



Far Eastern
Polychem
Industries
Limited

FAR EASTERN POLYCHEM INDUSTRIES LIMITED

(遠東化聚工業股份有限公司)*

(Incorporated in Bermuda with limited liability)

(Stock Code: 8012)

HALF-YEARLY RESULTS FOR THE SIX MONTHS ENDED 30TH JUNE 2005

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

HALF-YEARLY RESULTS HIGHLIGHTS

- Far Eastern Polychem Industries Limited (the “Company”) and its subsidiaries (together the “Group”) are principally engaged in the production and distribution of four major categories of polyester products, namely bottle-grade polyethylene terephthalate (“PET”) chips, polyester filaments and polyester staple fibers, and the dyeing and finishing of polyester fabrics in the People’s Republic of China (the “PRC”).
- The Group achieved a turnover of approximately HK\$1,417 million for the six months ended 30th June 2005, representing an increase of 12%, as compared to the corresponding six-months period ended 30th June 2004.
- Due to the upsurge in price of petrochemical raw materials and the oversupply within the PRC’s domestic polyester industry, the loss attributable to shareholders was approximately HK\$102 million, for the six months ended 30th June 2005 while the profit attributable to shareholders was approximately HK\$27 million for the corresponding six-months period ended 30th June 2004.
- Loss per share for the six months ended 30th June 2005 was HK\$0.25 per share while the earnings per share for the corresponding six-months period ended 30th June 2004 was HK\$0.06 per share.

HALF-YEARLY FINANCIAL STATEMENTS (UNAUDITED)

The directors of the Company (the “Directors”) have the pleasure of presenting the unaudited consolidated financial statements of the Group for the six months ended 30th June 2005 and, for comparison purposes, the audited consolidated balance sheet as at 31st December 2004 and figures for the corresponding six-months period ended 30th June 2004 in respect of the unaudited consolidated income statement, statement of changes in shareholders’ equity and cash flow statement as follows:

(a) Consolidated balance sheet

	<i>Note</i>	As at 30th June 2005 HK\$’000 (Unaudited)	As at 31st December 2004 HK\$’000 (Audited)
Non-current assets			
Investment in an associate		77,965	80,694
Available-for-sale investments		3,009	3,009
Property, plant and equipment		1,947,236	1,742,616
Land use rights		162,255	136,199
Deferred assets		5,263	5,712
Other non-current assets		534	300
		<u>2,196,262</u>	<u>1,968,530</u>
Current assets			
Inventories		662,336	663,968
Deposits, prepayments and other receivables		84,878	35,944
Trade and notes receivables	3	357,817	406,350
Tax recoverable		9,815	7,466
Cash and bank deposits		289,331	323,050
		<u>1,404,177</u>	<u>1,436,778</u>
Current liabilities			
Trade payables	4	583,059	561,422
Other payables and accruals		120,611	79,665
Taxes payable		8,232	74
Short-term bank loans		326,765	295,645
Long-term bank loans, current portion		523,233	343,023
		<u>1,561,900</u>	<u>1,279,829</u>
Net current (liabilities) asset		<u>(157,723)</u>	<u>156,949</u>
Total assets less current liabilities		<u>2,038,539</u>	<u>2,125,479</u>
Non-current liabilities			
Long-term bank loans, non-current portion		832,683	776,765
Deferred tax liabilities		3,394	3,394
Total non-current liabilities		<u>836,077</u>	<u>780,159</u>
Minority interest		39,278	39,316
Net assets		<u>1,163,184</u>	<u>1,306,004</u>
Represented by:			
Share capital		410,296	410,296
Reserves		752,888	895,708
		<u>1,163,184</u>	<u>1,306,004</u>

(b) **Unaudited consolidated income statement**

	<i>Note</i>	For the six months ended 30th June		For the three months ended 30th June	
		2005	2004	2005	2004
		<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
		<i>(unaudited)</i>	<i>(unaudited)</i>	<i>(unaudited)</i>	<i>(unaudited)</i>
PET chips		856,074	790,294	425,550	405,590
Polyester filaments		116,236	117,993	65,853	63,175
Polyester staple fibers		263,802	189,291	134,768	105,592
Finished fabrics		179,784	169,330	78,403	84,213
Others		922	—	595	—
Total Sales, net		1,416,818	1,266,908	705,169	658,570
Cost of sales		(1,413,329)	(1,158,431)	(704,671)	(621,614)
Gross profit		3,489	108,477	498	36,956
Other operating income	5	10,351	8,339	2,532	4,174
Distribution costs		(51,800)	(41,902)	(27,864)	(20,069)
Administrative expenses		(34,853)	(30,110)	(16,686)	(13,558)
(Loss) profit from operations	6	(72,813)	44,804	(41,520)	7,503
Finance costs, net	7	(26,288)	(12,656)	(14,176)	(6,415)
Share of result of an associate before tax		(2,729)	(1,342)	(974)	(827)
(Loss) profit before tax		(101,830)	30,806	(56,670)	261
Income tax expense	8	—	(4,228)	—	(20)
(Loss) profit before minority interest		(101,830)	26,578	(56,670)	241
Minority interest		39	34	15	16
(Loss) profit attributable to shareholders		(101,791)	26,612	(56,655)	57
Basic (loss) earnings per share	9(a)	HK\$(0.25)	HK\$0.06	HK\$(0.14)	HK\$0.00
Diluted (loss) earnings per share	9(b)	N/A	N/A	N/A	N/A

