理質量先進企業) and “High Quality Brand in favour of Protecting Customer’s Rights and Interests” (保護消費者優質信譽品牌).

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This annual report, for which the directors (the "Directors") of Mudan Auto collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the GEM of the Stock Exchange ("GEM Listing Rules") for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief: (1) the information contained in this annual report is accurate and complete in all material respects and not misleading; (2) there are no other matters the omission of which would make any statement in this annual report misleading; and (3) all opinions expressed in this annual report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

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Corporate Information

Executive Directors

SUN Min Biao (*Chairman*)
SHI Jin Cheng (*Vice-Chairman*)
SHAO Zhi Nan (*Vice-Chairman*)
HOU Cheng Bao
JIANG Wei Sheng

Non-executive Director

YOU Lian Qun

Independent non-executive Directors

ZHANG Xiao Yu
WU Chang Fa

Supervisors

ZHU Xia Zheng
DING Shao Hua
JIN Hong

Senior management

FAN Hong Xing
SHI You Liang
XU Hong Bing
LI Jing Shan
HE Wen Ge
TANG Wei Dong
LIU Jian Zhong
CHEN Jian Ming
CAO Quan
CHEN Yong Xiang

Qualified accountant

LUI Wing Hong, Edward CPA (Aust), FHKSA

Company secretary

LUI Wing Hong, Edward CPA (Aust), FHKSA

Members of the audit committee

ZHANG Xiao Yu
WU Chang Fa

Compliance officer

SHAO Zhi Nan

Authorized representatives

SUN Min Biao
SHAO Zhi Nan

Authorized persons to accept service of process and notice

LEE Sing Leung, Robin

Auditors

KPMG

Sponsor

VC CEF Capital Limited

Legal advisers to the Company

Kwok & Yih
Preston Gates & Ellis

Financial advisor to the Company

SCC Mandarin Financial Services Limited

Principal bankers

Bank of China
Zhangjiagang Branch

Agricultural Bank of China
Zhangjiagang Branch

Construction Bank of China
Zhangjiagang Branch

Hong Kong branch share registrar and transfer office

Hong Kong Registrars Limited
Rooms 1901-5, 19th Floor
Hopewell Centre
183 Queen's Road East, Hong Kong

Registered office

No. 30 Lehong Road
Le Yu Town
Zhangjiagang City
Jiangsu Province
PRC

Website

www.mudanauto.com

Principal place of business in Hong Kong

Room 3602
New York Life Tower
Windsor House
311 Gloucester Road
Causeway Bay
Hong Kong


GEM Stock code

8188

Chairman's Statement



I am pleased to submit to the shareholders the annual report of Mudan Auto for the year ended 31 December 2002.

The Company was incorporated on 18 September 1998 under the approval of Jiangsu Province People's Government as a joint stock limited company by six promoters including Zhangjiagang Municipal Public Assets Management Co., Ltd. (張家港市直屬公有資產經營有限公司) ("ZMPAM"), and Jiangsu Mudan Automobile Group Company Limited (江蘇牡丹汽車集團有限公司) ("Jiangsu Mudan"). The Company is principally engaged in the manufacture and sale of buses under the brandname "牡丹" and the trademark of "" in the PRC. The major products of the Company are six series of light-sized,

medium-sized and large-sized buses, namely MD6601, MD6701, MD6800, MD6901, MD6100 and MD6121 and the series are further classified into over 200 models. The Company is one of the largest bus manufacturers in the PRC.

On 18 December 2001, Mudan Auto was listed on the GEM of the Stock Exchange. As H share of the Company have accounted for approximately 31.09% of the Company's total issued share capital, Ministry of Foreign Trade and Economic Cooperation of the PRC approved on 25 April 2002 the change of the nature of the Company to an "Enterprise with Foreign Investment in the PRC" (「外商投資股份制企業」).

Business review

In 2002, under the leadership of the Board of Directors, the staff members devoted effort to further develop the business and continued to maintain the team spirit of "actively exploring new business opportunities and developing innovative ideas with a practical approach" by adopting changes within the Company and seeking new business opportunities. This has laid a firm foundation for further growth of the Company, the Company's business activities had performed satisfactorily. In order to develop new market and new customers, products mix of the Company have been changed to cater for customers' needs, and special efforts were made to develop medium and large-sized buses. The total number of sale and manufacture of all series of buses in the year of 2002 amounted to 10,554, among them large and medium-sized buses amounted to 2,424 units, representing an increase of 86.7% as compared with previous year.

Turnover for the year ended 31 December 2002 amounted to RMB888,526,140. Net profit stood at RMB47,672,699.

1. Development and progress in technology

- (a) **New products:** In 2002, new technologies and materials are adopted by the Company to keep abreast of new changes in the domestic and overseas city-bus and passenger transportation market, with more emphasis on the research on large and medium-sized buses. 36 new products were approved by the State Economic and Trade Commission of the PRC ("SETC") during the year.

One of the new models is a luxury low floor city-bus which has a neat and smooth look. It adopts special chassis for city-bus and the front and rear suspension is made by spring

Chairman's Statement

laminations loaded under-changing section. The bus is installed with landscape orientation stabilization shift and double process canister shake absorber producing a stable and comfortable performance. The inner adornments are elegant and fashionable, which offer a taste of pleasant new life style . At present, the model has a separate series with the length of 8.3 meters to 10.6 meters available to customers.

Another model, 12 meters long high-grade luxury tourist coach, has a unique style with powerful engine and beautiful inner adornments. It adopts high-grade chassis with safe-air cell and high power air conditioning. The whole body of the bus reaches the standard collocation requirements of the large high-grade bus finished bus. It becomes very popular since it was put into the markets.

- (b) **Technology management:** In order to adapt to the changes in the product mix, the Company rearranges of the Research & Development department ("R&D") which is further divided into high-grade bus research section, city-bus research section, chassis technology develop section and electricity system information office. A better R&D system was established to monitor changes in the market closely and respond sensitively.
- (c) **Product structure:** In the year of 2002, on the one hand, Mudan Auto grasped at any opportunities to develop new product and the product type were extended to 12 meters coach. On the other hand, the performance of existing product was further improved, which will further enhance the competitive advantages of the Company. Moreover, the Company has enhanced the quality of its products by developing environmental friendly, high quality and comfortable buses.

2. Marketing strategies adjustment

- (a) **Competing for the sales manager position and setting up overseas business department.** Last year, the Company organised internal competition for the post of manager for each sales office throughout the country, and the staff's rewards were linked with their sales results. The Company chose persons with high caliber and the staff was motivated by this plan.

To expand its overseas markets, the Company established an overseas business department. Following the growth in its international reputation, Mudan Auto receives growing attention from customers of foreign markets. During the year, small quantity of the Company's products were exported to other regions in South Asia, Europe, South America, North America, South Africa, North Africa, Mediterranean Countries, Middle East, Caribbean Sea and etc..

During the year, the Company was also granted a certificate of "You are approved to enter the wholesaling system of the international fine products wholesaling center" by Russia International fine product wholesaling center and Mongolia International Association Education and Business. This lay a firm foundation for Mudan buses go into Mongolia and Russia bus market.

- (b) **Promoting the brand name sales strategies and developing foreign and domestic markets.** The Company placed great emphasis on brand name promotion as well as enhancing products' recognition. Exhibition named "Spring Exhibitions for Mudan Automobiles" was held in major cities such as Chongqing, Suzhou and Nanjing in early 2002. In late 2002, the Company successfully organised a conference in Qingdao namely "Mudan New Model Buses Exhibition and Press Conference 2003" with the theme of safety, environmental protection, comfortable, luxury and to create a high quality of life. In this event, the Company focused on the promotion of large and medium-sized bus,

Chairman's Statement



passenger transport bus, city-bus and other new products. This event has received great attention from the automobile industry in the PRC. At the same time, advertisement was put on the website of the Company and on Star TV of Jiangsu to invite the best sub-brandname suggestion for our new products with rewards. This measure enhanced the public awareness of our products and further facilitate market development.

- (c) **Paying attention to quality management and building up the awareness of good products.** Mudan Auto placed great emphasis on product quality. In 1998, the Company implemented standard quality control system and got ISO9002 quality certificate. In 2002, the Company implemented ISO9001 (2000 version) certification project, about 50 courses had been implemented to train the related staff, and the quality improvement system had been established. During the year, the Company has implemented a "product enhancement" program advocating for "flawless" products. It regulated the technology practice, controlled the production flow strictly, launched the quality assessment activities, stepped up examination upon acceptance of chassis, made more dynamic checking, controlled the quality parts, sampled and checked regularly, collected the information about producing, testing, sales, servicing and etc, promoted the quality level, strengthened quality control and highlighted the responsibility for output quality. The Company provided quick and high quality maintenance services to its customers, which has therefore enhanced the Company's reputation in the PRC bus market. In 2002, during the activity of "15 March-Day of the Customer's Rights" (3.15消費者權益日), the Company was awarded as the "Enterprise of Outstanding After-sales Service and Quality Management" (售後服務管理質量先進企業) by "Inspection of Product Quality in China" (中國質量萬里行). On 18 December 2002, the Company was awarded "High Quality Brand in favour of Protecting Customer's Rights and Interests" (保護消費者權益優質信譽品牌) by China Consumer Protection Association.

3. Enterprise Management Innovation

- (a) **Adjusting the organization structure.** The Company has reformed the organization structure and the management function. To enhance the management and quality control capabilities, the Company discontinued the branch factory system and established production department I, II, III in accordance with the product types. There is integration within the management and becomes more scientific structure. The staff became more sophisticated and productive. The Company also recruited a team of energetic management staff of good knowledge, rich practical experience and enterprising spirits.

Chairman's Statement



- (b) **Innovating the management means:** The Company made a good beginning on the information technology system project, with all of the hardware job of the network have been finished, and office automation system ("OA") has been put into use, the feasibility analysis on Enterprise Resource Planning ("ERP") system has been started, upgrading of financial management software and development of storage module have begun. As internal resources and information sharing was put to work, the operation efficiency and the management level were enhanced.
- (c) **Other back-end management were enhanced:** The Company invited public tender for the supply of parts & components of buses and strictly assessed the supplier's qualification. It also carried out the zero level inventory management to reduce tied-up funds and enhance the fund flow situation.
- (d) **Technology innovation project:** In 2002, the Company received the "Approval on the Proposed Technical Reform Project of Medium-sized Buses of Mudan Automobile Shares Company Limited" issued by the SETC from Jiangsu Provincial Economic and Trade Commission. Pursuant to the approval, the SETC permitted the Company to carry out technology upgrade to the production line for medium-sized buses. The project was proceeding smoothly.

Future prospect

The Company is committed to continuously improving the technology level, perfecting the quality management system, building up an outstanding sales team, developing the human resources, developing cooperation with external parties, introducing new management skills, carrying out enterprise-wide digitalization project.

1. Technological improvement for medium-sized bus production lines

The Company intends to improve the quality of the products by improving the medium-sized bus producing line and bus testing line.

2. Perfecting the building of the R&D center

The Company intends to enhance parts and components test operation, workmanship and technology examination, and to expand the team of the technical center to enhance the R&D capability.

Chairman's Statement

The Company will step up the development of the high-grade, environmental friendly buses. Product development will take the form of gradual technology on grading, which will allow the Company to cross the high entry barrier for the market of environmental friendly buses. The new products will meet the requirement of the related environmental protection. Furthermore, the Company will put more emphasis on developing natural gas buses. In 2003, the Company intends to develop three basic models and five modified models, subject to approvals from the related departments of the PRC.

The Company will strengthen the authority of quality control ("QC") system, build up top-to-bottom integrated quality inspection system, enhance the design and development capabilities of the staff for new products, adopt modern design and test tools. New basic bus models must be tested according to test rules. In order to match requirements of the testing system of medium and large-sized buses, the Company will build a high grade test line with modern inspection devices.

The Company will enhance the overall operational efficiency and improve the combined competitiveness of the enterprise through the use of information by network expansion, software enhancement, system integration, overall system planning, upgrading in the training, use of ERP, Customer Relationship Management ("CRM") or Product Data Management ("PDM"), optimization in resources integration, implementation of internal information sharing, and feedback from the external sources to the management. It will fully utilize the website of Mudan Auto by highlighting its sales services, ensuring prompt delivery of news, implementing exchange of public information between LAN and WAN, so as to build up a solid foundation for digital business.

3. Improvement of Sales Network

The Company will improve the dealer's credit level review system and sales network, increase the number of distributors in central and western of China. Meanwhile, the Company will delegate distributorship to explore overseas markets to a further extent.

The Company also set up maintenance and spare parts stores throughout the PRC, designate new professionals who are young and proficient techniques to strengthen sales teams and after sales service teams.

Mudan Automobile Shares Company Limited

SUN Min Biao

Chairman

Zhangjiagang City, Jiangsu Province, the PRC

20 March 2003

Management Discussion and Analysis

Market overview

The outstanding performance of the completion of the highway and expressway in China of year 2002.

