



**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)*



Annual Report 2003

## 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 manufacture 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 202,000 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, Shanghai and etc.

Mudan buses are well received by customers. The Company’s products have received numerous awards in the past years including “The best appearance of the year 2003 (最佳造型設計獎)” awarded by BAAV (世界客車聯盟), “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, extensive distribution network, efficient after-sales services and reputable brandname provide a solid foundation for further business expansion. Mudan Auto’s mission is to become a leading bus manufacturer worldwide with good reputation and advanced technology. To accomplish this mission, the Company will use its successful experience gained in the PRC to capture overseas markets and opportunities for a global expansion.

During the year, the Company new products of model MD6122GDU was awarded “The best appearance of the year 2003 (最佳造型設計獎)” by BAAV (世界客車聯盟) and “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). Furthermore, the Company was granted the “Safety Running Authentication Certificate (安全行駛認證證書)” in the activities of “China Famous Brand Auto Vietnam Show (中國名牌產品(越南)巡展)”. The Company’s products also passed the China Compulsory Certification (“3C”) Test. The Company’s ISO9001 (2000 version) quality system was upgraded successfully.

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This announcement, for which the directors (the “Directors”) of Mudan Automobile Shares Company Limited (the “Company”) or “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 announcement 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 announcement misleading; and (3) all opinions expressed in this announcement 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*)  
YANG De Xiang  
XU Hong Bing  
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  
LI Jing Shan  
TANG Wei Dong  
GU Yu Zhong  
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

XU Hong Bing

### Authorized representatives

SUN Min Biao  
XU Hong Bing

### Authorized persons to accept Service of process and notice

Kwok & Yih

### Auditors

KPMG

### Sponsor

VC CEF Capital Limited

### Legal adviser to the Company

Kwok & Yih

### Principal bankers

Bank of China  
Zhangjiagang Branch

Agricultural Bank of China  
Zhangjiagang Branch

Construction Bank of China  
Zhangjiagang Branch

China Everbright Bank  
Suzhou Branch

### Hong Kong branch share registrar and transfer office

Computershare Hong Kong Investor  
Services 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](http://www.mudanauto.com)

### Principal place of business in Hong Kong

Rooms 3705-06, 37th Floor,  
Gloucester Tower, The Landmark  
Central  
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 2003.

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, over 230 models namely MD6601, MD6701, MD6800, MD6901, MD6100 and MD6121. 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.

### Business review

#### The bus market faced the challenge of the outbreak of SARS

The outbreak of SARS was suddenly happened in the first half year of 2003. It brought a large negative impacts on both the public passenger transportation and traveling transportation business. The sales of buses were dropped sharply in the SARS period. Even the China government has imposed certain policies and the bus industries enterprise also put much effort to change the situation, the whole bus market seems not to be so optimistic. According to bus statistical information website provided by Zhong Tong Group, the profit index of bus industries was lower 64.9% as compared with the year of 2002. Some of the bus companies even recorded a loss results at the end of the third quarter.

During the past year of 2003, Mudan Auto as well as China bus industry experienced two challenges of the outbreak of SARS and the price increase of raw material. Under the competitive bus market condition, all staff members of Mudan Auto devoted effort to develop the business and continued to maintain the enterprise philosophy of “Customers Guidance and Pursue Excellence” for the purpose of satisfy the customers' need. The Company also help customers to keep their competition capabilities by the usage of the reputable brandname of Mudan. We will try our best to establish a strategic partnership especially with tourist company,



## Chairman's Statement

long-distance and public transportation companies for the purpose of development of mutual benefits relationship. In the depression conditions of the bus market, Mudan Auto made good progress in business development and got satisfactory results. The total number of sale and manufacture of all series of buses in the year of 2003 amounted to 9,645 (2002: 10,554 ), among them large and medium-sized buses amounted to 3,260 (2002: 2,424 ) representing an increase 34.5% as compared with the same period of last year. According to the information from China Bus Statistical Information Net, the Company stands in the 3rd position in respect of the number of sales and production of buses in the PRC. In the series of passenger bus and city bus, the Company's sale of these two series of buses ranked the 4th and 3rd position in PRC respectively. Moreover, Mudan Auto keeps the No.1 position in the sale of 5 to 6 meters' long and 8 to 9 meter's long buses. In general, Mudan Auto products lie in the leading position in the bus market.

Turnover for the year ended 31 December 2003 amounted to RMB910,111,382 (2002: RMB888,526,140). Net loss stood at RMB15,415,082 (2002: profit of RMB47,672,699).

In 2003, 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 and development of large and medium-sized buses. 85 new products were approved by the National Development and Reform Commission ("NDRC") of the PRC during the year.

### **A: Alterations of two production lines**

#### **1. Modernization of medium and large-sized bus production lines**

In order to satisfied the customers' needs in the medium and large-sized buses, the Company has completed the alteration of a modernised production facilities line for medium and large-sized buses. This can make full use of the production capability to satisfy the needs of customers better. Turnover of the medium and large-sized buses for the year of 2003 amounted to RMB497,269,000 (2002: RMB396,425,000).

#### **2. Construction of a new inspection and testing line for finished buses.**

In order to comply with the State's new standard and extended the models to medium and large-sized, the Company started to construct an advanced technology testing line in the year of 2003 and the line will be put into use in the first half year of 2004. The new line has an "A" standard, it is qualified and even exceed the latest standard requirements of the State. The technology standard of the new equipments has an advanced position in domestic bus market. Another main characteristic of the new testing line is high automatic level and it realizes the automation of the quality testing.

### **B: Realization on two breakthroughs**

#### **1. Overseas market got a new breakthrough**

Due to our famous reputation brand, intensive cultivation quality, high quality and efficiency service and rapid feedback on enquiry, the Company has signed several overseas sales agencies successfully in the year of 2003.

Turnover of overseas market amounted to RMB47,742,426 (2002: RMB8,878,156). The markets covers Southeast Asia, North Africa, Caribbean, Middle East and Central America etc. in the year of 2003. According to the information from State Administration for Entry-Exit Inspection and Quarantine, Mudan Auto became a largest bus exporter in a single sales order as well as the largest bus exporter in China in March 2003.

## Chairman's Statement

### 2. New products on research and development of medium and large-sized buses.

Mudan Auto always close to the market needs and serve the customers with our service concepts which are human-oriented, comfort, luxury, environmental friendly and high technology. Mudan Auto already built up a scientific system together with strong capability research team for the products development. Mudan Auto continues to strengthen the base of research and development of the new products with emphasis on the new reallocation of human resources, material resources and operation strategy which towards new technology. This is to ensure the new technology which can lead the innovative of the new management concept. In March 2003, the model of MD6122GDU luxury high speed large-sized bus was awarded "The best appearance of the year 2003" from the exhibition of "Busworld Asia". This is the breakthrough of Mudan Auto's technology in the area of the research and development in medium and large-sized buses.

At present, there are more than 50 new products qualify for the Eour II emission standard and 18 products have been appraised as high grade buses by China Ministry of Communications. The revenue of large and medium-sized buses represented approximate 50% of the total revenue of 2003, Mudan Auto has successfully completed the change of its products mix.

## C. Completion of two uplift

### 1. Management capability was enhanced by enterprise resource planning (ERP)

To counteract the SARS impact, the Company plans to set up a contingent measure on the crisis to enhance the capability to meet the emergency in time to serve customers better, Mudan Auto was carrying out ERP project step by step. It covers Office Automation (OA), financial management system, ERP, Customer Relationship Management (CRM) system, Product Data Management (PDM) and Supply Chain Management (SCM) modules. During the special period of SARS, e-business has been promoted and operated fully by the Company. The website of the Company has also been revised. Customers can know more about Mudan Auto, acquaintance with Mudan's products, make order, learn normal maintenance skills of the bus and feedback information timely by accessing the Company's website. This feedback platform was established and the relationship between Mudan Auto and its customers are getting closer and closer. At present, we have realized the result of handling office business through internet. An enterprise communication platform was also established. Hence, the development of information technology in the office has achieved satisfactory results. Accordingly, the management efficiency was then improved. The overseas sales result was also increased markedly.

The Company will keep on setting up of the CRM throughout China so as to capture a higher percentage of the e-business sales. It will also enhance the ability of the Company to have quick respond to the similar crisis in the future.

### 2. ISO9001 enhanced the quality guarantee capability.

The Company's quality certificate has been upgraded to ISO9001 (2000 version). This enhanced the product quality guarantee capability and raised the reputation of products. This laid a firm foundation for Mudan Auto's brand-name.



## Chairman's Statement

### Future prospect

#### A. Establish a fittings center

The Company put emphasis on the fittings sales and delivery services. By setting up fitting center around the major market area to provide after-sale services and sale of spare parts or fittings can help the after-sale service station to control the inventory level to avoid over storage of stock or out of stock.

#### B. Build the base of technology research and development

##### 1. Establish the products development center

The Company will speed up the application of the new automobile technology and materials to the actual production. Also, the Company will carry out the research on the uplift of the overall technology quality and the development of the main products.

##### 2. Uplift the technology on the manufacture of chassis

The research and development of the manufacture of chassis was put on the top of the list for discussion and a medium-term development for the preparation of the manufacture of whole bus was planned.

At the same time, the Company also consider to obtain the right of manufacture of chassis through merger and acquisition or investment in those chassis manufacturers. The Company would also like to enter into partnership with foreign and/or domestic bus manufacturer or spare parts manufacturers for uplift the technology level of Mudan Auto.

##### 3. Adopt advanced technology

The Company will make the full effort in getting the approval of being as the industrialization of high-new technology from the State. After approval, the Company will fully utilize the benefits policy given to the industrialization of high-new technology by state for uplift the products technology and increase the benefits of the enterprise accordingly.

#### C. Carried out IT project

The Company promoted all the staff to fully use all modules in the OA system for the purpose of carry out a scientific management concept. The financial management and stock management modules will be fully operated in the year of 2004. Based on this, the Company will finally decide to choose the ERP suppliers and to carry out the sales modules accordingly.