(c) **Unaudited consolidated statement of changes in shareholders' equity**

For the year ended 31st December 2004:

	Share capital \$'000	Share premium \$'000	Statutory reserve fund \$'000	Revaluation reserve \$'000	Cumulative translation adjustments \$'000	Retained earnings \$'000	Total reserve \$'000	Total equity \$'000
Balance as at 1st January 2004	410,296	523,001	102,646	5,645	2,203	261,057	894,552	1,304,848
Profit appropriation	—	—	5,684	—	—	(5,684)	—	—
Dividends	—	—	—	—	—	(41,030)	(41,030)	(41,030)
Profit for the six months ended 30th June 2004	—	—	—	—	—	26,612	26,612	26,612
Balance as at 30th June 2004	410,296	523,001	108,330	5,645	2,203	240,955	880,134	1,290,430
Surplus on revaluation of buildings	—	—	—	15,299	—	—	15,299	15,299
Realisation of revaluation reserve due to additional depreciation	—	—	—	(1,411)	—	1,411	—	—
Profit for the six months ended 31st December 2004	—	—	—	—	—	1,048	1,048	1,048
Translation adjustments	—	—	—	—	(773)	—	(773)	(773)
Balance as at 31st December 2004	<u>410,296</u>	<u>523,001</u>	<u>108,330</u>	<u>19,533</u>	<u>1,430</u>	<u>243,414</u>	<u>895,708</u>	<u>1,306,004</u>

For the six months ended 30th June 2005:

	Share capital \$'000	Share premium \$'000	Statutory reserve fund \$'000	Revaluation reserve \$'000	Cumulative translation adjustments \$'000	Retained earnings \$'000	Total reserve \$'000	Total equity \$'000
Balance as at 1st January 2005	410,296	523,001	108,330	19,533	1,430	243,414	895,708	1,306,004
Dividends	—	—	—	—	—	(41,029)	(41,029)	(41,029)
Loss for the six months ended 30th June 2005	—	—	—	—	—	(101,791)	(101,791)	(101,791)
Balance as at 30th June 2005	<u>410,296</u>	<u>523,001</u>	<u>108,330</u>	<u>19,533</u>	<u>1,430</u>	<u>100,594</u>	<u>752,888</u>	<u>1,163,184</u>

(d) **Unaudited consolidated cash flow statement**

	For the six months ended 30th June	
	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
CASH FLOW FROM OPERATING ACTIVITIES		
Cash generated from (used in) operations	71,890	(22,302)
Interest paid	(30,704)	(10,973)
Income tax paid	—	(6,566)
	<hr/>	<hr/>
Net cash generated from (used in) operating activities	41,186	(39,841)
CASH FLOW FROM INVESTING ACTIVITIES		
Purchase of fixed assets	(273,474)	(18,794)
Purchase of land use right	(27,865)	—
Interest received	449	896
Increase in other long term assets	(233)	(465)
	<hr/>	<hr/>
Net cash used in investing activities	(301,123)	(18,363)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from short-term bank loans	137,247	148,603
Proceeds from long-term bank loans	427,578	180,000
Repayments of short-term bank loans	(106,127)	(87,140)
Repayments of long-term bank loans	(191,451)	(94,000)
Dividend paid	(41,029)	—
	<hr/>	<hr/>
Net cash from financing activities	226,218	147,463
	<hr/>	<hr/>
Net (decrease) increase in cash and cash equivalents	(33,719)	89,259
Cash and cash equivalents, beginning of the period	323,050	190,912
	<hr/>	<hr/>
Cash and cash equivalents, end of the period	<u>289,331</u>	<u>280,171</u>

(e) **Notes to the unaudited financial statements**

1) **Basis of presentation**

The unaudited financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) and the disclosure requirements of the Hong Kong Companies Ordinance and the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited. The unaudited financial statements have been prepared under the historical cost convention as modified by the revaluation of buildings.