In the latest report announced in the directors meeting of the Transportation Department (交通廳局長會議), it mentioned that the investment amount on the completion of the infrastructure on the transportation was reached RMB315 billions in year of 2002 and recorded the highest amount injected in the past history. RMB300 billions was invested in the completion of the highway and expressway. The length of the highway which has been upgraded, renovated, completed totally reached 1,758,000 km. Newly completed highway reached 60,000 km. The highway density reached 18.3 km per 100 sq. km. As many high-grade of the highway and expressway have been completed, it provides market opportunities for medium-sized to large-sized buses.

According to the information of Ministry of Communication, the total length of the highway and expressway together has reached 25,200 km. in the PRC today, of which 5,583 km are newly completed. There are 10 provinces which have the highway network breakthrough the length of 1,000 km. In Liaoning, Shandong and Zhejiang provinces, the highway has already connected to the capital of each provinces and major cities. The development of the village road has reached 1,300,000 km. The linkage of the highway to the urban area and administrative village has reached 99.4% and 92.5% respectively. The Company's light-sized buses suitable for running between town to town have a prosperous future.

Officials from the Ministry of Communication also stated that highway construction in the PRC in 2003 will continue to focus on constructing national trunk highway namely 5 vertical and 7 horizontal national highways. The plan has included newly constructs on 800 km of national trunk highway. Meanwhile, the government's program also start work on completing the final stage of the highway linkage with major village.

In 2002, the passenger transportation has increased. The volume of passenger transportation had reached 14.7 billion and the passenger-kilometers amounted to 764.3 billion and were increased by 4.5% and 6.0% as compared with last year. This phenomenon will continue as a result of the development of national economy. This leads to the further on the increase in the demand on the buses. This tendency matches with the strategy of the Company of developing western parts in the PRC.

Development after the Accession into World Trade Organisation ("WTO")

In view of the automobile market in the year of 2002, China's entering into WTO neither has any adverse impact on China's car market, nor has it upset the car industries in China. Oppositely, the policy has been carried out properly so that the number of production and sales of domestically manufactured car is very large.

Due to the above mentioned, the overall automobile industry market atmosphere is good, the support of the government to the infrastructure and domestic car industry make a bigger room for development of our products in the market.

Development of new products

To serve with customers' need, the Company had deployed substantial resources in developing and improving medium and large-sized buses. In 2002, the new models were developed included: 8 models of the MD6601 series of light-sized buses, 4 models of the MD6701 series of light-sized buses and 4 models of MD6701 series of medium-sized buses, 10 models of the MD6800 series of medium sized buses and 2 models of the MD6901 series of medium-sized buses, 7 models of the MD6100 series of large-sized buses, 1 model of the MD6121 series of large-sized bus, totally 36 products. All the products were approved by the respective governmental departments.

Management Discussion and Analysis

Revenue

Total revenue for the fiscal year of 2002 amounted to RMB888,526,140, representing approximately 3.7% increase compared to that of RMB857,038,069 generated in 2001, in which for light, medium and large-sized series of buses amounted to RMB492,100,699, RMB287,427,044 and RMB108,998,396 respectively. Compared to 2001, revenue for light-sized buses decreased by 25.4%, medium and large-sized series of buses increased by 97.7%, 108.5% respectively.

Cost of sales and gross profit

Due to the increase in total revenue, cost of sales increased proportionately to RMB780,226,789 in 2002 from RMB750,295,261 in 2001. Gross margin of the Company's products slightly decrease to 12.2% in 2002 from 12.5% in 2001. The decrease in gross margin was primarily attributable to the volume discount on medium and large sized buses given to customers in some regions in order to expand the market there.

Other operating income

Other operating income for the fiscal year 2002 amounted to RMB1,486,317 (2001: RMB5,829,036), which included the sale of scrap materials RMB444,893 (2001: RMB2,913,907).

Distribution expenses and general and administrative expenses

The Company also continued to expand its sales and marketing network. The Company strictly instituted a cost control policy (which was mainly used to control the fixed costs of all the representative offices, including costs and expenses relating to salaries, administration, housing and communications) to better control distribution expenses. As a result, distribution expenses for 2002 totalled RMB25,096,843. This represents a decrease of RMB613,742 from that of 2001.

The total general and administrative expenses for the fiscal year 2002 was RMB13,805,192, an increase of RMB5,431,344 as compared to the amount of RMB8,373,848 in 2001. Such increase was mainly attributed to the increase in number of staff and the payment of the professional charges.

The Company's expenses on salaries, wages and bonus for the fiscal year 2002 amounted to RMB46,394,011, as compared to RMB29,554,054 in 2001, an increase of RMB16,839,957. The reasons were (i) the increase in the number of staff and the salaries of the labour was linked with the increase of production of the medium and large-sized buses; (ii) instead of distribution fee paid to a related company in the year 2001, the Company paid bonus to its sales staff directly according to their sales performance. The average number of employees of the Company during 2002 was 2,179, as compared to 2,105 in 2001. The new staff included sales personnel, persons engaged in research and development as well as technical operators.

Other operating expenses for the fiscal year 2002 totalled to RMB802,750, as compared to RMB815,646 in 2001, a drop of 1.6%, which was mainly represents provision on finished goods incurred in 2002.

In the financial year of 2002, the net finance costs of approximately RMB1,498,461 comprised interest on bank advances and other borrowings, bank charges and interest income, representing approximately 0.2% of turnover for the year 2002, as compared to approximately RMB4,539,496 in year of 2001, a decrease of RMB3,041,035 which is due to decrease the amount of other borrowings and increase the bank interest income due to the increase of bank deposit.

Management Discussion and Analysis

Material investments and capital assets

Other than those disclosed in the Company's prospectus dated 4 December 2001 under the section headed "Business Objectives" and the announcement dated 19 November 2002 of the Company, the Company did not have any material investments and acquisition of material capital assets for the year of 2002 and at present it does not have other future plans for material investments or capital assets.

Exposure in exchange rate fluctuations

Most of the Company sales and raw materials purchase are settled in RMB. In such circumstances, the Directors considered that the exchange rate fluctuations is limited for the year of 2002.

Significant investments held

The Company has no significant investments held during the year of 2002.

Financial resources and liquidity

The Company continues to be in a healthy financial position with shareholders equity amounted to RMB375,549,489 as at 31 December 2002 (2001: RMB337,891,786). Current assets amounted to RMB564,739,422 as at 31 December 2002 (2001: RMB415,351,153), of which RMB92,594,293 (2001: RMB91,159,940) were cash and bank balances. RMB59,431,080 (2001: RMB31,920,018) was placed as pledged deposits to secure certain banks in issuing bill payable of RMB191,630,000 as at 31 December 2002 (2001: RMB36,470,000). As at 31 December 2002, the Company has a short-term bank loans and long-term bank loans of about RMB20,000,000 and RMB20,000,000 respectively, the short-term bank loans are repayable within one year and the long-term bank loans are repayable within two years.

Contingent liabilities

As at 31 December 2002, the Directors were not aware of any material contingent liabilities.

Charges on assets

As at 31 December 2002, the short-term bank loans was unsecured (2001: secured by certain machineries at net book value of RMB23,335,829) and long-terms bank loans was secured by certain machineries with a net book values of RMB37,027,056 (2001: RMB41,455,751).

Gearing ratio

The Company's gearing ratio, based on total liabilities to shareholders' equity, was 0.98 (2001: 0.77) as at 31 December 2002.

Capital structure

During the year, there has been no change in the Company's share capital. As at 31 December 2002, the Company's operations were financed mainly by shareholders' equity and internal resources. The Company will continue to adopt its treasury policy of placing the Company cash and cash equivalents in interest bearing deposits.

Employee information

During the year, the average number of employees of the Company had 2,179 employees (2001: 2,105). They were remunerated in accordance with their performance and market condition. Other benefits available to eligible employees include medical insurance and pensions fund. The Company does not have share option scheme.

Business Objective Review

Comparison of business plans and actual progress

From 1 January 2002 to 30 June 2002

Expected project progress

Actual project progress

(1) Business development/expansion in sales and marketing activities

- | | |
|--|---|
| 1. Launch one to five new bus models. | 17 new models comprising 4 models of MD6601 series of medium-sized buses, 2 models of MD6701 series of medium-sized buses, 2 models of MD6701 series of light-sized buses, 3 models of MD6800 series of medium-sized buses, 2 models of MD6900 series of medium-sized buses and 4 models of MD6100 series of large-sized buses had been approved and announced by SETC. |
| 2. Explore opportunities to expand the organized distribution network in the overseas market. | An overseas department was set up to study the expansion of the business into the overseas market. |
| 3. Appoint a non-exclusive distribution agent in South Africa, Asia and South America to increase the Company's presence in the overseas market. | 5 non-exclusive distribution agents were appointed in the overseas market. Part of its products were exported to Asia, Europe, South Africa etc. |
| 4. Commence feasibility study on setting up sales offices in the PRC. | The marketing department was conducting feasibility studies |
| 5. Place advertisement in the media to promote the Company's overall image. | Advertisements were made on "China Economic Daily", "China Consumer Daily", "China Automobile Daily", "New China Daily", and "Suzhou Daily" and "Zhangjiagang Daily" etc. |
| 6. Participate in major sales exhibitions and trade shows. | The Company organized exhibitions in Chongqing, Suzhou and Nanjing, on 21 March 2002, 18 and 26 April, 2002 respectively. The Company focused on products such as luxury touring buses for short and medium distance transport, high-speed and luxury buses for long distance transport and public transport buses etc. |
| 7. Recruit 150-230 sales staff. | 229 sales staff were recruited |

(2) Modernization of production facilities

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| 1. Enhance the functions and features of the existing production's facilities to improve efficiency and increase productivity | By streamlining the production process and re-arrangement of the working hours, working performance was improved accordingly. |
|---|---|

Business Objective Review

- | | |
|---|--|
| <p>2. Commence feasibility study on modernizing the existing production facilities for the production of medium-sized buses</p> | <p>SETC had formally approved the technical reform project of medium-sized buses of the Company. The Company was carrying out a feasibility study.</p> |
|---|--|

(3) Introduction of advanced technologies

- | | |
|--|---|
| <p>1. Commence feasibility study on introducing advanced technologies for the production of medium-sized bus body (in particular, the technologies in the welding, painting, assembly and final inspection processes).</p> | <p>Specialized personnel were appointed to conduct feasibility studies.</p> |
| <p>2. Seeking alliance with domestic/foreign bus manufacturers for technological transfer arrangement in respect of the production of medium-sized bus body.</p> | <p>Under preliminary negotiation.</p> |

(4) Enhancement of research and development capabilities

- | | |
|---|--|
| <p>1. Provide training for the existing research and development staff.</p> | <p>The Company cooperated with Jiangsu University to organize a further education class of mechanical and electrical (M & E) engineer during the Period. The program includes courses relating to the transmission system of M & E, automobile design, computer C-language design, test system and hydraulic transmission, automobile construction, body design, course design and automobile theory etc. 21 technicians attended such training. 6 persons who were engaged in technology research and development department were nominated to study the master program of M&E in Jiangsu University.</p> |
|---|--|

From 1 July 2002 to 31 December 2002

Expected project progress

(1) Business development/expansion in sales and marketing activities

1. Continue to launch one to five new bus models;

Actual project progress

19 new models comprising 4 models of MD6601 series light-sized buses, 2 models of MD6701 series of light-sized buses, 2 models of MD6701 series of medium-sized buses, 7 models of MD6800 series of medium-sized buses and 3 models of MD6100 series of large-sized buses, 1 model of MD6121 series large-sized buses, had been approved and announced by SETC.