Mudan Auto brand name has been deeply established in the China market. After experiencing the two challenges of SARS and the price increase of raw materials in 2003, Mudan Auto has rapidly adapted to the change of market environment. The Company can provide the customers with the most suitable and best quality buses timely as well as the efficiency of the after sales services. Mudan Auto will then get a higher return on it.

## Chairman's Statement

Due to the continue economic growth in China and the steady recovery of global economic, the foreign and domestic passenger transportation companies will have more demand on the bus performance. In the future, the Company will put more emphasis on providing the excellent services to customers, advanced technology in production, good quality products and capture more market share through the innovation of the management concept. These are to ensure Mudan Auto maintain its leading position in the China bus market. We will try our best to promote the reputation of Mudan Auto medium and large-sized buses. In order to make customer to have deep impression on Mudan buses, we will do our best to provide the customer with the human-oriented and environmental friendly buses.

**Mudan Automobile Shares Company Limited**

**SUN Min Biao**

*Chairman*

Zhangjiagang City, Jiangsu Province, the PRC

31 May 2004

# Management Discussion and Analysis

## Market overview

### Austere year of 2003

#### Impact of Severe Acute Respiratory Syndrome (“SARS”)

In 2003, SARS outbreak exposing flaws in China regime. A deadly disease that worries the public and threatens the economy. It has also brought negative impact on both people daily life and economy: (i) Many large economic activities had been cancelled or postponed. (ii) Business trip had been stringently controlled. (iii) Drastic decrease of the intention of travel. (iv) No huge seasonal locomotion of labour. (v) Within the city, many people prefer riding bicycle as transportation. During the period from April 2003 to October 2003, there were few economics activities in the country. The decrease of the locomotion of people leads to few people riding on the long distance bus, touring bus as well as public transportation bus. The demand of the city transportation bus decreased sharply in the bus market and operating income of public transportation companies also dropped significantly.

The adverse effect of SARS on Mudan Auto are the following:

#### 1. Products

The most affected Company products were touring bus, long-distance bus, light-sized bus which travel in village and public transportation bus. The impact on public transportation was relatively small, but the operating cost of public transportation rose greatly. (Such as increase of empty buses and other costs like sanitation measures) After the outbreak of SARS, many people had no intention to go outdoor. Some people prefer riding bicycle or walk instead of the usage of public transportation bus. The demand on the public transportation bus was dropped accordingly. As most of the payments terms for the public transportation bus by customers are settled by installments, the amount of account receivable was increased accordingly.

#### 2. Geographical sales

Guangdong province is one of the major and important sales markets of the Company. It was also the main victimized region in the SARS periods and where the first SARS case was found. Beijing and Tianjin are also the major sales regions in the year of 2003. However, the sales amount was dropped in those areas as compared to those of the corresponding period last year. Shanxi is the province where Mudan Auto was emphasis to promote the LPG bus. Unfortunately, the above provinces and cities were the most serious SARS infected areas.

#### 3. Delay the approval of new products

During the SARS periods, the respective government department stop the approval process of the new models of buses. (i) New products testing cannot be completed on time. (ii) Delay of the announcement of the new products in the approved list. (iii) Compulsory certificate test was delay for three months. (iv) Not to carry out approval process of the application of the environmental products. New environmental products of the Company launched at the market could not be sold efficiently.

## Management Discussion and Analysis

### 4. Market Development

The market is now in a difficult situation (i) The reduction of the demand of buses leads the bus industry more and more competitive. The profit margin of the bus industry was sharply slashed. (ii) Many companies refused to have meeting with the people from outsider during the SARS periods. Under this circumstance, the salesperson of the Company could not have the chance to promote the Company's products to the customers. (iii) As to lower the risk of the salesperson, factory worker or management person being infected the SARS epidemics, the Company spent an extra amount on the sanitary and security consumption. The amount paid for the business trip staff was also higher. (iv) Some of the customer cancelled their orders or delay the schedule for delivering the finished products. These caused the increase of the inventory level. As the Company is in the progress of changing the product's mix towards the medium and large-sized buses, both series of buses have higher material cost. Hence, it increased the cost of inventory as well. Furthermore, the sales person has difficulty to approach the customer in SARS period for debt collection. And also, the customers faced the difficulty in their business as well. Therefore, the balance of the account receivable increased accordingly.

### Strategy and Measures

During the prevalence of SARS, we analyzed the market and opted the "start from expanding our market and try to seize every business opportunity" strategy.

#### 1. Take the Initiative in Exploring E-business

Many customers refuse to receive visitors, making it difficult for us to promote the Company's products. Therefore, the Company enforced the use of e-business, publicized Mudan products on our website via Internet, look for new customers and sell our products through e-mails, telephone calls, faxes and business short messages. We will sort out our customers into different categories, such as long-distance passenger transportation, tourism and public traffic, etc. so as to recommend Mudan products via Internet by addressing their needs.

#### 2. Consolidate Overseas Markets to Expand Results

In 2003, because the domestic market was hampered by SARS we tried our best to make up the loss in revenue from overseas markets. We achieved a satisfactory result, the revenue of overseas market amounted to RMB47,742,426, represents an increase of 437% as compared to those of the corresponding period in 2002.

#### 3. Develop new products, seize Business Opportunities through Innovation to Establish Comparative Superiority

Firstly, we will install onboard sterilizers in our buses, such as ultraviolet generators, ozone generators and electronic ventilators, etc.; secondly, we will develop special vehicles for the prevention of SARS and recommend SARS ambulances, medicine carrier vehicles and meal carrier vehicles to the SARS Leading Groups in various places.

#### 4. Revitalize Stock Assets to Ensure the Safety of Funds

The first step is to speed up the collection of payment for goods by teaming up the sales department, Department of Finance and Investment and the law firm to jointly sort out the accounts receivable; the second step is to lose no time in lowering the numbers of cars in the stock and promote the sale of stocks; the third step is to dispose of returned cars quickly by measures of cutting down the prices appropriately; the fourth step is to dispose of chassis by transforming them so as to make full use of existing resources.

## Management Discussion and Analysis

### 5. Dare to confront difficulties and Dare to Win

Firstly, we should fully utilize the personnel who are sent out to work. Under the circumstances such as when they cannot come back and our headquarter staff cannot go to help them, we should give out commands through remote control, in this way, we can take initiation and win over customers. Secondly, we should take advantage of the delivery of buses so that our salespersons and servicemen can go to customers with these buses without the need of taking public vehicles. Thirdly, we should adjust our marketing strategy to focus on institutions of public health and medical service as one of the key customer groups of Mudan buses.

To maintain our market shares, the Company has decided to increase 1.5~2% of the turnover as the income of sales people to whet their enthusiasm and security, the total cost of sales people is expected to increase by RMB15,923,267. To stabilize our product market in this special environment, we would rather cut profits than cut market shares, for the market shares once lost are hard to regain again, even if we are willing to pay a higher cost. The salary increase for sales staff only applied to 2003 and would not affect the gross profit margin of the products in the future.

### 6. Straigten out Internal Affairs to Upgrade Management Ability

Firstly, we should enhance cost management to control prices of raw materials by implementing an entirely procurement through IFB to form an open structure of complete sets of Mudan products. We should control the production cost, make full use of various resources, avoid leaving equipment idle, pursue maximization of profits and control the consumption of energy, such as electricity, gas and water, in the production process. We should also control the production expenses by taping the potential of the enterprise and looking for ways of reducing sales expenses and office expenses. Secondly, we should optimize our product structure. (1) Strengthen the development of environmentally-friendly and high-grade buses; continue to use new technology, new process and new materials to develop new buses, while transforming the existing non-environmentally-friendly products and scaling up the development of gas-driven buses. (2) Integrate existing products by eliminating products which are in low sales volume and zero profitability. We should select several basic models to form series in order to facilitate their recommendation to customers, the batch procurement of fittings, quality control of fittings and manufacturing, the reduction of the cost of fittings and quality control efforts, and the organization of production as well.

#### **Price increase of raw material, products profits decreased in the bus industry enterprises**

According to the statistical figures from State Statistics Bureau on 30 Sept 2003, the price of heavy steel, medium-weight steel, light-weight steel, thick steel and thin steel were raised 15.7%, 20.8%, 12.2%, 21.5%, 11.5% respectively. In general, the price of steel was raised around RMB1,500 per ton.

## Management Discussion and Analysis

### 2004, a year with opportunities and challenges

“Village to Village” project has started country-wide. The demand of light-sized bus may increase.

In 2003, the Government has carried out a strategic investment planning on the infrastructure on the village road. The Government has started to inject more amount and promote the urban area government to renovate the village road. During the year of 2003, 5,300 new cases about the renovation of village road which amounted to 39.6 billion has been started. The other RMB3 billion will continue to invest for the “Linkage Project”. The aim is to solve the problem of the non-linkage between the highway with the urban area and administrative village. This is another measure after the road construction in western China which will promote the bus market in 2004. By the end of the year of 2005, the percentage of the highway linkage to urban area and administrative village will reach 99.8% and 96% respectively. In the coming three years, the government plans to complete the construction of village road of 176,000 km. The China government intends to implement three projects: i) village linkage to village in the Eastern region. ii) town linkage to town in Central region and iii) city linkage to city in the Western region. The Government has planned to inject RMB50 billion for those projects. The fast development of the construction of village road leads to the increase in the demand on the light and medium-sized passenger transportation buses. The Company can also get benefits from the potential sales of light-sized buses as well.

Fast development of the construction on grading highways may be lead to the increase of the demand of medium and large-sized buses.

In 2003, the length of highway completed in China has continued to growth. More than 800 km highway in the project of “5 vertical and 7 horizontal national highways” are newly completed. According to the China Ministry of Communications planning, the length of highway and expressway will reach 2.1 to 2.3 millions km over the country by the end of year 2010. At that time, the whole project of “5 vertical and 7 horizontal national highways” will be completed. Moreover, 8 national trunk highways linkage with provinces and 90% of the highways linkage to the cities over 200,000 population will also be completed. A highway network will be formed in the Eastern regions. The total length of expressway will reach 50,000 km. The length of second grade or above highway will reach 400,000 to 450,000km. The national highway will be ranked as second grade or above. All the second grade highway will be linkage to all cities in Eastern and Central regions. The construction of the highway and expressway leads to the further on the increase in the demand on the buses. This tendency matches with the strategy of the Company in development of the medium and large-sized buses.