The accounting policies and methods of computation used in the preparation of the unaudited financial statements are consistent with those used in the annual financial statements as at and for the year ended 31st December 2004 except that the Group has adopted IFRS 2 — Share-based Payment and IFRS 5 — Non-Current Assets Held for Sale and Discontinued Operations which are mandatory for the financial year beginning on and after 1 January 2005. The adoption of these new IFRS has no material effect on the Group’s financial statements.

2) **Fixed assets**

During the six months ended 30th June 2005, additions to fixed assets amounted to approximately HK\$285,352,000 (2004: HK\$19,089,000).

3) **Trade and note receivables**

	As at 30th June 2005 HK\$’000	As at 31st December 2004 HK\$’000
Trade receivables		
Current to 30 days	109,384	109,527
31 to 60 days	53,326	105,070
61 to 90 days	27,641	49,717
Over 90 days	49,794	27,766
	<hr/>	<hr/>
	240,145	292,080
Less: provision for doubtful debts	(3,569)	(4,224)
	<hr/>	<hr/>
	236,576	287,856
Notes receivable	121,241	118,494
	<hr/>	<hr/>
	<u>357,817</u>	<u>406,350</u>

Credit policy

No credit terms were granted to the PRC customers except for those with sound financial background and good repayment histories, for which the Group would grant credit terms ranging from 7 days to 60 days. For overseas customers, the Group would grants credit terms from 90 to 120 days. In addition, a predetermined maximum credit limit is set for each customer.

Concentrations of credit risk

Concentrations of credit risk with respect to trade receivables are limited due to the Group's large number of customers, who are internationally dispersed, cover the spectrum of manufacturing and distribution and have a variety of end markets in which they sell. Due to these factors, management believes that no additional credit risk beyond amounts provided for collection losses, if any, is inherent in the Group's trade receivables.

4) Trade payables

	As at 30th June 2005 HK\$'000	As at 31st December 2004 HK\$'000
Trade payables		
Current to 30 days	119,216	224,155
31 to 90 days	260,879	274,597
Over 90 days	29,144	62,670
	<hr/>	<hr/>
	409,239	561,422
Notes payables	173,820	—
	<hr/>	<hr/>
	<u>583,059</u>	<u>561,422</u>

5) Other operating income

Other operating income mainly represented income from sales of scrap materials.

6) **(Loss) profit from operations**

The following items have been included in arriving at (loss) profit from operations:

	For the six months 30th June	
	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
Cost of inventories recognised as expense included in 'Cost of sales')	1,306,744	1,158,431
Staff costs		
- wages and salaries	37,757	28,997
- pension costs (defined contribution plan)	2,355	2,404
- other staff welfare costs	8,686	6,567
Depreciation on property, plant and equipment	80,636	73,717
Amortisation of land use rights (included in 'Administrative expenses')	1,809	1,402
Amortisation of deferred assets (included in 'Cost of sales')	648	685
Operating lease rentals on property	2,845	1,887
Write (back) down bad and doubtful debts (included in administrative expense)	(655)	3,309
	<u> </u>	<u> </u>

7) **Finance costs, net**

	For the six months ended 30th June	
	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
Interest expenses on bank loans wholly repayable within five years	30,704	10,973
Less: amount capitalised as construction-in-progress	(11,885)	(295)
Interest income	(449)	(896)
Net foreign currency exchange loss	3,998	2,022
Other financial expenses	3,920	852
	<u> </u>	<u> </u>
	<u>26,288</u>	<u>12,656</u>

8) **Income tax expense**

The Company is exempted from taxation in Bermuda.

No Hong Kong profits tax was provided as the Group had no assessable profits arising in or deriving from Hong Kong.

The Company's subsidiaries registered in the PRC are subject to Enterprise Income Tax ("EIT") on the taxation income as reported in their PRC statutory accounts adjusted in accordance with relevant PRC income tax laws. The general applicable EIT rate is 33%. However, being registered in a designated high-technology development zone in the PRC, Far Eastern Industries (Shanghai) Ltd. ("FEIS") (the Company's major operating subsidiary in the PRC) is entitled to a preferential EIT rate of 15%. In addition, in accordance with the PRC "Law of Enterprise Income Tax for Enterprise with Foreign Investment", FEIS is entitled to full exemption from EIT for the first two years and a 50% reduction in EIT for the next three years, commencing from the first profitable year after offsetting all tax losses carried forward from the previous five years. Furthermore, being qualified as a "High-technology Enterprise", FEIS is entitled to a further reduced EIT rate of 10% for an additional three years following the end of the five-year period during which FEIS enjoyed the preferential EIT treatment as stated above. The "High-technology Enterprise" status is subject to review every year. The first profitable year of FEIS was 1999.