Business Objective Review

- | | |
|---|---|
| <p>2. Continue to strengthen the distribution network in South Africa, Asia and South America by appointing distribution agents if the business opportunities arises.</p> | <p>The Company had made sales agency agreements with distributors in Pakistan, Bengal, Babados in Caribbean, etc..</p> |
| <p>3. Continue the feasibility study an setting up the sales office in the PRC.</p> | <p>The marketing department continued to conduct feasibility studies.</p> |
| <p>4. Set up two sales offices in Lhasa and Xining in Western China.</p> | <p>Branch office of Urumchi was also used as Lhasa sales office and the branch office of Yinchuan was also used as Xining sales office.</p> |
| <p>5. Participate in major sales exhibitions and trade shows.</p> | <p>On 8 November 2002, the Company organised an event in Qingdao namely "Mudan New Model Buses Exhibition and Press Conference 2003".</p> |
| <p>6. Place advertisement in the media to promote the Company's overall image.</p> | <p>Propagandistic information about products and the Company had been published and put on Jiangsu TV, Guangdong TV, Shanxi TV, Shandong TV, China Automative News, Securities Daily, Urumchi Evening News, Liaoning Daily, Qingyuan TV and Zhangjiagang TV etc to promote the Company's overall image.</p> |

(2) Modernisation of production facilities

- | | |
|---|---|
| <p>1. Commence the installation of the modernised production facilities for the production of medium-sized buses into one of the production lines to improve quality of the products;</p> | <p>The production line is under reconstructing.</p> |
|---|---|

(3) Introduction of advanced technologies

- | | |
|---|---|
| <p>1. Enter into partnership with foreign and/or domestic bus manufacturers for technology transfer arrangement in relation to the production of medium-sized bus body.</p> | <p>Due to the change of the market, the model of medium-sized bus body has to be re-confirmed and the cooperation programme is therefore still under preliminary negotiation.</p> |
|---|---|

(4) Enhancement of research and development capabilities

- | | |
|--|--|
| <p>1. Recruit 10-30 number of high calibre R&D staff and acquire advanced and comprehensive facilities to strengthen the R&D capabilities.</p> | <p>12 R&D staff recruited and 19 units computers were added.</p> |
|--|--|

Business Objective Review

2. Continue to provide training to the existing R&D staff.

The Company cooperated with Jiangsu University to organize a tertiary promotion class of mechanical and electrical (M&E) engineer during the period. The program includes M&E courses, Computer Theory and Connection Technology, Automobile AC, Automobile Mould, Automobile Design, CAD/CAM, Pro-e Drawing Software, Automobile Electron, and etc. 21 technicians attended such training. 6 persons engaged in technology research and development department were nominated to study the master program of M&E in Jiangsu University.

Use of proceeds from listing

The Company had issued and allotted a total of 88,550,000 H Shares by public offer and placing, among which included the conversion of 8,050,000 state-owned shares by ZMPAM into H Share for sale to the public. These H shares were listed on the GEM of the Stock Exchange in December 2001. The net proceeds (net of relevant expenses) for the Company amounted to approximately HK\$67,438,116.


During the year, approximately HK\$1,344,029 was used in enhancement of the sales and marketing activities; approximately HK\$819,502 was used for research and development capabilities; approximately HK\$556,800 was used for the project of modernization of the Company's production facilities for medium-sized buses; and approximately HK\$21,438,166 was used for general working capital

During the year, the amount of net proceeds that have been utilized was about HK\$24,158,497. As at 31 December 2002, the balance of the unused proceeds from listing amount to approximately HK\$43,279,619. The unused proceeds will continue to be used for purpose as disclosed in the Prospectus and are placed on deposit with financial institutions.

Report of the Board of Directors

The board of Directors (“the Board”) takes the pleasure in submitting the report of the Board together with the audited financial statements of the Company for the year ended 31 December 2002.

Principal activities

The principal activities of the Company are the manufacture and sale of light-sized, medium-sized and large-sized buses under the brandname of “牡丹” and trademark of “” in the PRC.

Revenue mainly comprises the sale of automobiles in the PRC. In the circumstances, the Directors consider that the Company operates within a single business and geographical segment.

Major customers and suppliers

The Company’s sales to the five largest customers accounted for less than 30% of the Company’s turnover during the financial year (2001: less than 30%).

The information in respect of the Company’s purchases attributable to the major suppliers during the financial year are as follows:

	Percentage of the Company’s total purchases	
	2002	2001
The largest supplier	29%	20%
Five largest suppliers in aggregate	51%	32%

At no time during the year have the Directors, their associates or any shareholders of the Company (which to the knowledge of the Directors owns more than 5% of the Company’s share capital) had any interest in these major customers and suppliers.

Financial statements

The profit and cash flows of the Company for the year ended 31 December 2002 and the state of the Company’s affairs as at the date are set out in the financial statements on pages 29 to 54.

Dividends

No interim dividend (2001: a special dividend of RMB0.24 per share) was paid during the year. The Directors now recommend the payment of a final dividend of RMB0.015 per share (2001: RMB0.03) in respect of the year ended 31 December 2002.

Charitable donations

There was no charitable donations made by the Company during the year (2001: RMB689,000).

Property, plant and equipment

Details of the movements in property, plant and equipment of the Company during the year are set out in note 14 on the financial statements.

Share capital

Details of the share capital during the year are set out in note 26(a) on the financial statement.

Report of the Board of Directors

Reserves

Details of movements in reserves of the Company during the year are set out in the statement of changes in equity.

Substantial shareholders

As of 31 December 2002, holders of Domestic Shares and H Shares interest of whom are to be recorded in the register kept under section 16(1) of the Securities (Disclosure of Interests) Ordinance ("SDI Ordinance") were as follows:

Name of shareholders	Number of shares	Note
ZMPAM	195,250,000	(1)
Jiangsu Mudan	100,940,000	(2)
Zhangjiagang Municipal Leyu Town Assets Management Co., Ltd. ("Leyu Town Assets Management")	100,940,000	(3)
HKSCC Nominees Limited	87,976,000	

Notes:

- Out of 195,250,000 domestic shares, 100,340,000 domestic shares were held through by Jiangsu Mudan, 300,000 domestic shares were held through by Zhangjiagang Mudan Automobile Accessories Co., Ltd. ("ZMAAC") and 300,000 domestic shares held through by Zhangjiagang Mudan Bus Parts Co., Ltd. ("ZMBPC").
- Out of 100,940,000 domestic shares, 300,000 domestic shares were held through by ZMAAC and 300,000 domestic shares were held through by ZMBPC.
- Out of 100,940,000 domestic shares, 100,340,000 domestic shares were held through by Jiangsu Mudan, 300,000 domestic shares were held through by ZMAAC and 300,000 domestic shares were held through by ZMBPC.
- Jiangsu Mudan is owned by ZMPAM, Leyu Town Assets Management and three other shareholders as to 33.4%, 37.2%, 26.3%, 2.2% and 0.9%.

Save for the information stated above, the Company is not aware of any interests required to be disclosed by the Company pursuant to Section 16(1) of the SDI Ordinance as of 31 December 2002.

Interests of directors and supervisors in the share capital

At 31 December 2002, the interests of the directors and supervisors in the share capital of the Company as recorded in the register maintained by the Company pursuant to section 29 of the Securities (Disclosure of Interests) Ordinance (the "SDI Ordinance") or otherwise notified to the Company as required by Rule 5.40 of the GEM Listing Rules were as follows:

Non-executive director	Domestic Shares
You Lian Qun	(Note) 1,000,000

Note: As at 31 December 2002, Madam YOU Lian Qun, a non-executive Director of the Company, owns as to 12.2% interests in Zhangjiagang Automobile Accessories Factory ("ZAAF"), one of the promoters of the Company. ZAAF owns as to 0.35% interests in the Company. Madam YOU Lian Qun is also the director and legal representative of ZAAF.

Report of the Board of Directors

Save as disclosed above, as at 31 December 2002, none of the Directors or supervisors or any of their associates had any interest in any shares or debentures of the Company or any associated corporation (within the meaning of the SDI Ordinance).

Save as disclosed above, none of the Directors or the supervisors or any of their spouses or children under 18 years of age had, at 31 December 2002, any personal, family, corporate or other interests in the equity of the Company, as defined in the SDI Ordinance.

Directors' and supervisors' interests in contracts

No contract or significance to which the Company, its holding company or any of its fellow subsidiaries was a party in which a director or supervisor of the company had a material interest, subsisted at the end of the year or at any time during the year.

Service contracts of directors and supervisors

Each of the executive Directors and supervisors of the Company has entered into a service contract with the Company. These contracts are in all material respects identical. Each service contract is for an initial term of three years commencing on the respective date of appointment by the shareholder's meeting and shall continue until the conclusion of the annual general meeting of the Company in 2004 and thereafter, subject to the approval of the shareholders' meeting of the Company, each service contract may be renewed each time for three years.

Each of the non-executive director and independent non-executive directors was appointed pursuant to resolutions passed at the shareholders' meetings. Each appointment is for a term of three years commencing on the respective date of appointment and their emoluments are determined by the board annually.

Save as disclosed above, no Director and supervisor has an unexpired service contract which is not determinable by the Company within one year without payment of compensation, other than normal statutory obligations.

Directors and supervisors

The Directors and supervisors of the Company during the financial year were:

Executive Directors

SUN Min Biao (*Chairman*) (promoted to the Chairman on 3 June 2002)
SHI Jin Cheng (*Vice-chairman*)
SHAO Zhi Nan (*Vice-chairman*)
HOU Cheng Bao
JIANG Wei Sheng
SONG Bo Xiang (resigned on 3 June 2002)

Non-executive Director

YOU Lian Qun

Independent non-executive Directors

ZHANG Xiao Yu
WU Chang Fa

Supervisors

ZHU Xia Zheng
DING Shao Hua
JIN Hong

Report of the Board of Directors

Directors' and supervisors' emoluments

Details of the Directors and supervisors' emoluments for the year are set out in note 12 on the financial statements.

Connected transactions

Details of the connected transactions of the Company carried out in the year are disclosed in note 29 on the financial statements.

Competing interests

On 29 November 1999, Jiangsu Mudan, a substantial shareholder of the Company, together with four independent third parties, submitted a tender to the government of South Africa tendering for a contract for the supply of new buses of 5.98 m or above in length to replace 127,000 obsolete buses currently used in South Africa. In the event that such tender is accepted by the government of South Africa, Jiangsu Mudan has undertaken that it will use its best endeavour to procure the sub-contract of all the production orders to be responsible under the tender to the Company to avoid competition with the business of the Company. If Jiangsu Mudan fails to procure the sub-contracting of all the production orders, Jiangsu Mudan has further undertaken that it will not proceed with the tender and will not participate or provide any support in relation to the manufacturing of buses to the government of South Africa.

On 8 October 2001, each of ZMPAM and Jiangsu Mudan (the "Undertaking Party") has undertaken to the Company that neither of them nor their respective subsidiaries will engage or be interested, directly or indirectly, in business and hold any interest or benefits in or by any other means engage or participate in any business activities, which may compete directly or indirectly with the business of the Company. In relation to each Undertaking Party, such undertaking shall remain in force so long as (1) such Undertaking Party and its associates shall, singly or together, remain beneficially interested, directly or indirectly, in 30% or more of the entire shareholding interest of the Company; and (2) the H Shares or any equity securities of the Company are listed on the Stock Exchange or on any other stock exchange.

Save as disclosed herein, none of the Directors, supervisors, initial management shareholders, substantial shareholders and significant shareholders of the Company and their respective associates has any interest in any businesses which directly or indirectly compete with the business of the Company for the year ended 31 December 2002.

Purchase, sale or redemption of the listed shares of the Company

During the year, the Company has not purchased, sold or redeemed any of its listed securities.

Management contracts

No contract concerning the management and administration of the whole or any substantial part of the business of the Company was entered into or existed during the year.

Audit committee

The Company set up an audit committee (the "Committee") on 3 September, 2001 with written terms of reference in compliance with the requirements as set out in Rules 5.23 and 5.24 of the GEM Listing Rules. The primary duties of the Committee are to review and provide supervision over the financial reporting process and internal control of the Company. The Committee comprises two independent non-executive directors, ZHANG Xiao Yu and WU Chang Fa. The Company's financial statements for the year ended 31 December 2002 have been reviewed by the Committee, who were

Report of the Board of Directors

of the opinion that such statements complied with the applicable accounting standards, the Stock Exchange and legal requirements, and that adequate disclosure had been made. The Committee held four meetings for the year ended 31 December 2002.

Bank loans

Particulars of bank loans as at 31 December 2002 are set out in notes 23 and 25 on the financial statements.

Retirement scheme

Particulars of the retirement scheme of the Company are set out in note 7 on the financial statements.

Financial summary

A summary of the results and of the assets and liabilities of the Company for the last five financial years is set out on pages 56.

Interests of sponsor

Neither VC CEF Capital Limited (the "Sponsor") nor its directors or employees or associates (as referred to in Note 3 to Rule 6.35 of the GEM Listing Rules) had any interests in the share capital of the Company as at 31 December 2002.

Pursuant to the agreement dated 30 November 2001 entered into between the Company and the Sponsor, the Sponsor will receive a fee for acting as the Company's retained Sponsor for the period from 18 December 2001, the date on which the shares of the Company are listed, to 31 December 2003.

Save as disclosed above, the Sponsor has no other interest in the Company as at 31 December 2002.

Practices and procedures of the board

The Directors considered that the Company has complied with the requirement of Board practices and procedures of Rules 5.28 to 5.39 of the GEM Listing Rules throughout the year.

Auditors

KPMG Peat Marwick Huazhen and KPMG retire and being eligible, offer themselves for re-appointment. A resolution for the re-appointment of KPMG Peat Marwick Huazhen and KPMG as the domestic and international auditors of the Company respectively is to be proposed at the forthcoming Annual General Meeting.