Bus markets became more and more competitive.

At present, there are more than 100 bus manufactures ranged from large to little manufacture capabilities in China. With the entrance steps of State owned capital, the large automobile groups products scope was enlarged, together with the extending products scope of the bus chassis manufactures, the competitive conditions among the bus market become more and more drastical.

### 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 2003, new models were developed included: 28 models of the MD6601 series of light-sized buses, 5 models of the MD6701 series of light-sized buses and 11 models of the MD6701 series of medium-sized buses, 22 models of the MD6800 series of medium-sized buses and 3 models of the MD6901 series of medium-sized buses, 7 models of the MD6101 series of large-sized buses, 5 models of the MD6111 series of large-sized buses, 4 model of the MD6121 series of large-sized bus, totally 85 products. All these products were approved by the respective governmental departments.



## Management Discussion and Analysis

### Revenue

Total revenue for the fiscal year of 2003 amounted to RMB910,111,382, representing approximately 2.4% increase compared to that of RMB888,526,140 generated in 2002 in which for light, medium and large-sized series of buses amounted to RMB412,842,000, RMB317,311,000 and RMB179,958,000 (2002: RMB492,100,699, RMB287,427,044 and RMB108,998,396 respectively). Compared to 2002, revenue for light-sized buses decreased by 16.1%, medium and large-sized series of buses increased by 10.4%, 65.1% respectively.

### Cost of sales and gross profit

Due to the increase in total revenue, cost of sales increased proportionately to RMB830,658,384 in 2003 from RMB780,226,789 in 2002. Gross margin of the Company's products decreased to 8.7% in 2003 from 12.2% in 2002. 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 large order to expand the market there during the SARS period and price increase of raw materials.

### Other operating income

Other operating income for the fiscal year 2003 amounted to RMB2,438,717 (2002: RMB1,486,317), which included the sale of scrap materials RMB1,231,969 (2002: RMB444,893).

### Distribution expenses and general and administrative expenses

During the SARS period, the China government has stringent control on the locomotion of people to avoid the fast spread of the epidemic. The staff was forbidden to come back to the Company. This made the amount of the staff cost, which including the business trip was increased to RMB31,624,201 (2002: RMB12,703,118). In order to compensate for the loss of sales of buses of the Company in the SARS period and to maintain the original market shares in the bus field, the Company adopted aggressive strategy and lots of sales promotion projects were carried out in the second half year. The Company motivated the business development staff to carry out sales promotion work in different cities and provinces all over the country. As a result, the business development cost was increased. Based on the above reasons, the distribution expenses for 2003 was increased to a total of RMB46,975,611 (2002 : RMB25,096,843), representing an increase of 87.2% from that of 2002.

The total general and administrative expenses for the fiscal year 2003 was RMB28,079,116, represents an increase of approximately of 103.4% as compared to the amount of RMB13,805,192 in 2002. The main reasons are the increase of the 3C authentication fee and the automobile testing fee for the approval from NDRC and the payment of the professional charges.

The Company's expenses on salaries, wages and bonus for the fiscal year 2003 amounted to RMB70,468,817 as compared to RMB46,394,011 in 2002, representing an increase of RMB24,074,806. The reasons were (i) the salaries of the labour was linked with the increase of production of the medium and large-sized buses; (ii) the Company paid additional salary of approximately RMB15,923,267 to its sales staff in SARS period as an added incentive for sales staff to maintain its market share under the special circumstances. Such measure was only taken for 2003 and subsequently will not affect the gross profit margin.

Other operating expenses for the fiscal year 2003 totalled to RMB27,545,960, as compared to RMB802,750 in 2002, representing an increase of RMB26,743,210, which mainly represents provisions provided for bad debts in relation to certain account receivables and the provision for the diminishing in the value of certain inventories.

## Management Discussion and Analysis

In the financial year of 2003, the net finance costs of approximately RMB2,200,106 comprised interest on bank advances and other borrowings, bank charges and interest income, representing approximately 0.24% of turnover for the year 2003, as compared to approximately RMB1,498,461 in year of 2002, an increase of RMB701,645 which is due to increase the amount of the interest of bank borrowings.

### 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 of the Company dated 9 May 2003, the Company did not have any plan for material investments and acquisition of material capital assets for the year of 2003 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 the PRC. In such circumstances, the Directors considered that the exchange rate fluctuation is limited for the year of 2003.

### Significant investments held

The Company has no significant investments held during the year of 2003.

### Financial resources and liquidity

The financial position of the Company comprised shareholders equity which amounted to RMB355,862,407 as at 31 December 2003 (2002: RMB375,549,489), current assets which amounted to RMB859,441,244 as at 31 December 2003 (2002: RMB564,739,422), of which RMB142,932,375 (2002: RMB92,594,293) were cash and bank balances. RMB292,994,100 (2002: RMB59,431,080) was placed as pledged deposits to secure certain banks in issuing bill payable of RMB508,364,000 as at 31 December 2003 (2002: RMB191,630,000). As at 31 December 2003, the Company had a short-term bank loans and long-term bank loans of about RMB75,000,000 (2002: RMB20,000,000) and RMB NIL (2002: RMB20,000,000) respectively, the short-term bank loans are repayable within one year.

### Contingent liabilities

As at 31 December 2003, the Directors were not aware of any material contingent liabilities.

### Charges on assets

As at 31 December 2003, the short-term bank loans of RMB65,000,000 was unsecured (2002: unsecured) and short-term bank loan of RMB10,000,000 was pledged over factory building with a net book values of RMB35,612,824 (2002: RMB37,027,056).

### Gearing ratio

The Company's gearing ratio, based on total liabilities to shareholders' equity, was 2.1 (2002: 0.98) as at 31 December 2003.

## Management Discussion and Analysis

### Capital structure

During the year, there has been no change in the Company's share capital. As at 31 December 2003, 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 2,122 employees (2002: 2,179). 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.

### Disclosure of trade receivable pursuant to rules 17.15 and 17.17 of the GEM Listing Rules

As at 31 March 2004, there were 284,800,000 shares of the Company in issue. Based on the average closing price of the Company's shares of HK\$0.986 per share as stated in the Stock Exchange's daily quotation sheets for the trading days from 24 March 2004 to 30 March 2004 (both days inclusive), being the five business days immediately preceding 31 March, 2004, the total market capitalization for the Company was approximately HK\$281 million as at 31 March 2004.

As at 31 March 2004, trade receivable from a customer of the Company (the "Trade Receivable"), 廣州白雲華港汽貿中心 (Guangzhou Baiyun Huagang Automobile Trade Center, the "Customer"), a company which is independent of, and not connected with, the Company, the Directors, chief executive or substantial shareholders of the Company or their respective associates (as defined in the GEM Listing Rules), amounted to approximately HK\$70 million (RMB74,322,222), representing approximately 24.9% of the Company's total market capitalization as at 31 March 2004. The Customer was previously allowed to settle the Trade Receivables by instalments over a period of not more than 18 months. Some of these Trade Receivables due from the Customers were overdue. The Company has been negotiating with the Customer with respect to new arrangements for the repayment of the outstanding Trade Receivables. The repayment terms and schedule have not been determined yet.

The Trade Receivable was resulted from sales to the Customer by the Company in its ordinary course of business and on normal commercial terms. It is unsecured and interest free, and has normal terms of settlement. Due to the nature of the transactions and business practice, trade receivables can only be finalized after month end, which also need to be verified and confirmed by customers pursuant to the normal trading practices in respect of such receivables and the relevant trade terms. As the balance of the Trade Receivable as at 31 March 2004 is verified and confirmed by the Customer on 16 April 2004, this immediately gave rise to a disclosure obligation under rule 17.15 of the GEM Listing Rules, the Company therefore issues this announcement as it receives such verification so as to comply with the GEM Listing Rules.

## Management Discussion and Analysis

### **Qualified opinion arising from limitation of audit scope**

Please refer to the auditors's report on page 32.

## Business Objective Review

### Comparison of business plans and actual progress

From 1 January 2003 to 30 June 2003

#### Expected project progress

#### Actual project progress

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

- |  |   |
|--|---|
| <p>1. Continue to launch two to five new bus models.</p>   | <p>During the period, the new models were developed including: 16 models of the MD6601 series of light-sized buses, 2 models of the MD6701 series of light-sized buses and 3 models of the MD6701 series of medium-sized buses, 9 models of the MD6800 series of medium-sized buses and 2 models of the MD6901 series of medium-sized buses, 2 models of the MD6101 series of large-sized buses, 1 models of the MD6111 series of large-sized buses, 3 model of the MD6122 series of large-sized bus, totally 38 products. All these products were approved by NDRC.</p>  |
| <p>2. Continue to strengthen the distribution network and the sales of the Company's buses in South Africa, Asia and South America by appointing distribution agents and establishing sales offices if the business opportunities arise.</p> | <p>5 non-exclusive distribution agents were appointed in overseas market.</p>   |
| <p>3. Set up sales office in Inner Mongolia, the PRC.</p>  | <p>Branch office of Beijing was also used as Inner Mongolia sales office for the provision of services.</p>   |
| <p>4. Place advertisement in the media to promote the Company's overall image.</p>   | <p>In June 2003, the Company placed advertisements on sina website to propagandize environmental friendly buses. During the period, the Company placed advertisements on Sina website, China automobile website, China Central TV, Shanghai TV, Zhangjiagang TV, China Automotive Market Yearly, China's Foreign Trade Magazine, Business Car Magazine, China Automotive News, Economy Daily, China Customer Daily, Shanghai Economy Daily, Shanghai Automotive News, Business Car News, Contemporary Automotives News, Liaoning Daily, Urumchi Evening News, Suzhou Daily, Zhangjiagang Daily, etc. to promote the Company's overall image. Also, the Company took part in the exhibition of "Busworld Asia" and the activities of "China Famous Brand Auto Vietnam Show".</p> |

## Business Objective Review

### (2) Modernization of production facilities

1. Complete the installation of the modernized production facilities for the production of medium-sized buses. On 7 May 2003, the Company has entered into an agreement with Jiangsu Mudan in relation to the acquisition of the factory erected on a piece of land together with the existing production facilities installed therein (together the "Assets") at a consideration of RMB68,080,000. The acquisition of the Assets is to modernize the production of the abovementioned modernized production facilities for the production of medium-sized buses.
2. Provide training for staff to use the modernized production facilities. The Company has streamlined the production process, rearranged the working hours, the work efficiency was enhanced accordingly.
3. Carry out trial production to ensure the products produced are able to meet the Company's quality standard of the medium-sized bus with the modernized production facilities. In progress.