No PRC EIT had been provided for all the other PRC subsidiaries of the Company as they were either in pre-operating stage or had incurred losses for the year. The deferred tax assets derived from losses for previous years have not been recognized as these PRC subsidiaries have not yet commenced their first profitable year. A tax holiday creates a non-taxable status and the effective tax rate is zero. Since the loss carryforward accumulated prior to tax holiday will be either lost or used up before the tax holiday is activated, no deferred tax asset is recognized with respect to the loss carryforward.

The amount of income tax expense charged to the consolidated income statement represents:

	For the six months ended 30th June	
	2005	2004
	<i>\$'000</i>	<i>\$'000</i>
Current tax - PRC taxation	—	4,228
Share of tax of an associate	—	—
	<hr/>	<hr/>
Taxation charge	—	4,228
	<hr/> <hr/>	<hr/> <hr/>

9) **(Loss) earnings per share**

(a) **Basic (loss) earnings per share**

Basic (loss) earnings per share is calculated by dividing the (loss) profit attributable to shareholders by the weighted average number of ordinary shares in issue during the year.

	For the six months ended 30th June	
	2005	2004
	<i>\$'000</i>	<i>\$'000</i>
(Loss) profit attributable to shareholders (\$'000)	(101,791)	26,612
Weighted average number of ordinary shares in issue ('000)	<u>410,296</u>	<u>410,296</u>
Basic (loss) earnings per share (\$ per share)	<u>(0.25)</u>	<u>0.06</u>

(b) **Diluted (loss) earnings per share**

Diluted (loss) earnings per share is not presented because there has been no potentially dilutive ordinary shares in existence during the year.

10) Segmental information

The Group operates principally in the production and distribution of PET chips, polyester filaments and polyester staple fibers, and dyeing and finishing of polyester textile products and have four strategic business units (“SBUs”), namely the Chip SBU, the Filament SBU, the Fiber SBU and the Dyeing and Finishing SBU which are managed separately.

Primary reporting format — business segments

	Chip SBU		Filament SBU		Fiber SBU		Dyeing and Finishing SBU		Others		Consolidated	
	For the six months ended 30th June											
	2005	2004	2005	2004	2005	2004	2005	2004	2005	2004	2005	2004
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
Sales, net	856,074	790,294	116,236	117,993	263,802	189,291	179,784	169,330	922	—	1,416,818	1,266,908
Segment result	17,554	86,755	(11,952)	(1,699)	(18,396)	(2,617)	15,468	26,038	815	—	3,489	108,477
Unallocated corporate expenses											(76,302)	(63,673)
(Loss) profit from operations											(72,813)	44,804
Finance costs, net											(26,288)	(12,656)
Share of result of an associate before tax											(2,729)	(1,342)
(Loss) profit before tax											(101,830)	30,806
Income tax expense											—	(4,228)
Group (loss) profit before minority interest											(101,830)	26,578
Minority interest											39	34
(Loss) profit attributable to shareholders											(101,791)	26,612

Secondary report format — geographical segments

An analysis by geographical segment, as determined by location of customers, is presented below.

	For the six months ended	
	30th June	
	2005	2004
	\$'000	\$'000
Sales		
- The PRC	1,110,845	1,085,007
- Europe	135,378	153,950
- Middle East	13,522	12,414
- Asia (excluding PRC)	50,485	15,537
- North America	82,569	—
- Others	24,019	—
	<u>1,416,818</u>	<u>1,266,908</u>

11) Related party transactions

The Company's wholly-owned subsidiary, Far Eastern Industries (Shanghai) Ltd., is party to an on-going technological licence agreement with an associate of the Company's controlling shareholder, Far Eastern Textile Ltd. The Agreement, entered into prior to the Company's listing in January, 2000, is for a term of ten years expiring on 31st December 2009 and is in its sixth year of operation.

A waiver from strict compliance with the announcement and shareholders' approval requirements contained in Chapter 20 of the GEM Listing Rules was granted by the Stock Exchange at the time of the Company's listing. At the time of listing, the Company set and disclosed annual caps on the licence fee payable by FEIS for the Financial years up to the year ended 31st December 2001. In January 2002, the annual caps on the licence fee payable by FEIS were renewed at the same level for a period of three years from 1st January 2002 to 31st December 2004.

On 15th April 2005, the parties to the Agreement agreed to a reduction in the annual licence fee payable by FEIS from US\$10 per metric tonne of polyester polymer to US\$2.50 per metric tonne of polyester and agreed to set a reduced annual cap for a further period of three years from 1st January 2005 to 31st December 2007. The annual cap in respect of the licence fee payable by FEIS has been reduced from US\$1.5 million to US\$0.7 million (approximately HK\$5.5 million) per annum.