By order of the Board
Mudan Automobile Shares Company Limited
SUN Min Biao
Chairman

Zhangjiagang, Jiangsu Province, the PRC

20 March 2003

Report of the Supervisory Committee

To: All Shareholders

The supervisory committee (“we”) of Mudan Automobile Shares Company Limited (the “Company”), in accordance with the Company Law of the PRC, requirements of the relevant laws and regulations of Hong Kong and the articles of association of the Company (the “Articles of Association”) during the year ended 31 December 2002, have exercised conscientiously its authority, safeguarded the interests of the shareholders and the Company, following the principle of honesty and trustworthiness and worked cautiously and diligently.

During the year we carefully reviewed the use of the proceeds raised in strict compliance with the plan of use of proceeds disclosed in the Prospectus of the Company and provided reasonable suggestions and advice on the operations and development plans to the Directors and have strictly and effectively monitored whether the policies and decisions made had conformed with the state laws and regulations and the Articles of Association and have safeguarded the interests of the shareholders.

After investigation, we consider that the financial statements of the Company, audited by KPMG, truly and sufficiently reflects the operating results and asset positions of the Company. We also reviewed the Report of the Board of Directors and the profit distribution proposal. We consider that the above report and proposal meet the requirements of the relevant regulations and Articles of Association. We have attended the meeting of the Board. We consider that the members of the Board, the general manager and other officers have strictly complied with the principle of honesty and trustworthiness, worked diligently and sincerely acted in the best interests of the Company. Up to now, none of the Directors, general manager and the officers have abused their powers, caused damage to the interests of the Company and infringed upon the interests of the company and its staff, nor have they violated any laws, regulations or the Company’s Articles of Association.

We are satisfied with the various tasks achieved as well as the cost-effectiveness gained and are confident about the prospects of future development of the Company.

By order of the Board
Mudan Automobile Shares Company Limited
ZHU Xia Zheng
Chairman of the Supervisory Committee

Zhangjiagang City, Jiangsu Province, the PRC

20 March 2003

Profiles of Directors, Supervisors and Senior Management

Executive Directors

Mr. SUN Min Biao (孫敏彪), aged 40, is an executive Director, chairman of the board of directors and chief executive officer of the Company. Mr. SUN holds the title of senior engineer. Mr. SUN was formerly deputy general manager and chief economist of Jiangsu Mudan for the period from April 1995 to August 1998. He is now responsible for the overall business development, sales and marketing, financial planning, administration and human resources management of the Company. Mr. SUN has over 11 years of experience in business management. He graduated from Southeast University formerly known as Nanjing Industrial College with a bachelor degree in Automatic Control in 1982. He finished the postgraduates course of economy management research in Southeast University in 1999. He has been conferred the titles of Excellent Entrepreneur of Suzhou City (蘇州市優秀廠級領導幹部) in 1998; Top Ten Outstanding Youth in Zhangjiagang City (張家港市十大傑出青年) in 1999; and First Senior Talents in the 21st Century of Suzhou City (蘇州市首批跨世紀高級人才培養對象) in the same year. In the year of 2001 and 2002, Mr SUN has also been awarded the title of Advanced Entrepreneur (優秀企業家) by Zhangjiagang people' government. He joined the Company in September 1998.

Mr. SHI Jin Cheng (施錦成), aged 52, is an executive Director, vice-chairman of the board of directors, deputy general manager of the Company. He holds the title of economist. Mr. SHI was formerly deputy general manager of Jiangsu Mudan for the period from January 1996 to August 1998. He is now responsible for the overall product plan and material purchasing of the Company. He has over 11 years of experience in technology management and product development. He joined the Company in September 1998.

Mr. SHAO Zhi Nan (邵志南), aged 47, is an executive Director, vice-chairman of the board of directors, deputy general manager of the Company. Mr. SHAO holds the title of senior engineer. Mr. Shao was formerly the deputy general manager of Jiangsu Mudan for the period from January 1996 to August 1998. He is now responsible for the administration affairs and foreign economic co-operation of the Company. He has over 16 years of experience in product development, marketing and enterprise management. Mr. SHAO is the deputy chairman of the Automobile Engineering Council of Jiangsu Province, deputy chairman of the Automobile Engineer Council of Suzhou and Engineering Master teacher of Jiangsu University. He graduated from Suzhou Machinery Industrial University in Industrial Enterprise Management in 1992. He has been conferred the Prize of Technology Development in Shazhou County (沙州縣科學技術進步獎) in 1984. He joined the Company in September 1998.

Mr. HOU Cheng Bao (侯成保), aged 51, is an executive Director of the Company. Mr. HOU holds the title of engineer. He was formerly the head of general manager's office of Jiangsu Mudan for the period from January 1996 to August 1998. He graduated from Zhenjiang Agricultural Machinery College in machinery production and engineering in 1978. Mr. HOU is now responsible for the foreign investment project of the Company. He has extensive years of experience in the production management. He joined the Company in September 1998.

Mr. JIANG Wei Sheng (姜渭生), aged 47, is an executive Director of the Company. He is responsible for the oversea market of the Company. He was formerly the deputy section head of the production development of Jiangsu Mudan for the period from January 1996 to March 1997. He is currently the director and manager of Zhangjiagang Mudan Bus Parts Co., Ltd. ("ZMBPC"), a non-wholly owned subsidiary of Jiangsu Mudan, for the period from April 1997 to March 2002. He graduated from Le Yu Middle School in Zhangjiagang City in 1972. He has over 22 years of experience in enterprise management and automobile production. He joined the Company in September 1998.

Profiles of Directors, Supervisors and Senior Management

Non-executive Director

Madam YOU Lian Qun (游聯群), aged 40, is a non-executive Director. She is the chairman and legal representative of Zhangjiagang Automobile Accessories Factory (“ZAAF”), with a shareholding of approximately 12.3% in ZAAF. She graduated from Jiangsu Chinese Communist Party College with a diploma. Prior to joining the Company in September 1998, she was the deputy general manager and director of Jiangsu Mudan for the period from January 1996 to August 1998.

Independent non-executive Directors

Mr. ZHANG Xiao Yu (張小虞), aged 58, is an independent non-executive Director who joined the Company in July 2002. Mr. ZHANG holds the title of senior engineer. He is the vice-chairman of the China Machinery Industrial Association since April 2002. Prior to April 2002, Mr. ZHANG had been the deputy commissioner of SMIB, the chief of Automobile Industry Division of MMI, the deputy chief economist and the chief of the State Plan Division in China Automobile Industry Group Company, and the engineer of Automobile General Bureau of China First Engineering Industry Ministry. He obtained a bachelor’s degree in automobile engineering from Tsing Hua University.

Mr. WU Chang Fa (吳長發), aged 63, is an independent non-executive Director who joined the Company in July 2002. He was the deputy chief at the Changchun Automobile Research Institute (長春汽車研究所). He holds the title of senior engineer. He has been conferred the first prize for State Scientific Technology Advancement (國家科技進步一等獎) for automobile development in 1982 and 1988. In 1994, Mr. WU has also been conferred the title of Machinery Industrial Scientific Technology Specialist of the PRC (中國機械工業科技專家) from MMI. Prior to joining the Company, he was the deputy head of State Automobile Standard Committee. Mr. WU graduated from Jilin Industrial University in 1965 with a bachelor degree in automobile design.

Supervisors

Mr. ZHU Xia Zheng (朱俠征), aged 51, is the chairman of supervision department of the Company. He graduated from Nanjing University in History in 1977. He was formerly the deputy secretary of the Commission of Communist Party of Jiangsu Mudan. He joined the Company in September 1998.

Mr. DING Shao Hua (丁少華), aged 44, is the supervisor of the Company. He graduated from Shanxi Broadcasting and Television University in 1987. He was formerly the vice-chairman of the Union and a committee member of Political Consultant Committee of Zhangjiagang City. He joined the Company in September 1998.

Mr. JIN Hong (金洪), aged 42, is the supervisor of the Company. He joined the Company in September 1998. He graduated from Le Yu Middle School in Zhangjiagang City in 1977. He was formerly the section head of the servicing department of Jiangsu Mudan for the period from January 1996 to August 1998.

Senior management

Mr. FAN Hong Xing (樊紅星), aged 35, is general manager assistant of the Company, he holds the title of economist. He is currently in charge of making operating program, integrate layout, enterprise rules, examine & management, cost, interior audit, quality control and etc. He majored in Enterprise Management and graduated from Shazhou Technical college in 1988. Prior to joining to the Company, he was the deputy factory director of factory No. 1 of Jiangsu Mudan, head of enterprise management department of the Company, vice manager of sales & marketing department, deputy director of factory No. 2, factory director of factory No.3 and head of

Profiles of Directors, Supervisors and Senior Management

manufacture department III. He has been awarded “Labor model of Zhangjiagang city” (張家港市勞動模範) and “Zhangjiagang advanced technology operator” (張家港市先進科技工作者). In 2002, he has been awarded as “Third prize of Technology Development in Zhangjiagang” (張家港市科學技術進步三等獎). He joined the Company in September 1998.

Mr. SHI You Liang (施友良), aged 45, is general manager assistant of the Company. He now is in charge of the sales & marketing department, after sales services, technology management. Prior to joining to the Company, he was the factory director of factory No. 7 of Jiangsu Mudan, factory director of factory No.2 and head of manufacture department I of the Company. He joined the Company in September 1998.

Mr. XU Hong Bing (徐宏兵), aged 32, is the head of the general manager’s office and head of human resources department of the Company. He holds the title of economist. Mr. Xu graduated from Jiangsu Technical University with a bachelor degree in mechanical engineering in 1995. He is currently studying for a master degree in mechanical engineering in Jiangsu Technical University. He has been awarded as “advanced individual in human resources job in Zhangjiagang City” (張家港市人事工作先進個人), “Top Hundred Suzhou civilization employees” (蘇州市百佳文明職工). He is also a member of Youth League of Zhangjiagang. Prior to joining the Company, he was the section head of the staff training department, vice director of the administration office, vice director of the capital management office in Jiangsu Mudan. He joined the Company in September 1998.

Mr. LI Jing Shan (李京山), aged 31, is the manager of the enterprise management department of the Company. He holds the title of economist. He graduated from Huaiyin Industrial Professional Training School, with a diploma in mechanical engineering in 1993. Mr. Li has over 9 years’ experience in enterprise management. He was formerly the member of the staff disciplinary committee, section head of audit ministry, deputy director of enterprise management office of Jiangsu Mudan. He joined the Company in September 1998.

Mr. HE Wen Ge (何文鵠), aged 36, is the head of production and provider department of the Company. He holds the title of economist. He major in automobile engineering and graduated from Jiangsu Technical University in 1987. Prior to joining the Company in September 1998, Mr. He was the deputy factory director of Factory No.1 and Factory No.7, vice manager of sales & marketing department of the Company of Jiangsu Mudan.

Mr. TANG Wei Dong (唐衛東), aged 34, is the manager of finance and investment department of the Company. He holds the title of statistician. He graduated from Jiangsu Broadcasting and Television University, with a diploma in finance and accounting in 1995. Prior to joining the Company in September 1998, Mr. TANG was the section head of finance department and chief of human resources section of Factory No.7 of Jiangsu Mudan for the period from January 1996 to August 1998.

Mr. LIU Jian Zhong (劉建忠), aged 37, is the head of R&D department. He hold the title of engineer. He graduated from Jiangsu Technical University in 1987. Prior to joining the Company in September 1998, he was the director of the products office of the R&D department of the Company. He has been awarded as “Third Prize of Technology Development in Zhangjiagang” (張家港市科學技術進步三等獎), “Top Ten Technology Model in Zhangjiagang City” (張家港市十佳青年科技標兵), “Zhangjiagang Excellence Youth Technician” (張家港市優秀中青年專業技術人員), “Specialist of Suzhou Automobile Engineer Association” (蘇州市汽車工程學會專家).

Mr. CHEN Jiang Ming (陳建明), aged 39, is the head of manufacture department I. Prior to joining the Company in September 1998, he was the deputy section chief of the financial office of Jiangsu Mudan, factory director of factory No. 2 of the Company, deputy manager of sales & marketing department. He graduated from Leyu middle school in Zhangjiagang city in 1977.

Profiles of Directors, Supervisors and Senior Management

Mr. CAO Quan (曹泉), aged 47, is the head of manufacture department II. Prior to joining the Company in September 1998, he has been the manager of sales & marketing department of the Company. He was the deputy section head of sales department of Jiangsu Mudan for the period from January 1996 to August 1998. He graduated from Le Yu Dong Jiegang Middle School in Zhangjiagang City in 1972.

Mr. CHEN Yong Xiang (陳永祥), aged 41, is the head of manufacture department III. He graduated from Jiangsu Broadcasting and Television University in 1983. Prior to joining the Company in September 1998, he was the deputy factory director of factory No. 3 of Jiangsu Mudan for the period from January 1996 to August 1998.