### (3) Introduction of advanced technologies

1. Implement new technology adopted from transfer arrangements in relation to the production of medium-sized bus body. Designated team was appointed to conduct the research work.

### (4) Enhancement of research and development capabilities.

1. Develop its own new design on the bus body by the research and development staff. Model of MD6122GDU was awarded "The best appearance of the year 2003" by BAAV.
2. Continue to provide training to the existing research and development staff. The Company had organized the training program on ISO9001 (2000) quality system, 5S management and 3 Dimensions Computer-Aid Design.



## Business Objective Review

From 1 July 2003 to 31 December 2003

### Expected project progress

### Actual project progress

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

- |   |   |
|---|---|
| <p>1. Continue to launch three to six new bus models.</p>   | <p>During the period, the new models were developed including: 12 models of the MD6601 series of light-sized buses, 3 models of the MD6701 series of light-sized buses and 8 models of the MD6701 series of medium-sized buses, 13 models of the MD6800 series of medium-sized buses and 1 models of the MD6901 series of medium-sized buses, 5 models of the MD6101 series of large-sized buses, 4 models of the MD6111 series of large-sized buses, 1 model of the MD6121 series of large-sized bus, totally 47 products. All these products were approved by NDRC.</p> |
| <p>2. Continue to strengthen the distribution network and the sales of the Company's buses in South Africa, Asia and South America.</p> | <p>5 non-exclusive distribution agents were appointed in oversea market. The sales revenue of the Company amounted to RMB47,742,426 representing a new milestone of Mudan Auto.</p>   |
| <p>3. Set up sales office in Anhui province, the PRC.</p>   | <p>The Company has set up sales and after-sales station in Hefei, Anhui province.</p>   |
| <p>4. Place advertisements in the media to promote the Company's overall image.</p>   | <p>The Company placed advertisements on sina website, China automobile website, Shanghai TV, Zhangjiagang TV, China Automotive Market Yearly, China's Foreign Trade Magazine, Business Car Magazine, China Automotive News, Economy Daily, China Customer Daily, China Securities, Shanghai Economy Daily, Shanghai Automotive News, Business Car News, Contemporary Automotives News, Liaoning Daily, Urumchi Evening News, Suzhou Daily, Zhangjiagang Daily etc to promote the Company's overall image.</p>   |
| <p>5. Participate in the major sales exhibitions and trade shows.</p>   | <p>The Company had held a "New products promotion conference and corporation meeting of Mudan Auto 2004" in Harbin city successfully.</p>   |

#### (2) Modernisation of production facilities

- |   |   |
|---|---|
| <p>1. Commence commercial production of the medium-sized bus at the modernized production facilities.</p> | <p>The Company has begun to commence the commercial production of the medium-sized bus at the modernized production facilities.</p> |
|---|---|

## Business Objective Review

### (3) Introduction of advanced technologies.

1. Continue to implement technology transfer arrangements in relation to the production of medium-sized bus body. Designated team was appointed to conduct the research work.

### (4) Enhancement of research and development capabilities.

1. Continue to develop its own design on some of the automobile parts by the research and development staff. The Company has put out 22 new automobile parts.
2. Continue to provide training to the existing research and development staff. The Company had organized the training program on ISO9001 (2000) quality system, 5S management and 3 Dimensions Computer-Aid Design to its research and development staff.

## 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.


From 18 December 2001 to 31 December 2003, the net proceeds used in enhancement of the sales and marketing activities approximately HK\$3,000,000; approximately HK\$1,000,000 was used for research and development capabilities; approximately HK\$42,000,000 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 requirement.

The application of the proceeds from listing has been used up according to the business plan as stated in the Prospectus dated 4 December 2001.

## Report of the Board of Directors

The board of Directors (“the Board”) submit herewith the report of the Board together with the audited financial statements of the Company for the year ended 31 December 2003.

### 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 (2002: 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	
	2003	2002
The largest supplier	27%	29%
Five largest suppliers in aggregate	52%	51%

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 loss and cash flows of the Company for the year ended 31 December 2003 and the state of the Company’s affairs as at the date are set out in the financial statements on pages 34 to 60.

### Final dividend

The Directors does not recommend the payment of a final dividend in respect of the year ended 31 December 2003 (2002: RMB0.015).

### Charitable donations

There was no charitable donations made by the Company during the year (2002: none).

### Property, plant and equipment

Details of the movements in property, plant and equipment of the Company during the year are set out in note 15 on the financial statements.

## Report of the Board of Directors

### Share capital

Details of the share capital during the year are set out in note 27(a) on the financial statement.

### Reserves

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

### Interests discloseable under the securities and futures ordinance (chapter 571 of the laws of hong kong) (the “SFO”)

#### 1. Directors, supervisors and chief executive of the Company

As at 31 December 2003, none of the Directors, supervisors and chief executive of the Company had any interest and short position in shares, debentures or underlying shares of the Company and its associated corporation (within the meaning of Part XV of the SFO), which will have to be notified to the Company and the Stock Exchange pursuant to Part XV of the SFO, or which will be required, pursuant to section 352 of the SFO, to be entered in the register referred to therein or which will be required to be notified to the Company and the Stock Exchange pursuant to the Rules 5.46 to 5.67 of the GEM Listing Rules.

#### 2. Substantial shareholders of the Company and other persons

Save as disclosed below, as at 31 December 2003, the Directors are not aware of any other interests and short positions in shares and underlying shares of substantial shareholders of the Company and other persons, which will have to be required, pursuant to section 336 of the SFO, to be entered in the register referred to therein.

#### Long positions in the shares

Name of shareholder	Number of shares (domestic shares)	Capacity	Approximate percentage of the issued shares capital under the relevant classes of shares
Zhangjiagang Municipal Public Assets Management Co., Ltd. (“ZMPAM”)	94,310,000	Beneficial Owner	48.06%
	100,340,000	Interest of a controlled corporation ( <i>Notes 1</i> )	51.13%
Jiangsu Mudan	100,340,000	Beneficial owner	51.13%
Zhangjiagang Municipal Leyu Town Assets Management Co., Ltd (“Leyu Town Assets Management”)	100,340,000	Interest of a controlled corporation ( <i>Note 2</i> )	51.13%

## Report of the Board of Directors

Notes:

- 1 ZMPAM has 33.4% interests in Jiangsu Mudan which beneficially owns 100,340,000 domestic shares in the Company. Therefore, ZMPAM is deemed to be interested in 100,340,000 domestic shares, representing 51.13% of the issued domestic share of the Company under the SFO.
- 2 Leyu Town Assets Management has 37.2% interests in Jiangsu Mudan, which beneficially owns 100,340,000 domestic shares in the Company. Therefore, Leyu Town Assets Management is deemed to be interested in 100,340,000 domestic shares, representing 51.13% of the issued domestic share of the company under the SFO.

### Directors and supervisors

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

#### Executive Directors

SUN Min Biao (*Chairman*)

SHI Jin Cheng (*Vice-Chairman*)

SHAO Zhi Nan

(resigned on 20 June 2003)

YANG De Xiang

(appointed on 20 June 2003)

XU Hong Bing

(appointed on 20 June 2003)

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

### Directors' and supervisors' emoluments

Details of the Directors and supervisors' emoluments for the year are set out in note 13 on the financial statements.

### Connected transactions

Details of the connected transactions of the Company carried out in the year are disclosed in note 30 on the financial statements.

## Report of the Board of Directors

### 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 2003.

### 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 5.28 to 5.33 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 2003 have been reviewed by the Committee, who were 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 2003.

### Closure of H share register

The H Share register of the Company is closed from Sunday 30 May 2004 to Tuesday 29 June 2004, (both days inclusive), during which no transfers of H Shares are to be effected.



## Report of the Board of Directors

### Bank loans

Particulars of bank loans as at 31 December 2003 are set out in notes 24 and 26 on the financial statements.

### Retirement scheme

Particulars of the retirement scheme of the Company are set out in note 8 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 page 62.

### 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 2003.

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 2003.

### Practices and procedures of the board

The Directors considered that the Company has complied with the requirement of Board practices and procedures of Rules 5.34 to 5.45 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

31 May 2004

## 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 2003, 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

31 May 2004

## Profiles of Directors, Supervisors and Senior Management

### Executive Directors

**Mr. SUN Min Biao (孫敏彪)**, aged 41, 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 12 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 postgraduate courses 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 53, 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 12 years of experience in management and product development. He joined the Company in September 1998.

**Mr. YANG De Xiang (楊德祥)**, aged 50, is an executive Director, deputy general manager of the Company and general manager of sales company. Mr. YANG hold the title of engineer. He is responsible for the sales and marketing business of the Company. He was formerly the deputy general manager of Jiangsu Mudan. He finished the senior courses of automobile engineering in Jiangsu Technical University in 1997. Mr. YANG was awarded the title of Labor model of Zhangjiagang city (張家港市勞動模範). He has over 27 years of experience in the automobile production management. He joined the Company in 1998.

**Mr. XU Hong Bing (徐宏兵)**, aged 33, is an executive Director, head of the general manager's office and head of human resources department of the Company. He holds the title of economist. He is now responsible for the administration management and corporation relations to foreign countries. 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 is now studying for the EMBA degree in Hong Kong University and Fudan 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. HOU Cheng Bao (侯成保)**, aged 52, 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. He joined the Company in September 1998.