For the six months ended 30th June 2005, the Company has paid, an amount of approximately HK\$2,289,000 (2004: HK\$5,837,000) technological licence fee payable to Far Eastern Investment (Holdings) Company Limited, a subsidiary of Far Eastern Textile Limited, on the basis of the agreed reduction in the License fee rate.

12) Commitments

(a) Capital commitments

As at 30th June 2005, the Group had the following capital commitments which were not provided for in the accounts:

	As at 30th June	
	2005	2004
	HK\$'000	HK\$'000
Authorised and contracted for		
- Acquisition of property, plant and equipment	<u>42,984</u>	<u>85,177</u>

(b) Investment commitments

As at 30th June 2005, the Group had entered into agreement with the minority shareholders of FEDP (Holding) Limited ("FEDP"), currently an 80% subsidiary of the Group, to have the right to acquire the remaining 20% of the shareholding in FEDP. In addition, the minority shareholders of FEDP also have the right to sell the remaining 20% shareholding of FEDP to the Group. These rights are exercisable during the period from 2 October 2006 to 31 October 2006. The consideration upon exercise of the rights by either of the parties is US\$5,000,000 (equivalent to approximately RMB39,000,000) together with interest calculated at London Inter Bank Offer Rate plus 0.5% from 1 November 2004 to the date of exercise.

DIVIDEND

The Directors do not recommend an interim dividend for the six months ended 30th June 2005. The Group did not declare any dividends for the corresponding six months period ended 30th June 2004.

On 24th March 2005, the Directors declared a final dividend of HK\$0.10 per ordinary share for the year ended 31st December 2004, totaling approximately HK\$41,029,600.

OPERATIONAL REVIEW

The six months period ended 30th June 2005 was a tough period for the Group, the business environment was significantly affected by (i) the upsurge raw materials prices; (ii) the oversupply within the PRC's domestic polyester industry; and (iii) the trade disputes over PRC textile products exported to the United States and European Union. The Group incurred a loss of approximately HK\$102 million primarily caused by the increase in costs of production. The over-supply situation of domestic polyester products in the PRC made it difficult for the Group to pass on the increasing raw material costs to the customers.

The upsurge in raw material prices

Driven by various factors, crude oil prices have been rising since the second quarter of 2004. Since the principal raw materials for polyester production, such as PTA and mono-ethylene glycol ("MEG"), are all petrochemical derivative products, the rising crude oil price inevitably led to the increase of raw material prices, hence, an immediate rise in production costs and, to certain extent, a narrower profit margin for the Group's products.

Due to the limited supply of PTA and MEG in Asia, the average purchase cost of the PTA and MEG increased by 20% and 28% respectively in the six months period ended 30th June 2005 as compared with those in the corresponding period in 2004 while the average selling price of the Group's products increased at a lesser rate, hence the lower profit margin.

The oversupply within the PRC's domestic polyester industry

Although demand for polyester products showed growth, the over-supply situation of domestic polyester products in the PRC added pressure on product prices and made it more difficult for the polyester producers to pass on the increasing raw material costs to the customers. As a result, many sales are on low or sometimes negative margins. With a strong emphasis on economy of scale, it can be observed that major polyester producers in the PRC continue to expand their production capacities which will put additional pressure on the market and on smaller producers in particular.

Trade disputes over PRC textile products exported to United State and European Union

The revenue of our filament, dyeing and finishing business were affected, as our customers in those business adopted a more conservative purchasing strategies when there were trade disputes over PRC textile products exported to United State and European Union.

Active changes in product mix to react to unfavorable business environment

The following is a summary of the Group's sales volume achieved by various strategic business units ("SBUs"):

	For the six month ended 30th June		Percentage increase/ (decrease)
	2005	2004	(%)
Chip SBU (tonnes)	89,887	92,524	(3)%
Filament SBU (tonnes)	8,962	10,433	(14)%
Fiber SBU (tones)	28,067	23,061	22%
Dyeing and Finishing SBU (thousand yards)	13,390	13,223	1%

The sales volume of chips for the Group for the six months ended 30th June 2005 remained comparable with that of the six months ended 30th June 2004.

The decrease in sales volume of filament was anticipated due to the Group's strategic shift to produce more high-end specialty products such as low denier filaments which are subject to relatively less competition in the PRC. Although such products command higher selling prices, they require more sophisticated manufacturing processes that are more time consuming and they also lead to a drop in production and sales volume.

Both the Fiber SBU and the Dyeing and Finishing SBU have gradually expanded their production capacities and client bases in the past years which resulted in growth in sales volume in the second quarter of 2005.