Qualified accountant and company secretary

Mr. LUI Wing Hong (呂榮匡), Edward, aged 40, is a financial controller, company secretary and the qualified accountant of the Company. He is responsible for the financial and accounting management and secretarial affairs of the Company. He graduated from York University with a Bachelor of Arts degree in Business and Economics. He further obtained a postgraduate diploma in Financial Management from the University of New England. Mr. Lui is an associate member of the Australian Society of Certified Practising Accountants and the fellow of Hong Kong Society of Accountants. He has over 10 years of experience in, accounting, taxation and financial management in Hong Kong and the PRC. He joined the Company in September 2001.

Compliance officer

Mr. SHAO Zhi Nan (邵志南). For details, please refer to the paragraph headed "Executive Directors" above. Mr. Shao will be advising on and assisting the Board in implementing procedures to ensure that the Company complies with the GEM Listing Rules and other relevant laws and regulations applicable to the Company and responding promptly and efficiently to all enquires directed to him by the Stock Exchange.

Notice of Annual General Meeting

NOTICE IS HEREBY GIVEN that the 2002 annual general meeting (“AGM”) (or at any adjournment thereof) of Mudan Automobile Shares Company Limited (the “Company”) will be held at “JuXian” Hall, 3rd Floor, No. 1 Building, Guomao Hotel, 42 Renminzhong Road, Yangshe Town, Zhangjiagang City, Jiangsu Province, the People’s Republic of China (“PRC”) on Monday, 26 May 2003 at 9:00 a.m. for the following purposes:

- I. To consider and if thought fit, pass the following matters as ordinary resolutions:
 - (1) To consider and approve the report of the board of Directors of the Company (“the Board”) for the year 2002;
 - (2) To consider and approve the report of the supervisory committee of the Company for the year 2002;
 - (3) To consider and approve the audited financial statements of the Company for the year ended 31 December 2002;
 - (4) To consider and approve the proposal of re-appointment of KPMG and KPMG Peat Marwick Huazhen as the Company’s international and domestic auditors respectively for the year 2003 and to authorise the Board to fix their remuneration;
 - (5) To consider and approve a final dividend distribution proposal of the Company for the year 2002;
 - (6) To consider and approve the appropriation to statutory surplus reserve and statutory public welfare fund and other reserve for the year 2002;
 - (7) To consider and re-approve the various continuing connected transactions carried out during the year ended 31 December 2002, pursuant to the Raw Materials Supply Agreement which was entered by the Company and Jiangsu Mudan Automobile Group Company Limited (“Jiangsu Mudan”), Zhangjiagang Mudan Bus Parts Co. Ltd, Zhangjiagang Mudan Automobile Accessories Co. Ltd, Zhangjiagang Mudan Bus Body Stamping Co. Ltd and Zhangjiagang Automobile Accessories Factory (together, “the Suppliers”) on 8 October 2001, for the supplying to the Company of automobile parts and components which are required for the production of the Company’s products, and the cap amount. For the year ended 31 December 2002, the aggregate amount relating to aforementioned connected transactions amounts to RMB36,931,833 which is below the annual cap amount of RMB107,000,000 as set out in the letter dated 3 December 2001 issued by the GEM of the Stock Exchange of Hong Kong Limited (the “Waiver letter”), a copy of which is produced at the AGM and marked “A” by the chairman of the AGM for identification;
 - (8) To consider and re-approve a connected transaction carried out during the year ended 31 December 2002, pursuant to the PRC Sales Agency Agreement between the Company and Jiangsu Mudan on 8 October 2001, for appointing Jiangsu Mudan to act as its non-exclusive agent for the sale of Company’s product in PRC and paying an agency fee to Jiangsu Mudan, and the cap amount. For the year ended 31 December 2002, the total agency fee paid to Jiangsu Mudan was RMB NIL which is below the annual cap amount of RMB6,000,000 as set out in the Waiver letter;
 - (9) To consider and elect director(s).
- II. To consider and if thought fit, pass the following matters as special resolutions:

Special resolutions:

 - (1) That, subject to the granting of the necessary approval by China Securities Regulatory Commission, The Stock Exchange of Hong Kong Limited and other regulatory bodies,

Notice of Annual General Meeting

additional issuing and/or placing of domestic shares and/or H shares by the Company be and is hereby approved, the number of which shall not exceed 20% of the number of such shares in issue; and that the Board is hereby authorized to deal with all the matters relating to the above additional issue and/or placing.

That the above approval and authorization shall be valid for a period of 12 months from the date of passing the resolution, unless revocation or variation of the above approval and authorization is passed by a special resolution in general meeting.

- (2) If the aforesaid resolution is passed and implemented by the Board, authorise the Board to amend the relevant articles of the Company's Articles of Association to reflect the change of the shareholding structure of the Company.
- III. To consider and approve any proposals put forward by any shareholders holding 5% or more of the shares with voting rights at such meeting (if any).

By Order of the Board
Mudan Automobile Shares Company Limited
SUN Min Biao
Chairman

Zhangjiagang City, Jiangsu Province, the PRC
20 March 2003

Notes:

1. The register of the members of the Company will be closed from Saturday, 26 April 2003 to Sunday, 25 May 2003 (both days inclusive). No transfer of shares will be registered during this period. Holders of domestic shares and H shares whose names appear on the register of the Company before 4:00 p.m. Friday, 25 April, 2003 are entitled to attend and vote at the meeting mentioned above and may appoint one or more proxies to attend and, in the event of a poll, vote on their behalf. However, only the Independent shareholders for resolution No.I(7), only the shareholders who are not connected with the Suppliers and their respective associates (as defined in the GEM listing rules) and for resolution No.I(8), only the shareholders who are not connected with Jiangsu Mudan and its associates (as defined in the GEM listing rules) are entitled to vote for (against) the resolution No.I(7) or/and No.I(8) at the AGM. Shareholders may appoint one or more proxies to attend and, in the event of a poll, vote on their behalf. A proxy need not be a member of Shareholders of the Company.
2. A proxy form applicable to the AGM is hereinwith enclosed. In order to be valid, the proxy form, under which it is signed, must be deposited by hand or post, for holders of H Shares of the Company at the H shares registrar of the Hong Kong Registrars Limited at Rooms 1901-5, 19th Floor, Hopewell Center, 183 Queen's Road East, Hong Kong and, for holders of Domestic Shares, to the registered address of the Company not less than 24 hours before the time for holding the AGM or not less than 24 hours before the time appointed for taking the poll. If the proxy form is signed by a person under a power of attorney or other authority, a notarially certified copy of that power of attorney or authority shall be deposited at the same time as mentioned in the proxy form.
3. Shareholders or their proxies shall produce their identity documents when attending the meeting.
4. The final dividend for the year ended 31 December, 2002 is expected to be paid on or before Friday, 1 August, 2003 to the shareholders whose names appear on the register of the Company as at 4:00 p.m. on Thursday, 1 May, 2003. In order to ascertain the identity of shareholders who are entitled to receive the above dividend, all transfers of documents together with the relevant share certificates should be deposited at the share register of the Company (for holders of H shares) or to the Company (for holders of domestic shares) before 4:00 p.m. Friday, 25 April 2003.
5. Shareholders who intend to attend the AGM should complete and return the enclosed reply slip and return it by hand or post to the share registrar of the Company (for holders of H shares) or to the registered address of the Company (for holders of domestic shares) before 4:00 p.m. Tuesday, 6 May, 2003.
6. The AGM is expected to take half a day. Shareholders attending the Meeting shall be responsible for their own travel and accommodation expenses.
7. The registered address of the Company and the details of the secretarial office of the Board are as follows:

No. 30 Lehong Road
Le Yu Town
Zhangjiagang City
Jiangsu Province
The PRC
Tel: (512) 5860 5010
Fax: (512) 5866 0321
Post Code: 215621

Auditors' Report

Auditors' report to the shareholders of
Mudan Automobile Shares Company Limited

(Established as a joint-stock company in The People's Republic of China with limited liability)

We have audited the financial statements on pages 29 to 54 which have been prepared in accordance with International Financial Reporting Standards.

Respective responsibilities of directors and auditors

The company's directors are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently, that judgements and estimates are made which are prudent and reasonable and that the reasons for any significant departure from applicable accounting standards are stated.

It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion, the financial statements give a true and fair view of the state of affairs of the company as at 31 December 2002 and of the company's profit and cash flows for the year then ended and have been properly prepared in accordance with International Financial Reporting Standards and the disclosure requirements of the Hong Kong Companies Ordinance.

KPMG

Certified Public Accountants

Hong Kong, 20 March 2003

Income Statement

for the year ended 31 December 2002

(Expressed in Renminbi Yuan)

	Note	2002	2001
Revenue	3	888,526,140	857,038,069
Cost of sales	4	(780,226,789)	(750,295,261)
Gross profit		108,299,351	106,742,808
Other operating income	5	1,486,317	5,829,036
Distribution expenses	6	(25,096,843)	(25,710,585)
General and administrative expenses		(13,805,192)	(8,373,848)
Other operating expenses		(802,750)	(815,646)
Profit from operations		70,080,883	77,671,765
Net finance costs	8(a)	(1,498,461)	(4,539,496)
Profit before tax	8	68,582,422	73,132,269
Income tax expense	9(a)	(20,909,723)	(23,702,448)
Profit attributable to shareholders		47,672,699	49,429,821
Dividends attributable to the year:	10		
Interim dividend declared during the year		–	48,805,282
Final dividend proposed after the balance sheet date		4,272,000	8,544,000
		4,272,000	57,349,282
Basic earnings per share	11	0.17	0.24

The notes on pages 34 to 54 form part of these financial statements.

Statement of Changes in Equity

for the year ended 31 December 2002

(Expressed in Renminbi Yuan)

	Note	Share capital (Note 26(a))	Share premium (Note 26(b))	Statutory surplus reserve (Note 26(c))	Statutory public welfare fund (Note 26(d))	Retained earnings	Total capital and reserves
Balance at 1 January 2001		204,300,000	–	6,016,907	6,016,906	46,406,568	262,740,381
Issue of share capital		80,500,000	15,977,479	–	–	–	96,477,479
Costs of issuing shares		–	(15,977,479)	–	–	(8,915,126)	(24,892,605)
Deferred tax effect in respect of the costs of issuing shares	16	–	–	–	–	2,941,992	2,941,992
Net profit for the year		–	–	–	–	49,429,821	49,429,821
Transfer to/(from) reserve		–	–	4,630,991	4,630,992	(9,261,983)	–
Dividends declared in respect of the current year	10	–	–	–	–	(48,805,282)	(48,805,282)
Balance at 31 December 2001		284,800,000	–	10,647,898	10,647,898	31,795,990	337,891,786
Balance at 1 January 2002		284,800,000	–	10,647,898	10,647,898	31,795,990	337,891,786
Dividends approved in respect of previous year	10	–	–	–	–	(8,544,000)	(8,544,000)
Deferred tax assets in respect of the costs of issuing shares realised during the year	16	–	–	–	–	(1,470,996)	(1,470,996)
Net profit for the year		–	–	–	–	47,672,699	47,672,699
Transfer to/(from) reserve		–	–	4,517,948	4,517,948	(9,035,896)	–
Balance at 31 December 2002		284,800,000	–	15,165,846	15,165,846	60,417,797	375,549,489

The notes on pages 34 to 54 form part of these financial statements.

Balance sheet

at 31 December 2002

(Expressed in Renminbi Yuan)

	Note	2002	2001
Non-current assets			
Property, plant and equipment	14	177,332,713	177,719,337
Construction in progress	15	428,000	–
Deferred tax assets	16	1,611,772	5,047,112
Total non-current assets		179,372,485	182,766,449
Current assets			
Inventories	17	165,337,068	64,830,391
Trade and other receivables	18	236,705,417	170,728,649
Amounts due from a shareholder	19	10,180,064	56,210,314
Amount due from a related company	19	–	501,841
Pledged deposits	20	59,431,080	31,920,018
Investments in unit trusts	21	491,500	–
Cash and cash equivalents	22(a)	92,594,293	91,159,940
Total current assets		564,739,422	415,351,153
Current liabilities			
Short-term bank loans (unsecured)	23	20,000,000	13,000,000
Trade and other payables	24	317,732,756	181,683,611
Amounts due to shareholders	19	2,651,730	4,289,807
Income tax payable		8,177,932	41,252,398
Total current liabilities		348,562,418	240,225,816
Net current assets		216,177,004	175,125,337
Total assets less current liabilities		395,549,489	357,891,786
Non-current liabilities			
Long-term bank loan (secured)	25	20,000,000	20,000,000
Total non-current liabilities		20,000,000	20,000,000
Net assets		375,549,489	337,891,786

Balance sheet

at 31 December 2002

(Expressed in Renminbi Yuan)

	Note	2002	2001
Equity and liabilities			
Share capital	26(a)	284,800,000	284,800,000
Statutory surplus reserve	26(c)	15,165,846	10,647,898
Statutory public welfare fund	26(d)	15,165,846	10,647,898
Retained earnings	26(e)	60,417,797	31,795,990
Total capital and reserves		375,549,489	337,891,786

Approved and authorised for issue by the board of directors on 20 March 2003

)	
SUN Min Biao)	
)	Directors
SHAO Zhi Nan)	
)	

The notes on pages 34 to 54 form part of these financial statements.