**Mr. JIANG Wei Sheng (姜渭生)**, aged 48, is an executive Director 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 has been 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 23 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 41, is a non-executive Director. She is the chairman and legal representative of Zhangjiagang Automobile Accessories Factory ("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 59, is an independent non-executive Director who joined the Company in July 2001. Mr. Zhang holds the title of senior engineer. He is the vice-chairman of the China Machinery Industrial Association since April 2001. Prior to April 2001, 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 64, is an independent non-executive Director who joined the Company in July 2001. 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 52, is the chairman of supervision Committee 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 45, 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 43, 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 36, 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 manufacture department III. He has been awarded "Labor model of Zhangjiagang

## Profiles of Directors, Supervisors and Senior Management

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 46, is general manager assistant of the Company. He now is in charge of the 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. LI Jing Shan (李京山)**, aged 32, 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 10 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. GU Yu Zhong (顧裕忠)**, aged 46, is the head assistant of production and provider department of the Company. He holds the title of engineer assistant. He graduated from Nanfeng middle school. He has majored in the machinery manufacturing in Jiangsu Technical University. Prior to joining the Company in September 1998, He was the director of production department of factory No.1 of Jiangsu Mudan.

**Mr. TANG Wei Dong (唐衛東)**, aged 35, 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 38, is the head of R&D department. He hold the title of Senior engineer. He majored in Automobile Engineering and 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 40, is the head of manufacture department I. He hold the title of engineer. 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.

**Mr. CAO Quan (曹泉)**, aged 48, 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 Leyu Dongjiegang Middle School in Zhangjiagang City in 1972.

**Mr. CHEN Yong Xiang (陳永祥)**, aged 42, 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.

## Profiles of Directors, Supervisors and Senior Management

### Qualified accountant and company secretary

**Mr. LUI Wing Hong (呂榮匡)**, Edward, aged 41, 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 12 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. XU Hong Bing (徐宏兵)**. For details, please refer to the paragraph headed “Executive Directors” above. Mr. XU 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.



## 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 34 to 60 which have been prepared in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board.

### 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, as a body, and for no other purpose. We do not assume responsibility toward or accept liability to any other person for the contents of this report.

### Basis of opinion

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants except that the scope of our work was limited as explained below.

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. However the evidence available to us was limited by the matters referred to (1) to (3) below:

- (1) Included in the company's balance sheet as at 31 December 2003 are amounts due from certain trade debtors of RMB62,890,572, net of provisions of RMB21,689,650, and a deferred tax asset of RMB5,157,008 arising thereon. Due to the lack of adequate financial information in respect of these trade debtors, we were unable to carry out auditing procedures necessary to satisfy ourselves as to whether this provision was appropriate. Any adjustment to the figure may have a consequential effect on the loss for the year and the net assets at 31 December 2003.
- (2) As shown in note 18 to the financial statements, the company has made a provision of RMB11,025,464 to write down certain of its inventories of RMB34,264,783 to their net realisable value, and has recognised a deferred tax asset of RMB3,638,403 arising thereon. Due to the lack of detailed analysis of the condition of these inventories and adequate financial information in respect of estimated net realisable value, we were unable to carry out auditing procedures necessary to satisfy ourselves as to whether this provision was appropriate. Any adjustment to the figure may have a consequential effect on the loss for the year and the net assets at 31 December 2003. In addition, there were no satisfactory audit procedures that we could adopt to obtain sufficient evidence regarding the ownership and physical existence of certain other inventories amounting to RMB5,337,708 as at 31 December 2003 as the company did not carry out a physical count of these inventories on that date.

## Auditors' Report

- (3) Note 30 to the financial statements discloses certain related party transactions of the Company. Due to the lack of adequate documentary evidence, we were unable to carry out auditing procedures necessary to satisfy ourselves as to the accuracy of the disclosure in respect of items (i), (vi) to (viii) and (x) to (xiv) in that note. In addition, we were unable to carry out auditing procedures necessary to satisfy ourselves that the disclosure in note 30 is complete. We were also unable to carry out auditing procedures necessary to satisfy ourselves as to whether the cash flows in connection with related party transactions as presented in the company's cash flow statement were fairly stated.

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.

### ***Fundamental uncertainty***

In forming our opinion, we have considered the adequacy of the disclosures made in note 2(b) on the financial statements which explains that the company relies on bills financing arrangements at the backing of Jiangsu Mudan Automobile Group Company Limited ("Jiangsu Mudan") to finance its working capital requirement. The financial statements have been prepared on a going concern basis, the validity of which depends on the continuing availability of the financing arrangements; guarantee from Jiangsu Mudan; and on the company's ability to repay its financial obligations when they fall due. The financial statements do not include any adjustments that would be necessary if this basis was no longer to be appropriate. Details of the circumstances relating to this fundamental uncertainty are described in note 2(b). We consider that the fundamental uncertainty has been adequately accounted for and disclosed in the financial statements and our opinion is not qualified in this respect.

### **Qualified opinion arising from limitation of audit scope**

Except for any adjustments that might have been found to be necessary had we been able to obtain sufficient evidence concerning (1) to (3) above, in our opinion, the financial statements give a true and fair view of the state of the company's affairs as at 31 December 2003 and of its loss 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, 31 May 2004

## Income Statement

for the year ended 31 December 2003

(Expressed in Renminbi Yuan)

	Note	2003	2002
Revenue	3	<b>910,111,382</b>	888,526,140
Cost of sales	4	<b>(830,658,384)</b>	(780,226,789)
<b>Gross profit</b>		<b>79,452,998</b>	108,299,351
Other operating income	5	<b>2,438,717</b>	1,486,317
Distribution expenses	6	<b>(46,975,611)</b>	(25,096,843)
General and administrative expenses		<b>(28,079,116)</b>	(13,805,192)
Other operating expenses	7	<b>(27,545,960)</b>	(802,750)
<b>(Loss)/profit from operations</b>		<b>(20,708,972)</b>	70,080,883
Net finance costs	9(a)	<b>(2,200,106)</b>	(1,498,461)
<b>(Loss)/profit before tax</b>	9	<b>(22,909,078)</b>	68,582,422
Income tax benefit/(expense)	10(a)	<b>7,493,996</b>	(20,909,723)
<b>(Loss)/profit attributable to shareholders</b>		<b>(15,415,082)</b>	47,672,699
<b>Dividends attributable to the year:</b>	11		
Final dividend proposed after the balance sheet date		–	4,272,000
(Loss)/earnings per share			
– basic	12	<b>(0.05)</b>	0.17

The notes on pages 39 to 60 form part of these financial statements.

## Statement of Changes in Equity

for the year ended 31 December 2003

(Expressed in Renminbi Yuan)

	Note	Share capital (Note 27(a))	Statutory surplus reserve (Note 27(b))	Statutory public welfare fund (Note 27(c))	Retained earnings	Total capital and reserves
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	11	–	–	–	(8,544,000)	(8,544,000)
Deferred tax assets in respect of the costs of issuing shares realised during the year	17	–	–	–	(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
Balance at 1 January 2003		284,800,000	15,165,846	15,165,846	60,417,797	375,549,489
Dividends approved in respect of previous year	11	–	–	–	(4,272,000)	(4,272,000)
Net loss for the year		–	–	–	(15,415,082)	(15,415,082)
Balance at 31 December 2003		284,800,000	15,165,846	15,165,846	40,730,715	355,862,407

The notes on pages 39 to 60 form part of these financial statements.

## Balance Sheet

at 31 December 2003

(Expressed in Renminbi Yuan)

	Note	2003	2002
<b>Non-current assets</b>			
Property, plant and equipment	15	230,311,093	177,332,713
Construction in progress	16	3,930,699	428,000
Net deferred tax assets	17	10,190,527	1,611,772
<b>Total non-current assets</b>		<b>244,432,319</b>	179,372,485
<b>Current assets</b>			
Inventories	18	120,220,687	165,337,068
Trade and other receivables	19	297,410,958	236,705,417
Amounts due from a shareholder	20	162,557	10,180,064
Amount due from a related company	20	5,123,067	–
Pledged deposits	21	292,994,100	59,431,080
Investments in unit trusts	22	597,500	491,500
Cash and cash equivalents	23(a)	142,932,375	92,594,293
<b>Total current assets</b>		<b>859,441,244</b>	564,739,422
<b>Current liabilities</b>			
Short-term bank loans	24	75,000,000	20,000,000
Trade and other payables	25	664,975,674	317,732,756
Amounts due to shareholders	20	5,718,170	2,651,730
Income tax payable		2,317,312	8,177,932
<b>Total current liabilities</b>		<b>748,011,156</b>	348,562,418
<b>Net current assets</b>		<b>111,430,088</b>	216,177,004
<b>Total assets less current liabilities</b>		<b>355,862,407</b>	395,549,489
<b>Non-current liabilities</b>			
Long-term bank loan (secured)	26	–	20,000,000
<b>Total non-current liabilities</b>		<b>–</b>	20,000,000
<b>Net assets</b>		<b>355,862,407</b>	375,549,489

## Balance Sheet

at 31 December 2003

(Expressed in Renminbi Yuan)

	Note	2003	2002
<b>Shareholders' funds</b>			
Share capital	27(a)	<b>284,800,000</b>	284,800,000
Statutory surplus reserve	27(b)	<b>15,165,846</b>	15,165,846
Statutory public welfare fund	27(c)	<b>15,165,846</b>	15,165,846
Retained earnings	27(d)	<b>40,730,715</b>	60,417,797
		<b>355,862,407</b>	375,549,489

Approved and authorised for issue by the board of directors on 31 May 2004

SUN Min Biao	)	Directors
	)	
YANG De Xiang	)	
	)	

The notes on pages 39 to 60 form part of these financial statements.