Active management of domestic and export sales mix

In view of the fierce competition for polyester products market in the PRC, the Group endeavors to achieve an optimal mix of domestic and export sales. The export ratio in terms of sales revenue increased from 14% for the six months ended 30th June 2004 to 22% for the six months ended 30th June 2005. The increase in exports helps the Company to mitigate the effects of over competition from the local manufacturers in the PRC market. Besides, the Group will put more efforts to expand the Asia and Middle East market so as to alleviate the effect of trade disputes over PRC textile products exported to the United States and the European Union.

FUTURE PROSPECTS

The Group will continue to focus on high value-added and specialty products

The Group will continue to focus on high value-added and specialty products. The Directors believe that diversification and differentiation are key to the Group's future development. The Group will continue to position itself at the high-end market, to produce products that involve technology that cannot easily be copied by other producers in China. The Group will continue to focus on the production of high-quality bottle-grade PET chips for carbonated soft drink and hot-filled bottles, low denier filaments and specialty fabrics. The Directors believe that the Group's current product mix is competitive in the current adverse market conditions, and the Directors will continue to monitor the market situation so as to achieve the optimal product mix with a view to maximising profitability.

The investment in a joint venture to produce terephthalic acid ("PTA") in the PRC

In 2003, the Group formed a joint venture with two connected parties to establish and operate a new PTA plant adjacent to the Group's existing manufacturing facilities in Pudong, Shanghai. This PTA plant is now under construction as planned and is expected to commence operation by the end of 2005. The Group's investment amounted to US\$11.1 million. Since PTA is a fundamental raw material for manufacturing polyester products, this investment will enable the Group to vertically integrate its production process. The Directors are confident that it will also improve the Group's production efficiency and, as a result, strengthen its competitiveness.

MANAGEMENT DISCUSSION AND ANALYSIS

RESULTS OF OPERATIONS

1. Sales, net

The Group's total sales increased by 12% from HK\$1,267 million for the six months ended 30th June 2004 to HK\$1,417 million for the six months ended 30th June 2005. The increase was mainly attributable to the increase in average unit selling prices of polyester products driven by the increase in raw material costs during the six months ended 30th June 2005.

2. Cost of sales and gross margin

The average unit costs of PTA and MEG rose by 20% and 28% respectively for the six months ended 30th June 2005 when compared to those in the corresponding period in 2004. Consequently, the cost of sales increased by 22%, as compared to those in the corresponding period in 2004, whereas sales only increased by 12%. The unparalleled increase in cost of sales resulted in the erosion in the profit margin of the Group.

3. Distribution costs, administrative expenses, other income and finance costs

As the export ratio of the Group in terms of sales revenue increased from 14% for the six months ended 30th June 2004 to 22% for the six months ended 30th June 2005, distribution costs increased by 24%.

Additional administrative costs, including staff salaries, depreciation expenses and other general office expenses were incurred when the number of employees increased to 2,440 and new subsidiaries of the Group were established for the purpose of expanding the Group's operations. Administrative costs increased by 16% from HK\$30 million for the six months ended 30th June 2004 to HK\$35 million for the six months ended 30th June 2005.

Due to the fluctuation of exchange rate of European currency, an amount of approximately HK\$4 million exchange loss was incurred for the six months ended 30th June 2005. These, together with the increase in interest rate and additional loans for the Group's expansion in operations, resulted in an increase of finance costs from HK\$13 million for the six months ended 30th June 2004 to HK\$26 million for the six months ended 30th June 2005.

4. (Loss) profit attributable to shareholders

The Group's loss attributable to shareholders for the six months ended 30th June 2005 was approximately HK\$102 million while the Group's profit attributable to shareholders for the six months ended 30th June 2004 was approximately HK\$27 million. The loss was mainly caused by various factors affecting gross profit explained above.

DIRECTORS' SERVICE CONTRACTS

No Director has any existing or proposed service contract with any member of the Group (excluding contracts expiring or determinable by the employer within one year without payment of compensation other than statutory compensation).

DIRECTORS' INTERESTS IN SECURITIES

As at 30th June 2005, the interests and short positions of the Directors and chief executive in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")), as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.40 of the GEM Listing Rules were as follows:

Associated Corporations

Long positions in shares of FET (Note 1)

Name of director	Number of shares				Total
	Personal interests	Family interests	Corporate interests	Other interests	
Mr. Shu-Tong Hsu	69,757,572	Nil	Nil	Nil	69,757,572
Mr. Jar-Yi Shih	1,897,864	25,501,263	Nil	Nil	27,399,127
Mr. Champion Lee	162,857	Nil	Nil	Nil	162,857
Mr. Chin-Sen Tu	76,855	Nil	Nil	Nil	76,855
Mr. Shaw-Y Wang	280,649	Nil	Nil	Nil	280,649
Mr. Lih-The Chang	22,097	Nil	Nil	Nil	22,097

Note:

1. FET is an associated corporation of the Company as FET is the Company's ultimate holding company. As at 30th June 2005, FET had a 64.2% interest in the Company, comprising (i) a direct interest of 11.4%; (ii) an indirect interest of 46.8% through its controlling shareholding in Yuang Ding Investment Corporation; and (iii) an indirect interest (arising by virtue of FET's status as the discretionary object of a discretionary trust) of 6%.