Cash flow statement

for the year ended 31 December 2002

(Expressed in Renminbi Yuan)

	Note	2002	2001
Operating activities			
Profit before tax		68,582,422	73,132,269
Depreciation		14,622,910	15,042,675
Unrealised loss on investments in unit trusts		13,500	–
Write off of obsolete inventories		–	747,646
Waiver of an amount due to a related company		–	(2,706,331)
Interest expense (net)		1,285,254	4,492,622
(Increase)/decrease in inventories		(100,506,677)	20,832,147
Increase in trade and other receivables		(65,976,768)	(5,547,424)
Decrease in amounts due from/(to) shareholders		27,373,585	57,144,415
Decrease/(increase) in amount due from/(to) a related company		501,841	(20,211,204)
Increase in trade and other payables		135,493,222	4,161,915
Interest paid		(2,523,277)	(3,728,481)
Income tax paid		(35,001,257)	(1,000,000)
Cash flows from operating activities		43,864,755	142,360,249
Investing activities			
Acquisition of property, plant and equipment		(12,988,063)	(4,968,617)
Acquisition of construction in progress		(1,120,300)	–
Acquisition of investments in unit trusts		(505,000)	–
Interest received		1,238,023	305,094
Increase in pledged deposits		(27,511,062)	(30,112,818)
Cash flows from investing activities		(40,886,402)	(34,776,341)
Financing activities			
Net proceeds from the issue of share capital		–	66,817,300
Repayment to a shareholder		–	(92,680,000)
Proceeds from bank loans		20,000,000	121,320,000
Repayment of bank loans		(13,000,000)	(88,320,000)
Dividends paid		(8,544,000)	(48,805,282)
Cash flows from financing activities		(1,544,000)	(41,667,982)
Net increase in cash and cash equivalents		1,434,353	65,915,926
Cash and cash equivalents at beginning of year		91,159,940	25,244,014
Cash and cash equivalents at end of year	22(a)	92,594,293	91,159,940

The notes on pages 34 to 54 form part of these financial statements.

Notes on the financial statements

(Expressed in Renminbi Yuan)

1 Background of the company

The company was established in the People's Republic of China (the "PRC") on 18 September 1998 as a joint stock company with limited liability. The company's principal activities are the manufacture and sales of automobiles.

2 Significant accounting policies

(a) Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") promulgated by the International Accounting Standards Board and the disclosure requirements of the Hong Kong Companies Ordinance. IFRS includes International Accounting Standards and interpretations. These financial statements also comply with the applicable disclosure provisions of the Listing Rules of the Growth Enterprise Market ("GEM") of The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). A summary of the significant accounting policies adopted by the company is set out below.

(b) Basis of preparation

The measurement basis used in the preparation of the financial statements is historical cost modified by the marking to market of investments in unit trusts as explained in the accounting policy set out below.

The accounting policies have been consistently applied by the company and are consistent with those used in the previous year.

(c) Property, plant and equipment

(i) Owned assets

Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses (note 2(i)).

Where an item of property, plant and equipment comprises major components having different useful lives, they are accounted for as separate items of property, plant and equipment.

(ii) Subsequent expenditure

Expenditure incurred to replace a component of an item of property, plant and equipment that is accounted for separately, is capitalised with the carrying amount of the component being written off. Other subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the item of property, plant and equipment. All other expenditure is recognised in the income statement as an expense as incurred.

Notes on the financial statements

(Expressed in Renminbi Yuan)

2 Significant accounting policies (continued)

(c) Property, plant and equipment (continued)

(iii) Depreciation

Depreciation is calculated to write off the cost on a straight-line basis over the estimated useful lives of items of property, plant and equipment, as follows:

Buildings	35 years
Plant and equipment	12 years
Motor vehicles	8 years
Other equipment	8 years

(iv) Disposals

Gains or losses arising from the retirement or disposal of a property, plant and equipment are determined as the difference between the estimated net disposal proceeds and the carrying amount of the asset and are recognised in the income statement on the date of retirement or disposal.

(d) Construction in progress

Construction in progress represents items of property, plant and equipment under construction and pending installation and is stated at cost less impairment losses (note 2(i)). Cost comprises direct costs of construction.

Capitalisation of these costs ceased and the construction in progress is transferred to property, plant and equipment when the asset is substantially ready for its intended use.

No depreciation is provided in respect of construction in progress.

(e) Investments in unit trusts

Unit trusts held for trading are classified as current assets and are stated at fair value, with any resultant gain or loss recognised in the income statement.

The fair value of unit trusts is their bid price quoted by the investment managers at the balance sheet date.

Unit trusts held for trading are recognised/derecognised by the company on the date it commits to purchase/sell the investments.

(f) Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value represents the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

Notes on the financial statements

(Expressed in Renminbi Yuan)

2 Significant accounting policies (continued)

(f) Inventories (continued)

The cost of inventories is calculated based on the weighted-average costing method and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition.

When inventories are sold, the carrying amount of those inventories is recognised as an expense in the period in which the related revenue is recognised. The amount of any write-down of inventories to net realisable value and all losses of inventories is recognised as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realisable value, is recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

(g) Trade and other receivables

Trade and other receivable are stated at their cost less allowance for doubtful accounts. An allowance for doubtful accounts is provided based upon the evaluation of the recoverability of these accounts at the balance sheet date.

(h) Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the company's cash management are included as a component of cash and cash equivalents for the purpose of cash flow statement.

(i) Impairment

The carrying amounts of the company's assets, other than investments in unit trusts (note 2(e)), inventories (note 2(f)), trade and other receivables (note 2(g)) and deferred tax assets (note 2(n)), are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement.

(i) Calculation of recoverable amount

The recoverable amount of an asset is the greater of their 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. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

(ii) Reversals of impairment

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Notes on the financial statements

(Expressed in Renminbi Yuan)

2 Significant accounting policies (continued)

(j) Provisions

A provision is recognised in the balance sheet when the company has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

(k) Revenue recognition

(i) Sale of goods

Revenue from the sale of goods is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer. No revenue is recognised if there are significant uncertainties regarding recovery of the consideration due, associated costs or the possible return of goods, or when the amount of revenue and the costs incurred or to be incurred in respect of the transaction cannot be measured reliably.

(ii) Service income/management fee

Service income/management fee is recognised when the relevant services are provided.

(l) Borrowing costs

Borrowing costs are expensed in the income statement in the period in which they are incurred.

(m) Expenses

(i) Retirement benefits

Obligations for contributions to defined contribution retirement benefit scheme are recognised as an expense in the income statement as and when incurred.

(ii) Net finance costs

Net finance costs comprise interest payable on borrowings calculated using the effective interest rate method, interest receivable on funds invested, bank charges and foreign exchange gains and losses that are recognised in the income statement.

Interest income is recognised in the income statement as it accrues, taking into account the effect yield on the asset.

(iii) Warranty costs

Warranty costs are charged to the income statement as and when incurred.

(iv) Research and development costs

Research and development costs are charged to the income statement as and when incurred.

Notes on the financial statements

(Expressed in Renminbi Yuan)

2 Significant accounting policies (continued)

(m) Expenses (continued)

(v) Operating lease payments

Payments made under operating leases are recognised in the income statement on a straight-line basis over the term of the respective leases. Lease incentives received are recognised in the income statement as an integral part of the total lease expense.

(n) Income tax

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly to equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Initial recognition of assets or liabilities that affect neither accounting nor taxable profit is regarded as temporary difference which is not provided for. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(o) Foreign currencies transactions

Transactions in foreign currency are translated to Renminbi at the foreign exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to Renminbi at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement.

(p) Dividends

Dividends are recognised as a liability in the period in which they are declared.

(q) Segment reporting

A segment is a distinguishable component of the company that is engaged either in providing products (business segment), or providing products within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

Notes on the financial statements

(Expressed in Renminbi Yuan)

2 Significant accounting policies (continued)

(r) Related parties

For the purposes of these financial statements, parties are considered to be related to the company if the company has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the company and the party are subject to common control or common significant influence. Related parties may be individuals or other entities.

3 Revenue and segmental information

The principal activities of the company are the manufacture and sales of automobiles in the PRC. Revenue represents income arising from the sales of automobiles net of value added tax.

The directors consider the company operates within a single business and geographical segment.

4 Cost of sales

	2002	2001
Materials costs	725,102,720	694,916,914
Direct labour	30,642,054	26,775,082
Factory overheads	24,482,015	28,603,265
	780,226,789	750,295,261

5 Other operating income

	2002	2001
Sale of scrap materials	444,893	2,913,907
Service fee	349,338	–
Management fee	200,000	30,000
Waiver of an amount due to a related company	–	2,706,331
Other income	492,086	178,798
	1,486,317	5,829,036

6 Distribution expenses

	2002	2001
Staff costs	12,703,118	3,691,024
Travelling and transportation expenses	6,859,700	1,336,837
Advertising and promotion expenses	2,608,041	1,334,561
Entertainment expenses	1,857,441	271,312
Distribution fees paid to a related company	–	11,672,011
Commission paid	–	6,068,689
Others	1,068,543	1,336,151
	25,096,843	25,710,585

Notes on the financial statements

(Expressed in Renminbi Yuan)

7 Personnel expenses

	2002	2001
Salaries, wages and bonus	46,394,011	29,554,054
Staff welfare	7,460,365	4,687,298
Contributions to retirement benefit scheme	2,036,539	1,810,350
	55,890,915	36,051,702
Average number of employees during the year	2,179	2,105

Pursuant to the relevant labour regulations of the PRC, the company participates in a defined contribution retirement plan organised by the municipal government for its employees. The company is required to make contributions to the retirement plan at 18% (2001: 18%) of the deemed salary rates stipulated by the municipal government. Retired employees are entitled to a pension equal to a fixed proportion of the salary prevailing at the retirement date payable by the Zhangjiagang Society Protection Management Department. The company has no other material obligation for the payment of pension benefits beyond the annual contributions described above.

8 Profit before tax

Profit before tax is arrived at after charging/(crediting):

	2002	2001
(a) Net finance costs:		
Interest on bank advances and other borrowings repayable within five years	2,523,277	4,797,716
Bank charges	213,207	46,874
Interest income	(1,238,023)	(305,094)
	1,498,461	4,539,496
(b) Other items:		
Auditors' remuneration	1,049,400	1,145,448
Depreciation	14,622,910	15,042,675
Operating lease rentals in respect of land use rights and properties	1,370,434	560,000
Research and development expenses	844,054	550,665

Notes on the financial statements

(Expressed in Renminbi Yuan)

9 Income tax expense

(a) Income tax expense represents:

	2002	2001
Current tax expense	21,050,499	23,702,448
Deferred tax (note 16)	(140,776)	–
	20,909,723	23,702,448

The provision for PRC income tax is calculated at the unified tax rate of 33% (2001: 33%) of the estimated assessable income for the year as determined in accordance with the relevant income tax rules and regulations of the PRC.

(b) The following is a reconciliation of income taxes calculated at the applicable tax rate with income tax expense:

	2002	2001
Accounting profit before tax	68,582,422	73,132,269
Income tax expense computed by applying tax rate of 33%	22,632,199	24,133,649
Over-provision in respect of prior years	–	(431,201)
Non-deductible expenses	4,455	–
Deferred tax assets realised and charged directly to retained earnings	(1,470,996)	–
Tax allowance granted	(255,935)	–
Income tax expense	20,909,723	23,702,448

10 Dividends

(a) Dividends attributable to the year

	2002	2001
Interim dividend declared and paid of RMB Nil per share (2001: a special dividend of RMB0.24 per share)	–	48,805,282
Final dividend proposed after the balance sheet date of RMB0.015 per share (2001: RMB0.03)	4,272,000	8,544,000
	4,272,000	57,349,282

The final dividend proposed after the balance sheet date has not been recognised as a liability at the balance sheet date.

Notes on the financial statements

(Expressed in Renminbi Yuan)

10 Dividends (continued)

(b) Dividends attributable to the previous financial year, approved and paid during the year

	2002	2001
Final dividend in respect of the previous financial year, approved and paid during the year, of RMB0.03 per share (2001: RMB Nil per share)	8,544,000	–

11 Basic earnings per share

The calculation of basic earnings per share is based on the profit attributable to shareholders of RMB47,672,699 (2001: RMB49,429,821) divided by the weighted average number of shares in issue during the year of 284,800,000 (2001: 207,387,671).

The amount of diluted earning per share is not presented as there were no dilutive potential ordinary shares in existence for both years.