## Cash Flow Statement

for the year ended 31 December 2003

(Expressed in Renminbi Yuan)

	Note	2003	2002
<b>Operating activities</b>			
(Loss)/profit before tax		<b>(22,909,078)</b>	68,582,422
Provision for bad and doubtful debts		<b>15,627,297</b>	–
Provision for diminution in value of inventories		<b>11,025,464</b>	–
Depreciation		<b>17,094,102</b>	14,622,910
Unrealised (gain)/loss on investments in unit trusts		<b>(106,000)</b>	13,500
Interest expense (net)		<b>1,853,166</b>	1,285,254
Decrease/(increase) in inventories		<b>34,090,917</b>	(100,506,677)
Increase in trade and other receivables		<b>(76,132,119)</b>	(65,976,768)
Decrease/(increase) in amounts due from/(to) shareholders		<b>11,344,396</b>	27,373,585
(Increase)/decrease in amount due from/(to) a related company		<b>(5,123,067)</b>	501,841
Increase in trade and other payables		<b>68,096,619</b>	135,493,222
Interest paid		<b>(6,835,944)</b>	(2,523,277)
Income tax paid		<b>(6,945,379)</b>	(35,001,257)
<b>Cash flows from operating activities</b>		<b>41,080,374</b>	43,864,755
<b>Investing activities</b>			
Acquisition of property, plant and equipment		<b>(70,072,482)</b>	(12,988,063)
Acquisition of construction in progress		<b>(3,502,699)</b>	(1,120,300)
Acquisition of investments in unit trusts		–	(505,000)
Interest received		<b>6,225,618</b>	1,238,023
Increase in pledged deposits		<b>(233,563,020)</b>	(27,511,062)
<b>Cash flows used in investing activities</b>		<b>(300,912,583)</b>	(40,886,402)
<b>Financing activities</b>			
Advances from Jiangsu Mudan		<b>756,252,625</b>	–
Repayment of advances from Jiangsu Mudan		<b>(555,192,000)</b>	–
Proceeds from discounting of bills received from Jiangsu Mudan		<b>417,114,923</b>	–
Repayment to banks in respect of bills issued to Jiangsu Mudan		<b>(338,733,257)</b>	–
Proceeds from bank loans		<b>75,000,000</b>	20,000,000
Repayment of bank loans		<b>(40,000,000)</b>	(13,000,000)
Dividends paid		<b>(4,272,000)</b>	(8,544,000)
<b>Cash flows from/(used in) financing activities</b>		<b>310,170,291</b>	(1,544,000)
<b>Net increase in cash and cash equivalents</b>		<b>50,338,082</b>	1,434,353
<b>Cash and cash equivalents at beginning of year</b>		<b>92,594,293</b>	91,159,940
<b>Cash and cash equivalents at end of year</b>	23(a)	<b>142,932,375</b>	92,594,293

The notes on pages 39 to 60 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 ("IFRSs") issued by the International Accounting Standards Board. IFRSs includes International Accounting Standards and interpretations.

These financial statements also comply with the disclosure requirements of the Hong Kong Companies Ordinance and 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) Going concern**

During the year ended 31 December 2003, the company and one of its shareholders, Jiangsu Mudan Automobile Group Company Limited ("Jiangsu Mudan") entered into certain bills financing arrangements whereby certain bank acceptance drafts were issued by the company and discounted with banks at the backing of guarantees issued by Jiangsu Mudan as disclosed in note 25 on the financial statements. The company has relied on these financing arrangements for its working capital requirement.

The directors consider that in preparing the financial statements of the company they have given careful consideration to the impact of the above bills financing arrangements on the future liquidity of the company and have taken into consideration all information that could reasonably be expected to be available. On this basis, the directors consider that it is appropriate to prepare the financial statements of the company on a going concern basis. This assumes inter alia that the banks will continue to provide the financing arrangements; Jiangsu Mudan will continue to guarantee the bills payables of the company; and the company will be able to meet in full its financial obligations as the bills fall due. The financial statements do not include any adjustments that would be necessary if the assumptions are no longer appropriate.

#### **(c) 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.



## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 2 Significant accounting policies (continued)

#### (d) Property, plant and equipment

##### (i) Owned assets

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

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.

##### (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.

#### (e) 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(j)). 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.

## Notes on the financial statements

*(Expressed in Renminbi Yuan)*

### **2 Significant accounting policies (continued)**

#### **(f) 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.

#### **(g) 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.

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.

#### **(h) Trade and other receivables**

Trade and other receivables 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. If the effect is material, receivables 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 asset.

#### **(i) 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.

#### **(j) Impairment**

The carrying amounts of the company's assets, other than investments in unit trusts (note 2(f)), inventories (note 2(g)), trade and other receivables (note 2(h)) and deferred tax assets (note 2(o)), 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.

## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 2 Significant accounting policies (continued)

#### (j) Impairment (continued)

##### (i) Calculation of recoverable amount

The recoverable amount of an asset is the greater of its 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.

#### (k) 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.

#### (l) 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.

In respect of instalment sales, under which the consideration is receivable in instalments, revenue attributable to the sales price, exclusive of interest, is recognised at the date of sale which is taken to be the point in time when the customer has accepted the goods and the related risks and rewards of ownership. The sale price is the present value of the consideration, determined by discounting the instalments receivable at the imputed rate of interest. The interest element is recognised as interest income as it is earned, on a time proportion basis that takes into account the imputed rate of interest.

##### (ii) Service income/management fees

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

## Notes on the financial statements

*(Expressed in Renminbi Yuan)*

### **2 Significant accounting policies (continued)**

#### **(m) Borrowing costs**

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

#### **(n) 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 comprise all costs that are directly attributable to research and development activities or that can be allocated on a reasonable basis to such activities. Because of the nature of the company's research and development activities, the criteria for the recognition of such costs as an asset are generally not met until late in the development stage of the project when the remaining development costs are immaterial. Hence both research costs and development costs are generally recognised as expenses in the period in which they are incurred.

##### **(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.

## Notes on the financial statements

*(Expressed in Renminbi Yuan)*

### **2 Significant accounting policies (continued)**

#### **(o) Income tax**

Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Current tax and movements in deferred tax assets and liabilities are recognised in the income statement except to the extent that they relate to items recognised directly in equity, in which case they are 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.

#### **(p) 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.

#### **(q) Dividends**

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

#### **(r) 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.

#### **(s) 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.

## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 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

	2003	2002
Materials costs	<b>734,526,206</b>	725,102,720
Direct labour	<b>32,232,111</b>	30,642,054
Factory overheads	<b>28,603,164</b>	24,482,015
Subcontracting fee	<b>35,296,903</b>	–
	<b>830,658,384</b>	780,226,789

### 5 Other operating income

	2003	2002
Sale of scrap materials	<b>1,231,969</b>	444,893
Service fee	<b>479,193</b>	349,338
Management fee	<b>50,000</b>	200,000
Other income	<b>677,555</b>	492,086
	<b>2,438,717</b>	1,486,317

### 6 Distribution expenses

	2003	2002
Staff costs	<b>31,624,201</b>	12,703,118
Travelling and transportation expenses	<b>4,986,925</b>	6,859,700
Advertising and promotion expenses	<b>3,863,799</b>	2,608,041
Entertainment expenses	<b>1,668,858</b>	1,857,441
Distribution fee paid	<b>3,218,950</b>	–
Others	<b>1,612,878</b>	1,068,543
	<b>46,975,611</b>	25,096,843

## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 7 Other operating expenses

	2003	2002
Provision for bad and doubtful debts	15,627,297	–
Provision for diminution in value of inventories	11,025,464	–
Others	893,199	802,750
	<b>27,545,960</b>	802,750

### 8 Personnel expenses

	2003	2002
Salaries, wages and bonus	70,468,817	46,394,011
Staff welfare	8,239,457	7,460,365
Contributions to retirement benefit scheme	3,977,446	2,036,539
	<b>82,685,720</b>	55,890,915
Average number of employees during the year	<b>2,122</b>	2,179

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% (2002: 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.

### 9 (Loss)/profit before tax

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

	2003	2002
(a) Net finance costs:		
Interest on bank advances and other borrowings repayable within five years	3,313,793	2,212,350
Interest on discounting of bills receivable	4,965,710	310,927
Bank charges	346,940	213,207
Interest income from bank deposits	(4,532,622)	(1,238,023)
Interest income from instalment sales	(1,893,715)	–
	<b>2,200,106</b>	1,498,461

## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 9 (Loss)/profit before tax (continued)

	2003	2002
(b) Other items:		
Auditors' remuneration	1,066,809	1,049,400
Depreciation	17,094,102	14,622,910
Operating lease rentals in respect of land use rights and properties	1,728,168	1,370,434
Research and development costs	4,849,764	844,054
Quality compensation expenses	800,000	-

### 10 Income tax (benefit)/expense

#### (a) Income tax (benefit)/expense represents:

	2003	2002
Current tax expense	2,555,755	21,050,499
Deferred tax (note 17)	(10,049,751)	(140,776)
Income tax (benefit)/expense	(7,493,996)	20,909,723

The charge for PRC income tax is calculated at the unified tax rate of 33% (2002: 33%) of the estimated assessable income for the year as determined in accordance with the relevant income tax rules and regulations of the PRC applicable to items that are charged or credited to the income statement in the same or different periods.

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

	2003	2002
Accounting (loss)/profit before tax	(22,909,078)	68,582,422
Income tax (benefit)/expense computed by applying tax rate of 33%	(7,559,996)	22,632,199
Non-deductible expenses	66,000	4,455
Tax allowance granted	-	(255,935)
Others	-	(1,470,996)
Income tax (benefit)/expense	(7,493,996)	20,909,723



## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 11 Dividends

(a) Dividends attributable to the year

	2003	2002
Final dividend proposed after the balance sheet date of RMB Nil per share (2002: RMB0.015)	–	4,272,000

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

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

	2003	2002
Final dividend in respect of the previous financial year, approved and paid during the year, of RMB0.015 per share (2002: RMB0.03 per share)	4,272,000	8,544,000

### 12 Basic (loss)/earnings per share

The calculation of basic (loss)/earnings per share is based on the loss attributable to shareholders of RMB15,415,082 (2002: profit attributable to shareholders of RMB47,672,699) divided by the weighted average number of shares in issue during the year of 284,800,000 (2002: 284,800,000).

The amount of diluted (loss)/earning per share is not presented as there were no dilutive potential ordinary shares in existence for either years.