In aggregate, the above interests represented, as at 30th June 2005, approximately 2.6% of the total issued common shares of FET.

Save as disclosed above, none of the Directors or the chief executive had any interests or short positions in any shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.40 of the GEM Listing Rules.

DIRECTORS' RIGHTS TO PURCHASE SHARES OR DEBENTURES

The Company has a share option scheme approved by the shareholders of the Company on 11th January 2000, under which it may grant options to full-time employees, including executive directors of the Company or of its subsidiaries, to subscribe for shares in the Company.

As at 30th June 2005, no options had been granted under the Company's share option scheme.

SUBSTANTIAL SHAREHOLDERS

As at 30th June 2005, the following persons (other than the Directors and chief executive of the Company) were the substantial shareholders of the Company who had interests and short positions in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO.

Long positions in shares of the Company

Name	Capacity	Number and class of shares	Approximate percentage of interest
FET (<i>Note 1</i>)	Beneficial Owner	263,400,800 ordinary shares	64.2%
Yuang Ding Investment Corporation ("YDIC")	Beneficial Owner	191,870,160 ordinary shares	46.8%
Everest Textile Co. Ltd. ("Everest Textile") (<i>Note 2</i>)	Beneficial Owner	69,750,000 ordinary shares	17.0%
Everest Investment (Holding) Limited ("Everest Investment")	Beneficial Owner	69,750,000 ordinary shares	17.0%

Notes:

1. FET is interested in approximately 99.99% of the issued share capital of YDIC and is accordingly deemed to have an interest in the Company's shares in which YDIC has an interest. FET owns approximately 100% of the issued share capital of Far Eastern Investment (Holdings) Company Limited ("FEIH") and is accordingly taken to be interested in the Company's shares in which FEIH has an interest.
2. Everest Textile is interested in the entire issued share capital of Everest Investment and is accordingly deemed to have an interest in the Company's shares in which Everest Investment is deemed to have an interest.

INTERESTS DISCLOSEABLE UNDER THE SFO

As at 30th June 2005, the following persons (other than the substantial shareholders, the Directors and chief executive of the Company) had interests and short positions in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO.

Long positions in Shares

Name	Capacity	Number and class of shares	Approximate percentage of interest
Far Eastern Investment (Holdings) Company Limited (“FEIH”) <i>(Note 1)</i>	Founder of Trust	24,733,040 ordinary shares	6.0%
Glorious Victory Limited (Note 2)	Beneficial Owner	24,733,040 ordinary shares	6.0%
HSBC International Trustee Limited <i>(Note 3)</i>	Trustee	24,733,040 ordinary shares	6.0%

Notes:

1. FEIH, as the founder of The Kai Yuan Trust, is deemed to have an interest in the shares of the Company held by Glorious Victory Limited, the entire share capital of which is held under The Kai Yuan Trust.
2. Glorious Victory Limited is interested in approximately 6% of the entire issued share capital of the Company. The entire issued share capital of Glorious Victory Limited is in turn held under The Kai Yuan Trust.
3. HSBC International Trustee Limited is the trustee of The Kai Yuan Trust and as such is deemed to be interested in the shares of the Company held by Glorious Victory Limited.

Save as disclosed above, the Company had no notice of any interests required to be recorded in the register required to be kept under Section 336 of the SFO as at 30th June 2005.

COMPETING INTERESTS

FET (*Note 1*) and Everest Textile (*Note 2*), being management shareholders of the Company, are engaged in, and have interests in other companies engaged in, the production and sales of petrochemical, polyester and textile products.

During the six months ended 30th June 2005, FET produced approximately 303,353 tonnes of polyester polymer, 134,984 tonnes of various types of PET chips (for PET bottles, food and industrial packaging), 106,791 tonnes of polyester staple fibers, 58,912 tonnes of pre-oriented yarn (POY), 20,896 tonnes of draw textured yarn (DTY), 164,067 bales of yarn, 10,256 thousand yards of finished fabrics and 189,377 thousand pieces of PET performs. Everest Textile also produced approximately 8,064 tonnes of polyester filaments and 36,781 thousand yards of finished fabrics.