12 Directors' and supervisors' emoluments

Details of directors' and supervisors' emoluments are as follows:

	2002	2001
Fees	190,000	70,000
Basic salaries, allowances and other benefits	155,994	195,895
Discretionary bonuses	679,073	1,225,601
Contributions to retirement benefit scheme	40,615	74,598
	1,065,682	1,566,094
Number of directors and supervisors	11	21

An analysis of directors' and supervisors' emoluments by the number of directors and supervisors and emolument range is as follows:

	2002	2001
RMB Nil – RMB1,000,000	11	21

The executive directors, non-executive directors and supervisors received individual emoluments of approximately RMB Nil (2001: RMB247,110), RMB186,064 (2001: RMB207,110), RMB149,882 (2001: RMB186,933), RMB149,799 (2001: RMB186,814), RMB75,585 (2001: RMB124,648), RMB58,611 (2001: RMB108,910), RMB Nil (2001: RMB4,064), RMB Nil (2001: RMB49,755), RMB Nil (2001: RMB5,762), RMB50,000 (2001: RMB50,000), RMB Nil (2001: RMB4,008), RMB Nil (2001: RMB7,416), RMB129,150 (2001: RMB109,820), RMB67,462 (2001: RMB52,348), RMB59,129 (2001: RMB49,324), RMB Nil (2001: RMB58,820), RMB Nil (2001: RMB26,175), RMB Nil (2001: RMB52,137) and RMB Nil (2001: RMB14,940).

Notes on the financial statements

(Expressed in Renminbi Yuan)

12 Directors' and supervisors' emoluments (continued)

The independent non-executive directors received individual emoluments of approximately RMB20,000 (2001: RMB10,000) and RMB20,000 (2001: RMB10,000), respectively.

The above emoluments also include emoluments paid to former directors of RMB Nil (2001: RMB223,077).

There were no amounts paid during the years ended 31 December 2001 and 2002 to directors and supervisors in connection with their retirement from employment with the company, or inducement to join. There was no waiver of any emoluments by the directors or supervisors during the years ended 31 December 2001 and 2002.

13 Senior management's emoluments

Of the five individuals with the highest emoluments, four (2001: four) are directors whose emoluments are disclosed in note 12 above. The emoluments in respect of the other one (2001: one) individual is as follows:

	2002	2001
Basic salaries, allowances and other benefits	604,750	222,040
Discretionary bonuses	-	-
Contributions to retirement benefit scheme	-	-
	604,750	222,040

The emolument of the one (2001: one) individual with the highest emoluments is within the following band:

	2002	2001
RMB Nil – RMB1,000,000	1	1

There were no amounts (2001: RMB Nil) paid during the year to the one (2001: one) individual with the highest emoluments in connection with their retirement from employment with the company, or inducement to join.

Notes on the financial statements

(Expressed in Renminbi Yuan)

14 Property, plant and equipment

	Buildings	Machinery and equipment	Motor vehicles	Other equipment	Total
Cost:					
Balance at					
1 January 2002	85,886,062	138,948,736	943,528	474,872	226,253,198
Additions	584,452	11,479,586	604,564	319,461	12,988,063
Transfer from construction in progress (note 15)	174,223	1,074,000	–	–	1,248,223
Disposals	–	–	(45,500)	–	(45,500)
Balance at 31 December 2002	86,644,737	151,502,322	1,502,592	794,333	240,443,984
Depreciation and impairment losses:					
Balance at					
1 January 2002	14,729,265	32,992,002	563,192	249,402	48,533,861
Charge for the year	2,458,709	11,824,654	282,091	57,456	14,622,910
Written back on disposal	–	–	(45,500)	–	(45,500)
Balance at 31 December 2002	17,187,974	44,816,656	799,783	306,858	63,111,271
Carrying amount:					
At 31 December 2002	69,456,763	106,685,666	702,809	487,475	177,332,713
At 31 December 2001	71,156,797	105,956,734	380,336	225,470	177,719,337

Upon establishment, all items of property, plant and equipment of the company were revalued by Nanjin Yong Hua, an independent PRC valuer registered in the PRC, on a depreciated replacement cost basis. The value of property, plant and equipment has been determined at RMB163 million. This revaluation was to establish the deemed cost of the property, plant and equipment at the time of the company's establishment.

All of the company's buildings are located in the PRC.

As at 31 December 2002, machineries at net book value totalling RMB37,027,056 (2001: RMB64,791,580) were pledged to secure a long-term bank loan (note 25) (2001: a long-term bank loan and two short-term bank loans).

Notes on the financial statements

(Expressed in Renminbi Yuan)

15 Construction in progress

Balance at 1 January 2002	–
Additions	1,676,223
Transferred to property, plant and equipment (note 14)	(1,248,223)
	–
Balance at 31 December 2002	428,000

16 Deferred tax assets

	2002	2001
Deferred tax assets are attributable to the following:		
Accounting depreciation in excess of tax depreciation	140,776	–
Costs of equity transaction deductible for tax purposes	1,470,996	2,941,992
Provision for accounting purposes	–	2,105,120
	1,611,772	5,047,112
Movements in deferred tax assets:		
At the beginning of the year	5,047,112	2,105,120
Transferred from income statement	140,776	–
Transferred (to)/from retained earnings	(1,470,996)	2,941,992
Transferred to amount due from a shareholder (note 22(b)(i))	(2,105,120)	–
At the end of the year	1,611,772	5,047,112

17 Inventories

Inventories represent:

	2002	2001
Raw materials	54,033,602	26,570,114
Work in progress	34,612,398	14,612,770
Finished goods	76,691,068	23,647,507
	165,337,068	64,830,391

None of the inventories is stated at net realisable value.

Notes on the financial statements

(Expressed in Renminbi Yuan)

18 Trade and other receivables

Trade and other receivables comprise:

	2002	2001
Trade debtors and bills receivable	206,104,879	145,582,753
Advance deposits to suppliers	28,134,949	15,201,581
Other debtors	2,465,589	9,944,315
	236,705,417	170,728,649

An ageing analysis of trade debtors and bills receivable (net of provisions for bad and doubtful debts) is as follows:

	2002	2001
Within 3 months	98,728,832	119,520,832
Over 3 months but less than 6 months	45,255,051	21,850,268
Over 6 months but less than 1 year	49,680,276	3,661,653
Over 1 year but less than 2 years	12,440,720	550,000
Over 2 years	-	-
	206,104,879	145,582,753

Customers are normally granted credit terms of three months to twelve months (2001: three months to six months), depending on the company's assessment of the credit worthiness of individual customers. In addition, certain established customers with good repayment record are allowed to settle by instalments over a period of not more than 18 months (2001: 15 months).

The amount of trade and other receivables expected to be recovered after more than one year is RMB31,450,000 (2001: RMBNil). All other trade and other receivables are expected to be settled within one year.

19 Amounts due from/to shareholders/a related company

Amounts due from/to shareholders/a related company are interest free and have no fixed terms of repayment. The balances arose from the related party transactions are disclosed in note 29.

20 Pledged deposits

The deposits are pledged with banks for certain bills facilities granted to the company.

21 Investments in unit trusts

	2002	2001
Unit trusts held for trading, at investment manager's valuation	491,500	-

Notes on the financial statements

(Expressed in Renminbi Yuan)

22 Cash and cash equivalents

(a) Analysis of the balances of cash and cash equivalents is set out below:

	2002	2001
Deposits with banks	67,467,009	66,817,800
Cash at bank and in hand	25,127,284	24,342,140
	92,594,293	91,159,940

(b) Non-cash transactions

- (i) Historically, income tax liabilities of the company and its shareholder, Jiangsu Mudan Automobile Group Company Limited ("Jiangsu Mudan") were assessed by the Zhangjiagang Municipal Tax Bureau on a combined basis. According to a tax notice issued by the Zhangjiagang Municipal Tax Bureau during the years ended 31 December 2002, income tax liabilities of the company in respect of the years ended 31 December 1999 and before totalling RMB19,123,708, had been paid by Jiangsu Mudan. In addition, Jiangsu Mudan was also utilised certain deferred tax assets of the company which amounted to RMB2,105,120. The related income tax liabilities and deferred tax assets were settled through the current account with Jiangsu Mudan without cash payment/receipt.
- (ii) During the year ended 31 December 2001, the company transferred certain property, plant and equipment, which were not primarily employed for the operations of the company, with an aggregate net book value of RMB495,182 to Jiangsu Mudan at their net carrying values, the consideration of which was satisfied by a set off of an equivalent amount against the amount due to Jiangsu Mudan.
- (iii) During the year ended 31 December 2001, an amount of RMB2,706,331 due to a related company was waived and is included in the income statement for the year then ended as other operating income (note 5).

23 Short-term bank loans

	2002	2001
Unsecured bank loans	20,000,000	13,000,000

Details of the short-term bank loans as at 31 December 2002 are as follows:

Principal	Interest rate	Loan period
10,000,000	5.04% p.a.	16 August 2002 to 16 February 2003
10,000,000	4.2% p.a.	1 December 2002 to 18 March 2003
<u>20,000,000</u>		

Notes on the financial statements

(Expressed in Renminbi Yuan)

24 Trade and other payables

Trade and other payables comprise:

	2002	2001
Trade creditors	86,144,676	83,194,175
Bills payable	191,630,000	36,470,000
Accrued salaries, bonus and welfare fund	16,065,740	14,182,595
Other payables	23,892,340	47,836,841
	317,732,756	181,683,611
An ageing analysis of trade creditors and bills payable is as follows:		
Due within 3 months	188,774,676	117,394,175
Due after 3 months within 6 months	89,000,000	2,270,000
	277,774,676	119,664,175

25 Long-term bank loan

	2002	2001
Secured bank loan	20,000,000	20,000,000

Details of the long-term bank loan as at 31 December 2002 are as follows:

Principal	Interest rate	Loan period	Security
20,000,000	6.534% p.a.	28 March 2001 to 28 March 2003	Pledge over machinery (note 14)

The above bank loan with an original term of over one year and repayable on 28 March 2003 remains classified as a non-current liability in the balance sheet as an agreement has been reached with the banker subsequently to refinance the loan on a long term basis.

Notes on the financial statements

(Expressed in Renminbi Yuan)

26 Capital and reserves

(a) Share capital

	2002	2001
Registered, issued and fully paid:		
196,250,000 (2001: 196,250,000) domestic shares of RMB1.00 each	196,250,000	196,250,000
88,550,000 (2001: 88,550,000) H shares of RMB1.00 each	88,550,000	88,550,000
	284,800,000	284,800,000

All the domestic shares and H shares rank pari passu in all material respects.

(b) Share premium

Pursuant to the PRC Company Law, the share premium account was utilised to pay off certain listing costs incurred in connection with the issue of share capital.

(c) Statutory surplus reserve

According to the company's articles of association, the company is required to transfer 10% of its net profit, as determined in accordance with the PRC accounting rules and regulations, to statutory surplus reserve until the reserve balance reaches 50% of the registered capital. The transfer to this reserve must be made before distribution of a dividend to shareholders.

Statutory surplus reserve can be used to make good previous years' losses, if any, and may be converted into share capital by the issued of new shares to shareholders in proportion to their existing shareholdings or by increasing the par value of the shares currently held by them, provided that the balance after such issue is not less than 25% of the registered capital.

For the year ended 31 December 2002, the board of directors proposed the transfer of RMB4,517,948 (2001: RMB4,630,991) to the statutory surplus reserve, being 10% of the current year's net profit determined in accordance with the PRC accounting rules and regulations, subject to the shareholders' approval at the annual general meeting.

(d) Statutory public welfare fund

According to the company's articles of association, the company is required to transfer 10% of its net profits, as determined in accordance with the PRC accounting rules and regulations, to the statutory public welfare fund. This fund can only be utilised on capital items for the collective benefits of the company's employees such as the construction of dormitories, canteen and other staff welfare facilities. This fund is non-distributable other than on liquidation. The transfer to this fund must be made before distribution of a dividend to shareholders.

For the year ended 31 December 2002, the board of directors proposed the transfer of RMB4,517,948 (2001: RMB4,630,992) to the statutory public welfare fund, being 10% of the current year's net profit determined in accordance with the PRC accounting rules and regulations, subject to the shareholders' approval at the annual general meeting.

Notes on the financial statements

(Expressed in Renminbi Yuan)

26 Capital and reserves (continued)

(e) Distributable reserve

Pursuant to the company's articles of association, the net profit of the company for the purpose of profit distribution to shareholders will deem to be the lesser of (i) the net profit determined in accordance with the PRC accounting rules and regulations; and (ii) the net profit determined in accordance with IAS.

Under the PRC Company Law and the company's articles of association, net profit after taxation can be distributed as dividends after allowance has been made for:

- (i) making up cumulative prior years' losses, if any;
- (ii) allocations of 10% after-tax profit, as determined in accordance with the PRC accounting rules and regulations, to the company's statutory surplus reserve until the fund aggregates to 50% of the company's registered capital;
- (iii) allocation of 10% of after-tax profit, as determined in accordance with the PRC accounting rules and regulations, to the company's statutory public welfare fund; and
- (iv) allocations to the discretionary surplus reserve, if approved by the shareholders.