### 13 Directors' and supervisors' emoluments

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

	2003	2002
Fees	140,000	190,000
Basic salaries, allowances and other benefits	255,000	155,994
Discretionary bonuses	640,100	679,073
Contributions to retirement benefit scheme	59,040	40,615
	<b>1,094,140</b>	<b>1,065,682</b>
Number of directors and supervisors	<b>13</b>	<b>11</b>

## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 13 Directors' and supervisors' emoluments (continued)

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

	2003	2002
RMB Nil – RMB1,000,000	<b>13</b>	11

The executive directors, non-executive directors and supervisors received individual emoluments of approximately RMB185,522 (2002: RMB186,064), RMB149,861 (2002: RMB149,882), RMB83,482 (2002: RMB149,799), RMB68,462 (2002: RMB75,585), RMB104,064 (2002: RMB58,611), RMB64,025 (2002: RMB Nil), RMB48,340 (2002: RMB Nil), RMB Nil (2002: RMB50,000), RMB128,049 (2002: RMB129,150), RMB65,199 (2002: RMB67,462), RMB57,136 (2002: RMB59,129).

The independent non-executive directors received individual emoluments of approximately RMB20,000 (2002: RMB20,000) and RMB120,000 (2002: RMB120,000), respectively.

There were no amounts paid during the years ended 31 December 2002 and 2003 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 2002 and 2003.

### 14 Senior management's emoluments

Of the five individuals with the highest emoluments, none of them (2002: four) are directors whose emoluments are disclosed in note 13 above. The emoluments in respect of the five (2002: one) individuals are as follows:

	2003	2002
Basic salaries, allowances and other benefits	<b>1,722,829</b>	604,750
Discretionary bonuses	–	–
Contributions to retirement benefit scheme	<b>11,521</b>	–
	<b>1,734,350</b>	604,750

The emolument of the five (2002: one) individual with the highest emoluments is within the following band:

	2003	2002
RMB Nil – RMB1,000,000	<b>5</b>	1

There were no amounts (2002: RMB Nil) paid during the year to the five (2002: one) individuals 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)

### 15 Property, plant and equipment

	Buildings	Machinery and equipment	Motor Vehicles	Other equipment	Total
<i>Cost:</i>					
Balance at					
1 January 2003	86,644,737	151,502,322	1,502,592	794,333	240,443,984
Additions	44,273,590	24,664,669	512,407	621,816	70,072,482
Balance at					
31 December 2003	130,918,327	176,166,991	2,014,999	1,416,149	310,516,466
<i>Depreciation and impairment losses:</i>					
Balance at					
1 January 2003	17,187,974	44,816,656	799,783	306,858	63,111,271
Charge for the year	3,193,435	13,574,527	169,381	156,759	17,094,102
Balance at					
31 December 2003	20,381,409	58,391,183	969,164	463,617	80,205,373
<i>Carrying amount:</i>					
At 31 December 2003	110,536,918	117,775,808	1,045,835	952,532	230,311,093
At 31 December 2002	69,456,763	106,685,666	702,809	487,475	177,332,713

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 2003, a factory building at net book value totalling RMB35,612,824 (2002: RMB37,027,056) was pledged to secure a short-term bank loan (note 24) (2002: a long-term bank loan (note 26)).

### 16 Construction in progress

	2003	2002
Balance at 1 January	428,000	—
Additions	3,502,699	1,676,223
Transferred to property, plant and equipment	—	(1,248,223)
Balance at 31 December	3,930,699	428,000

## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 17 Net deferred tax assets

	2003	2002
<i>Deferred tax assets and liabilities are attributable to the following:</i>		
Accounting depreciation in excess of tax depreciation	488,131	140,776
Costs of equity transaction deductible for tax purposes	–	1,470,996
Provision for bad and doubtful debts	5,157,008	–
Provision for diminution in value of inventories	3,638,403	–
Unrecognised interest in respect of receivables from instalment sales	941,965	–
Unrealised gain on investments in unit trusts	(34,980)	–
Net deferred tax assets	<b>10,190,527</b>	1,611,772
<i>Movements in net deferred tax assets:</i>		
Balance at 1 January	1,611,772	5,047,112
Transferred from income statement (note 10)	10,049,751	140,776
Transferred to retained earnings	(1,470,996)	(1,470,996)
Transferred to amount due from a shareholder (note 23(b)(ii))	–	(2,105,120)
Balance at 31 December	<b>10,190,527</b>	1,611,772

### 18 Inventories

Inventories represent:

	2003	2002
Raw materials	36,727,124	54,033,602
Work in progress	30,568,214	34,612,398
Finished goods	52,925,349	76,691,068
	<b>120,220,687</b>	165,337,068
Inventories stated at net realisable value	<b>23,239,319</b>	–

## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 19 Trade and other receivables

Trade and other receivables comprise:

	2003	2002
Trade debtors and bills receivable	<b>250,444,946</b>	206,104,879
Advance deposits to suppliers	<b>45,944,903</b>	28,134,949
Other debtors	<b>1,021,109</b>	2,465,589
	<b>297,410,958</b>	236,705,417

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

	2003	2002
Within 3 months	<b>101,308,259</b>	98,728,832
Over 3 months but less than 6 months	<b>74,046,817</b>	45,255,051
Over 6 months but less than 1 year	<b>29,826,517</b>	49,680,276
Over 1 year but less than 2 years	<b>35,893,717</b>	12,440,720
Over 2 years	<b>9,369,636</b>	–
	<b>250,444,946</b>	206,104,879

Customers are normally granted credit terms of 3 months to 12 months (2002: 3 months to 12 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 24 months (2002: 18 months).

The amount of trade and other receivables expected to be recovered after more than one year is RMB13,564,040 (2002: RMB31,450,000). All other trade and other receivables are expected to be settled within one year.

### 20 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 30.

### 21 Pledged deposits

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

## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 22 Investments in unit trusts

	2003	2002
Unit trusts held for trading, at investment manager's valuation	<b>597,500</b>	491,500

### 23 Cash and cash equivalents

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

	2003	2002
Deposits with banks	<b>65,757,200</b>	67,467,009
Cash at bank and in hand	<b>77,175,175</b>	25,127,284
	<b>142,932,375</b>	92,594,293

(b) **Non-cash transactions**

- (i) During the year ended 31 December 2003, the company utilised its bills facilities and instructed its bankers to issue certain bills to Jiangsu Mudan. In addition, the company transferred certain of its bills, which the company received from its customers, to Jiangsu Mudan. The total value of bills issued/transferred to Jiangsu Mudan amounted to RMB617,733,258 (2002: RMB Nil). On the other hand, the company received certain bank acceptance drafts from Jiangsu Mudan, totalling RMB418,739,808 (2002: RMB Nil). The bank acceptance drafts issued/received in this respect were recorded through the current account with Jiangsu Mudan without cash payment/receipt.
- (ii) Historically, income tax liabilities of the company and its shareholder, 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.

## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 24 Short-term bank loans

	2003	2002
Secured bank loan	10,000,000	–
Unsecured bank loans	65,000,000	20,000,000
	<b>75,000,000</b>	20,000,000

Details of the short-term bank loans as at 31 December 2003 are as follows:

Principal	Interest rate	Loan period	Security/Guarantee
10,000,000	5.04% p.a.	22 December 2003 to 22 June 2004	Pledged over factory building (note 15)
15,000,000	4.536% p.a.	25 September 2003 to 24 March 2004	Nil
10,000,000	4.536% p.a.	28 November 2003 to 27 May 2004	Nil
20,000,000	4.536% p.a.	28 November 2003 to 27 May 2004	Guaranteed by Jiangsu Mudan
20,000,000	4.536% p.a.	16 December 2003 to 15 June 2004	Guaranteed by Jiangsu Mudan
<u>75,000,000</u>			

### 25 Trade and other payables

Trade and other payables comprise:

	2003	2002
Trade creditors	79,739,523	86,144,676
Bills payable	508,364,000	191,630,000
Accrued salaries, bonus and welfare fund	26,075,373	16,065,740
Other payables	50,796,778	23,892,340
	<b>664,975,674</b>	317,732,756

Certain bills payable of RMB416,364,000 as at 31 December 2003 (2002: RMB Nil) were guaranteed by Jiangsu Mudan.

## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 25 Trade and other payables (continued)

An ageing analysis of trade creditors and bills payable is as follows:

	2003	2002
Due within 3 months	445,739,523	188,774,676
Due after 3 months within 6 months	142,364,000	89,000,000
	588,103,523	277,774,676

### 26 Long-term bank loan

	2003	2002
Secured bank loan (note 15)	–	20,000,000

### 27 Capital and reserves

#### (a) Share capital

	2003	2002
Registered, issued and fully paid:		
196,250,000 (2002: 196,250,000) domestic shares of RMB1.00 each	196,250,000	196,250,000
88,550,000 (2002: 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) 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 issue 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.

No transfer was made to the statutory surplus reserve in 2003 (2002: transfer of RMB4,517,948) as there was no net profit available for appropriation.



## Notes on the financial statements

*(Expressed in Renminbi Yuan)*

### **27 Capital and reserves (continued)**

#### **(c) 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.

No transfer was made to the statutory public welfare fund in 2003 (2002: transfer of RMB4,517,948) as there was no net profit available for appropriation.

#### **(d) 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 be deemed 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 IFRSs.

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 2003 amounted to RMB31,488,885 (2002: RMB57,178,346). After the balance sheet date the directors had not recommended the payment of proposed a final dividend in respect of the year ended 31 December 2003 (2002: final dividend of RMB0.015 per share).

## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 28 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 and amounts due to shareholders. The company does not hold or issue financial instruments for trading purposes. The company had no positions in derivatives contracts at 31 December 2002 and 2003. Exposure to credit, interest rate and currency risk arises in the normal course of the company's business.

#### (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 a 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.

Amounts due from customers (net of provision for bad and doubtful debts) which represented more than 10% of the outstanding receivables at each balance sheet date are as follows:

	2003	2002
Guangzhou Bai Yun Hua Gang Automobile Company	<b>57,732,572</b>	76,788,993

#### (b) Interest rate risk

The interest rates and terms of repayment of the bank loans of the company are disclosed in notes 24 and 26.