Notes:

1. As at 30th June 2005, Mr. Shu-Tong Hsu, Mr. Jar-Yi Shih, Mr. Champion Lee, Mr. Chin-Sen Tu and Mr. Shaw-Y Wang, who were Directors of the Company, were also directors of FET.
2. As at 30th June 2005, Mr. Shu-Tong Hsu, Mr. Jar-Yi Shih and Mr. Chin-Sen Tu were also directors of Everest Textile.

THE STATEMENT OF CORPORATE GOVERNANCE

Board of Directors

The Board comprises nine Directors, each bringing different facet of expertise or experience to the Company and each with a clearly defined role. In particular, the roles of Chairman and Chief Executive are vested in different people (Mr. Shu-Tong Hsu and Mr. Lih-Teh Chang respectively) with the former concentrating on strategic overview and direction and the latter on the Group's day-to-day operations.

The Company has, from its listing in 2000, always had three independent non-executive directors who have played a significant part in overseeing the Company's affairs, in particular through their consistent attendance and presence on audit committee, as noted further below.

The Board believes that the Company has complied with the code provision set out in the code on Corporate Governance Practices (the "Code") contained in Appendix 15 to the GEM Listing Rule throughout the six months ended 30th June 2005.

Remuneration Committee

The Remuneration Committee (“RC”) was constituted on 10th August 2005 and comprises

Lih-Teh Chang

Shih-Hung CHAN

Ying-Ho WONG, JP

Shaw-Y WANG

Tak-Lung Tsim

A majority of the members of the RC are non-executive and independent directors.

The primary objective of the RC is to ensure formal and transparent procedures for developing remuneration policy, and for overseeing the remuneration packages of Directors and Senior Management.

In reviewing and determining the remuneration package of the executive Directors and senior executives, the RC considered, amongst other things, their responsibilities, skills, expertise and contribution to the Group’s performance and whether the remuneration packages are competitive and sufficient to ensure that the Group is able to attract and retain the best available executive talent.

Internal Control

The Board believes that the system of internal controls maintained by the Company is sufficient to provide reasonable assurances that the Group’s assets are safeguarded against loss from unauthorized use or disposition, transactions are properly authorized and proper accounting records are maintained.

The Company has its internal audit function in place. The functions of the internal audit are to review the effectiveness of the Company’s material internal control and provide assurance that key business and operational risks are identified and managed. The findings and recommendations from internal audit are reported primarily to the audit committee on an annual basis.

Share options and general mandate

The Company has yet to issue any share options. Moreover, it has not, since it was listed, effected any allotment of shares pursuant to the annual general mandate afforded to the Directors. Finally, it has never sought from shareholders a general mandate to repurchase any of its shares.

Audit Committee

The Company has established an audit committee with written terms of reference based upon the guidelines published by the Hong Kong Institute of Certified Public Accountants. The primary duties of the audit committee are to review the Company's annual report and accounts, half-year reports and quarterly reports and to provide advice and comments thereon to the board of Directors. The audit committee is also responsible for reviewing and supervising the Company's financial reporting and internal control procedures. The audit committee comprises three non-executive Directors, namely Mr. Shaw-Y Wang, Mr. Ying-Ho Wong, Kennedy, and Mr. Shih-Hung Chan. The audit committee has met twenty three times since its formation and two time during the six months ended 30th June 2005. The results of the Group for the six months ended 30th June 2005 have been reviewed by the audit committee.

Code of Conduct Regarding Securities Transactions by Directors

During the six months ended 30th June 2005, the Company continued to adopt a code of conduct regarding securities transactions by Directors on terms no less exacting than the required standard of dealings set out in Rules 5.48 to 5.67 of the GEM Listing Rules. The Company has made specific enquiry of all Directors, and the Company is not aware of any non-compliance with the required standard of dealings or otherwise in connection with its code of conduct regarding securities transactions by Directors.

PURCHASE, SALE OR REDEMPTION OF SHARES

Neither the Company nor its subsidiaries has purchased, sold or redeemed any of the Company's shares during the period from 31st January 2000 (date of listing) to 30th June 2005.

By Order of the Board
Far Eastern Polychem Industries Limited
Shu-Tong Hsu
Chairman

Taipei, 10th August 2005

As at the date of this report, Mr. Shi-Tong Hsu, Mr. Jar-Yi Shih, Mr. Champion Lee, Mr. Lih-Teh Chang and Mr. Chin-Sen Tu are Executive Directors of the Company; Mr. Shaw-Y Wang is a Non-executive Directors and Mr. Tak-Lung Tsim, Mr. Ying-Ho Wong and Mr. Shih-Hung Chan are Independent Non-executive Directors.