The distributable reserve of the company as at 31 December 2002 amounted to RMB57,178,346 (2001: RMB25,306,762). After the balance sheet date the directors proposed a final dividend of RMB0.015 per share (2001: RMB0.03 per share), amounting to RMB4,272,000 (2001: RMB8,544,000). This dividend has not been recognised as a liability at the balance sheet date.

27 Financial instruments

Financial assets of the company include cash and cash equivalents, pledged deposits, trade and other receivables, investments in unit trusts and amounts due from shareholders and a related company. Financial liabilities of the company include bank loans, trade and other payables, amounts due to shareholders and a related company. The company does not hold or issue financial instruments for trading purposes. The company had no positions in derivatives contracts at 31 December 2001 and 2002. Exposure to credit, interest rate and currency risk arises in the normal course of the company's business.

Notes on the financial statements

(Expressed in Renminbi Yuan)

27 Financial instruments (continued)

(a) Credit risk

Management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all customers requiring credit over a certain amount. The company does not require collateral in respect of financial assets.

At the balance sheet date the company had no significant concentrations of credit risk except for trade receivable from one of its customers. The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet.

Amount due from customer represented more than 10% of the outstanding receivables at each balance sheet date is as follows:

	2002	2001
Guangzhou Bai Yun Hua Gang Automobile Company (formerly known as "Guangzhou Tian He Hua Gang Automobile Company")	76,788,993	47,995,651

(b) Interest rate risk

The interest rates and terms of repayment of the bank loans of the company are disclosed in notes 23 and 25.

(c) Foreign currency risk

Substantially all the revenue-generating operations of the company are transacted in Renminbi, which is not freely convertible into foreign currencies. On 1 January 1994, the PRC government abolished the dual rate system and introduced a single rate of exchange as quoted by the People's Bank of China. However, the unification of the exchange rate does not imply convertibility of Renminbi into other foreign currencies. All foreign exchange transactions continue to take place either through the People's Bank of China or other institutions authorised to buy and sell foreign currencies. Approval of foreign currency payments by the People's Bank of China or other institutions requires submitting a payment application form together with suppliers' invoices, shipping documents and signed contracts.

Notes on the financial statements

(Expressed in Renminbi Yuan)

27 Financial instruments (continued)

(d) Fair value

The carrying amounts of significant financial assets and liabilities approximate to their respective fair values as at 31 December 2001 and 2002.

The following methods and assumptions were used to estimate the fair value for each class of financial instruments:

- (i) Cash and cash equivalents, pledged deposits, trade and other receivables, investments in unit trusts, trade and other payables, amounts due from/to shareholders and a related company.

The carrying values approximate their respective fair values due to the nature or short term maturity of these instruments.

- (ii) Bank loans

The carrying amount of bank loans approximate its fair value based on the borrowing rates currently available for bank loans with similar terms and maturity.

28 Commitments

At 31 December 2002, the total future minimum lease payments under non-cancellable operating leases are as follows:

	2002	2001
Less than one year	560,000	560,000
Between one and five years	2,240,000	2,240,000
More than five years	7,700,000	8,260,000
	10,500,000	11,060,000

The company leases rights to use two pieces of land and a property in the PRC under operating leases. The leases run for an initial period of twenty years, with an option to renew the lease after that date. Lease payments are fixed for the initial five years of the term and thereafter be renegotiated every five years to reflect market rentals. None of the leases includes contingent rentals.

Notes on the financial statements

(Expressed in Renminbi Yuan)

29 Material related party transactions

Particulars of material transactions between the company and certain related parties in which a director or a shareholder of the company is in a position to exercise significant influence are as follows:

	Note	2002	2001
Purchases from shareholders/a related company	(i)	36,913,833	47,089,093
Rent paid for land use rights	(ii)	460,000	460,000
Rent paid for property	(iii)	100,000	100,000
Management fee received	(iv)	200,000	30,000
Distribution fee paid	(v)	–	11,672,011

Notes:

- (i) This represents purchases of raw materials from the shareholders/a related company (Zhangjiagang Mudan Bus Body Stamping Co., Ltd, Zhangjiagang Mudan Automobile Accessories Co., Ltd, Zhangjiagang Mudan Bus Parts Co., Ltd and Zhangjiagang Automobile Accessories Factory) during the year.
- (ii) The company has entered into a lease agreement with Jiangsu Mudan whereby the company is granted rights to use two pieces of land in the PRC on which its buildings are erected for a term of 20 years. The annual fixed rental payment is RMB460,000.
- (iii) The company has entered into a lease agreement with Jiangsu Mudan whereby the company is granted rights to use a property in the PRC for a term of 20 years. The annual fixed rental payment is RMB100,000.
- (iv) In October 2001, the company entered into a custodian agreement with Jiangsu Mudan for an indefinite period whereby the management of Factory No. 1 and Factory No. 7 and certain production facilities of Jiangsu Mudan ("the business") are rested with the company. In return, the company receives a management fee of RMB200,000 per annum. Assets and liabilities arising from the business are held for the benefit of Jiangsu Mudan and are not assumed by the company. In addition, the company is not liable, whether severally or jointly and severally, for debts and obligations incurred by the business.
- (v) Distribution fees were payable to Jiangsu Mudan Automobiles Group Sale Company ("JMAGS"), controlled by Jiangsu Mudan, which handled the sales of the company's products in the PRC. The fee was determined by negotiation between both parties and with reference to the estimated costs of JMAGS in providing the agency services in the PRC. Since 8 October 2001, the sales of the company's products have been handled substantially by the company's sales team.
- (vi) During the years ended 31 December 2001 and 2002, Jiangsu Mudan allowed the company to use the trademark of "Mudan", certain of its sales offices, office equipment and public facilities at nil consideration.
- (vii) During the year, the company obtained certain interest-free advances from Jiangsu Mudan. The maximum outstanding balance of the advances from Jiangsu Mudan was RMB77,917,522 (2001: RMBNil) during the year ended 31 December 2002 and the outstanding balance was RMBNil (2001: RMBNil) at 31 December 2002.

Notes on the financial statements

(Expressed in Renminbi Yuan)

29 Material related party transactions (continued)

Notes: (continued)

- (viii) The company made payments for purchases on behalf of Jiangsu Mudan which amounted to RMB29,513,842 during the year ended 31 December 2001. There was no payments for purchases on behalf of Jiangsu Mudan for the year ended 31 December 2002.
- (ix) Jiangsu Mudan made payments for purchases on behalf of the company which amounted to RMB409,907,406 during the year ended 31 December 2001. There was no payments for purchases on behalf of the company for the year ended 31 December 2002.
- (x) Jiangsu Mudan received sales receipts on behalf of the company which amounted to RMB22,509,230 (2001: RMB297,894,690) during the year ended 31 December 2002.
- (xi) The company received sales receipts on behalf of Jiangsu Mudan which amounted to RMB20,138,311 (2001: RMBNil) during the year ended 31 December 2002.
- (xii) During the year ended 31 December 2002, the company acted as the agent of Jiangsu Mudan and purchased certain raw materials, totalling RMB11,490,811 (2001: RMB Nil), on its behalf. On the other hand, Jiangsu Mudan acted as the agent of the company and purchased certain raw materials, totalling RMB28,096,784 (2001: RMBNil), on behalf of the company. No service fee was received/paid by the company in this respect.
- (xiii) During the year, Jiangsu Mudan acted as the agent of the Company in connection with certain export sales, totally RMB5,478,541 (2001: RMB NIL). No service fee was paid by the Company in this respect.

The directors of the company are of the opinion that the above transactions (excluding notes (vi) to (xiii)) with related parties were entered into:

- in the ordinary and usual course of its business;
- either (a) on normal commercial terms; or (b) on terms no less favourable than those available from/to independent third parties; or where there is no available comparison for the purpose of determining whether (a) or (b) is satisfied, on terms that are fair and reasonable so far as the shareholders of the company are concerned; and
- either in accordance with the terms of the agreement governing each such transaction or where there is no such agreement, on terms no less favourable than terms available from/to third parties

and these have been confirmed by the independent non-executive directors.

30 Ultimate holding company

The directors consider the ultimate holding company at 31 December 2002 to be Zhangjiagang Municipal Public Assets Management Co., Ltd, which is a state-owned enterprise established in the PRC.

Reconciliation of net profit and net assets under International Financial Reporting Standards ("IFRS") and PRC accounting rules and regulations

(Expressed in Renminbi Yuan)

	Note	2002		2001	
		Profit attributable to shareholders for the year	Net assets as at 31 December	Profit attributable to shareholders for the year	Net assets as at 31 December
As determined pursuant to PRC accounting rules and regulations		45,179,480	374,123,280	46,309,911	333,215,800
Adjustments:					
Restatement of costs of issuing shares	(i)	4,457,563	(4,457,563)	–	(8,915,126)
Recognition of deferred tax assets	(ii)	140,776	1,611,772	–	5,047,112
Restatement of overprovided income tax expense in respect of prior years	(iii)	(2,105,120)	–	–	–
Restatement of dividends	(iv)	–	4,272,000	–	8,544,000
Restatement of operating lease rentals	(v)	–	–	1,306,668	–
Restatement of waiver of an amount due to a related company (after tax effect)	(vi)	–	–	1,813,242	–
As determined pursuant to IFRS		47,672,699	375,549,489	49,429,821	337,891,786

Notes:

- (i) The amount represents the different treatment on the costs of issuing shares between the IFRS and PRC financial statements. Under the PRC accounting rules and regulations, costs of issuing shares (in excess of the share premium arising from the issue) are recognised as an asset and amortised over 2 years. Pursuant to IFRS, the costs of issuing shares are accounted for as part of the equity transaction to which they relate and are reported as a movement in equity.
- (ii) This represents the recognition of deferred tax assets in respect of the IFRS adjustment as noted in note (i) and certain accounting depreciation in excess of tax depreciation for the year ended 31 December 2002.
- (iii) This amount represents write-back of prior years' income tax expense in the PRC financial statements. Under the IFRS financial statements, the overprovision was adjusted in the period to which it occurred.
- (iv) Under the PRC accounting rules and regulations, dividends are recognised as a liability in the period to which they related. Pursuant to IFRS, dividends are recognised in the period in which they are declared.
- (v) In October 2001, the company entered into lease agreements with Jiangsu Mudan Automobile Group Company Limited which was effective retrospectively since the establishment of the company in September 1998, whereby the company is granted rights to use two pieces of land in the PRC and a property for a term of 20 years. The annual fixed rental payment for the lease of land and property are RMB460,000 and RMB100,000 respectively. This represents a cut-off adjustment for the PRC financial statements.
- (vi) The amount represents the different treatment on a waiver of an amount due to a related company between the IFRS and PRC financial statements for the year ended 31 December 2001. Under the PRC accounting rules and regulations, such waiver is dealt with directly as a movement in the capital reserve. In the IFRS financial statements, the waiver is recognised as other operating income in the period to which it occurred.

Five year summary

(Expressed in Renminbi Yuan)

	Year ended 31 December			Period from 18 September 1998 (date of establishment) to 31 December	
	2002	2001	2000	1999	1998
Results					
Revenue	888,526,140	857,038,069	775,719,118	507,051,801	179,614,759
Profit from operations	70,080,883	77,671,765	48,808,986	46,793,734	27,133,223
Net finance costs	(1,498,461)	(4,539,496)	(7,819,607)	(6,465,142)	(3,326,455)
Profit before tax	68,582,422	73,132,269	40,989,379	40,328,592	23,806,768
Income tax expense	(20,909,723)	(23,702,448)	(13,711,295)	(13,493,235)	(7,856,233)
Profit attributable to shareholders	47,672,699	49,429,821	27,278,084	26,835,357	15,950,535
Assets and liabilities					
Property, plant and equipment	177,332,713	177,719,337	188,288,577	221,701,919	146,022,164
Construction in progress	428,000	–	–	–	–
Deferred tax assets	1,611,772	5,047,112	2,105,120	2,105,120	–
Total current assets	564,739,422	415,351,153	312,360,640	121,170,495	224,998,825
Total current liabilities	(348,562,418)	(240,225,816)	(240,013,956)	(109,515,237)	(155,973,182)
Total assets less current liabilities	395,549,489	357,891,786	262,740,381	235,462,297	215,047,807
Non-current liabilities	(20,000,000)	(20,000,000)	–	–	(4,880,000)
	375,549,489	337,891,786	262,740,381	235,462,297	210,167,807
Share capital	284,800,000	284,800,000	204,300,000	204,300,000	204,300,000
Reserves	90,749,489	53,091,786	58,440,381	31,162,297	5,867,807
	375,549,489	337,891,786	262,740,381	235,462,297	210,167,807