#### (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)

### 28 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 2002 and 2003.

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, 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) Investments in unit trusts

The carrying value of investments in unit trusts approximates its fair value as the unit trusts are stated at bid price quoted by the investment managers at the balance sheet date.

- (iii) Bank loans

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

### 29 Commitments

- (a) Capital commitments outstanding at 31 December 2003 not provided for in the financial statements were as follows:

	2003	2002
Contracted for	<b>119,301</b>	–

- (b) At 31 December 2003, the total future minimum lease payments under non-cancellable operating leases are as follows:

	2003	2002
Less than one year	<b>1,005,500</b>	560,000
Between one and five years	<b>4,022,000</b>	2,240,000
More than five years	<b>13,487,020</b>	7,700,000
	<b>18,514,520</b>	10,500,000

The company leases rights to use four (2002: two) pieces of land and a property (2002: one) 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)

### 30 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:

	Notes	2003	2002
Purchases from shareholders/a related company	(i)	<b>67,015,391</b>	36,931,833
Rent paid for land use rights	(ii)	<b>786,833</b>	460,000
Rent paid for property	(iii)	<b>100,000</b>	100,000
Management fee received	(iv)	<b>50,000</b>	200,000
Acquisition of plant and machinery	(v)	<b>68,080,923</b>	—
Subcontracting fee paid	(vi)	<b>9,892,723</b>	—
Sales of scrap materials	(vii)	<b>827,402</b>	—

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, Zhangjiagang Automobile Accessories Factory and Zhangjiagang Jishun Transportation Industrial Co., Ltd.) during the year.
- (ii) The company has entered into lease agreements with Jiangsu Mudan whereby the company is granted rights to use four (2002: 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 RMB905,500 (2002: 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. The custodian agreement with Jiangsu Mudan was terminated in April 2003.
- (v) During the year, the company acquired one factory building and certain machineries from Jiangsu Mudan at an amount of RMB68,080,923.
- (vi) During the year, the company paid subcontracting fees, totalling RMB9,892,723 to Jiangsu Mudan (2002: RMB Nil).
- (vii) During the year, the company sold certain scrap materials to a shareholder (Zhangjiagang Mudan Bus Parts Co., Ltd.) which amounted to RMB827,402 (2002: RMB Nil).
- (viii) During the year ended 31 December 2003, the company utilised its bills facilities and instructed its bankers to issue certain bills to Jiangsu Mudan. In addition, the company transferred certain of its bills, which the company received from its customers, to Jiangsu Mudan. The total value of bills issued/transferred to Jiangsu Mudan amounted to RMB617,733,258 (2002: RMB Nil). On the other hand, the company received certain bills from Jiangsu Mudan, totalling RMB418,739,808 (2002: RMB Nil). In consequence, the company provided certain interest-free advances to Jiangsu Mudan during the year ended 31 December 2003. The maximum outstanding balance of the advances to Jiangsu Mudan was RMB148,769,216 during the year ended 31 December 2003 and the outstanding balance of the advances was RMB Nil at 31 December 2003.

During the year ended 31 December 2002, the company obtained certain interest-free advances from Jiangsu Mudan. The maximum outstanding balance of the advances from Jiangsu Mudan was RMB77,917,522 during the year ended 31 December 2002 and the outstanding balance of the advances was RMB Nil at 31 December 2002.

## Notes on the financial statements

(Expressed in Renminbi Yuan)

### 30 Material related party transactions (continued)

Notes: (continued)

- (ix) During the years ended 31 December 2002 and 2003, Jiangsu Mudan allowed the company to use the trademark of "Mudan", certain of its sales offices, office equipment and public facilities at nil consideration.
- (x) Jiangsu Mudan received sales receipts on behalf of the company which amounted to RMB1,645,000 (2002: RMB22,509,230) during the year ended 31 December 2003.
- (xi) The company received sales receipts on behalf of Jiangsu Mudan which amounted to RMB20,138,311 during the year ended 31 December 2002. There was no sales receipts by the company on behalf of Jiangsu Mudan for the year ended 31 December 2003.
- (xii) During the year ended 31 December 2003, the company acted as the agent of Jiangsu Mudan and purchased certain raw materials, totalling RMB4,355,974 (2002: RMB11,490,811), on its behalf. On the other hand, Jiangsu Mudan acted as the agent of the company and purchased certain raw materials, totalling RMB3,133,037 (2002: RMB28,096,784), 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, totalling RMB40,193,903 (2002: RMB5,478,541). No service fee was paid by the company in this respect.
- (xiv) Jiangsu Mudan made payments for certain expenses on behalf of the company which amounted to RMB3,689,020 during the year ended 31 December 2003. There were no payments for expenses on behalf of the company for the year ended 31 December 2002.
- (xv) As at 31 December 2003, certain bank loans of the company totalling RMB40,000,000 (2002: RMB Nil) were guaranteed by Jiangsu Mudan (note 24).
- (xvi) As at 31 December 2003, certain bills payables of the company totalling RMB416,364,000 (2002: RMB Nil) were guaranteed by Jiangsu Mudan (note 25).

The directors of the company are of the opinion that the above transactions (excluding notes (viii) to (xvi)) 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.

### 31 Ultimate holding company

The directors consider the ultimate holding company at 31 December 2003 to be Zhangjiagang Municipal Public Assets Management Co., Ltd, which is a state-owned enterprise established in the PRC.

## Reconciliation of net (loss)/profit and net assets under International Financial Reporting Standards (“IFRSs”) and PRC accounting rules and regulations

(Expressed in Renminbi yuan)

	Note	2003		2002	
		Loss 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		<b>(25,689,461)</b>	<b>348,433,819</b>	45,179,480	374,123,280
Adjustments:					
Restatement of costs of issuing shares	(i)	<b>4,457,563</b>	–	4,457,563	(4,457,563)
Recognition of net deferred tax assets	(ii)	<b>10,049,751</b>	<b>10,190,527</b>	140,776	1,611,772
Restatement of instalment receivables	(iii)	<b>(2,854,439)</b>	<b>(2,854,439)</b>	–	–
Restatement of investments in unit trusts	(iv)	<b>92,500</b>	<b>92,500</b>	–	–
Restatement of overprovided income tax expense in respect of prior years	(v)	–	–	(2,105,120)	–
Restatement of dividends	(vi)	–	–	–	4,272,000
Restatement of current tax effect of the costs of issuing shares	(vii)	<b>(1,470,996)</b>	–	–	–
As determined pursuant to IFRS		<b>(15,415,082)</b>	<b>355,862,407</b>	47,672,699	375,549,489

### 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 IFRSs, 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 IFRSs adjustments as noted in notes (i), (iii) and (iv), certain accounting depreciation in excess of tax depreciation and certain provision for accounting purposes for the year ended 31 December 2003.
- (iii) Under the PRC accounting rules and regulations, instalment receivables are stated at their cost less allowance for doubtful accounts. Pursuant to IFRSs, instalment receivables are determined by discounting the expected future cash flows at an imputed rate of interest. The interest element is recognised as interest income as it is earned on a time proportion basis that takes into account the imputed rate of interest.
- (iv) Under the PRC accounting rules and regulations, investments in unit trusts are stated at lower of cost or fair value. Pursuant to IFRSs, investments in unit trusts are stated at fair value.
- (v) This amount represents write-back of prior years' income tax expense in the PRC financial statements. Under the IFRSs financial statements, the overprovision was adjusted in the period to which it occurred.
- (vi) Under the PRC accounting rules and regulations, dividends are recognised as a liability in the period to which they related. Pursuant to IFRSs, dividends are recognised in the period in which they are declared.
- (vii) The amount represents the different treatment on the current tax effect of the costs of issuing shares as noted in note (i). Under the PRC accounting rules and regulations, the current tax effect of the costs of issuing shares are recognised as current tax charge as the costs of issuing shares are recognised as an asset and amortised to the income statement over 2 years. Pursuant to IFRSs, the current tax effect of the costs of issuing shares are accounted for as part of the equity transaction as the costs of issuing shares are accounted for as part of the equity transaction.

## Five year summary

(Expressed in Renminbi Yuan)

	2003	Year ended 31 December			
		2002	2001	2000	1999
<b>Results</b>					
Revenue	<b>910,111,382</b>	888,526,140	857,038,069	775,719,118	507,051,801
<b>(Loss)/profit from operations</b>	<b>(20,708,972)</b>	70,080,883	77,671,765	48,808,986	46,793,734
Net finance costs	<b>(2,200,106)</b>	(1,498,461)	(4,539,496)	(7,819,607)	(6,465,142)
<b>(Loss)/profit before tax</b>	<b>(22,909,078)</b>	68,582,422	73,132,269	40,989,379	40,328,592
Income tax benefit/(expense)	<b>7,493,996</b>	(20,909,723)	(23,702,448)	(13,711,295)	(13,493,235)
<b>(Loss)/profit attributable to shareholders</b>	<b>(15,415,082)</b>	47,672,699	49,429,821	27,278,084	26,835,357
<b>Assets and liabilities</b>					
Property, plant and equipment	<b>230,311,093</b>	177,332,713	177,719,337	188,288,577	221,701,919
Construction in progress	<b>3,930,699</b>	428,000	–	–	–
Net deferred tax assets	<b>10,190,527</b>	1,611,772	5,047,112	2,105,120	2,105,120
Total current assets	<b>859,441,244</b>	564,739,422	415,351,153	312,360,640	121,170,495
Total current liabilities	<b>(748,011,156)</b>	(348,562,418)	(240,225,816)	(240,013,956)	(109,515,237)
Total assets less current liabilities	<b>355,862,407</b>	395,549,489	357,891,786	262,740,381	235,462,297
Non-current liabilities	<b>–</b>	(20,000,000)	(20,000,000)	–	–
	<b>355,862,407</b>	375,549,489	337,891,786	262,740,381	235,462,297
Share capital	<b>284,800,000</b>	284,800,000	284,800,000	204,300,000	204,300,000
Reserves	<b>71,062,407</b>	90,749,489	53,091,786	58,440,381	31,162,297
	<b>355,862,407</b>	375,549,489	337,891,786	262,740,381	235,462,297