上海復旦微電子股份有限公司

Shanghai Fudan Microelectronics Company Limited*

FM

(a joint stock limited company incorporated in the People's Republic of China)
(stock code: 8102)

annual report

2005

* for identification only

CHARACTERISTICS OF THE GROWTH ENTERPRISE MARKET ("GEM") OF THE STOCK EXCHANGE OF HONG KONG LIMITED (THE "EXCHANGE")

GEM has been established as a market designed to accommodate companies to which a high investment risk may be attached. In particular, companies may list on GEM with neither a track record of profitability nor any obligation to forecast future profitability. Furthermore, there may be risks arising out of the emerging nature of companies listed on GEM and the business sectors of countries in which the companies operate. Prospective investors should be aware of the potential risks of investing in such companies and should make the decision to invest only after due and careful consideration. The greater risk profile and other characteristics of GEM mean that it is a market more suited to professional and other sophisticated investors.

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Chairman's Statement

The annual results of Shanghai Fudan Microelectronics Company Limited (the "Company") and its subsidiaries (the "Group") for the year ended 31 December 2005 was desirable with turnover of RMB211,211,000, increased by 59% as compared to the previous year; the audited profits attributable to shareholders was RMB8,037,000, increased by 189% as compared to the last year (after excluding an extraordinary gain from the disposal of the Company's interest in an associate), and strengthens the confidence on the future business development of the Group. The turnover and profits continued to record a health growth in 2005, largely due to the Group's intensive works on developing its business. Besides allocation of substantial resources in research and development of new high technological products, the Group also took a series of measures to explore and develop markets, to enhance products quality and cut production costs.

OBJECTIVE

The Group's long term core business is still the IC design. Relying on the "fabless" mode of operation and solid academic support, the Group was enabled to cope with keen competition and rapid market changes in a flexible manner, to achieve its business objectives, to establish a leading position in the industry of IC design and system in the People's Republic of China (the "PRC") and to become one of the major IC card chips production and Application Specific Integrated Circuits ("ASIC") design companies that offers diversified products. Our financial objective is to enhance our shareholders' value by increasing the Group's profit through steady business growth. Our financial objective is to enhance our shareholders' value by increasing the Group's profit.

PROSPECTS

The Directors anticipate the recovery of global IC market in 2006. Attributable to the steady developing economy in China, the domestic market will continue to maintain a good growth. Considering the rapid development of IC design industry, fast replacement of electronics products and strong market demand, the Group foresees a great business opportunity. In accordance with products competition and future market trend, the Group would adjust its market strategy on the project development and direction of marketing. Besides concentrating on the research and development of self-developed products and application functions in different areas, the Group would also exploit markets with large projects and actively participate in government projects.

The Group has released IC circuits for the applications of multimedia interface on mobile phones to the market with satisfactory result. In addition to the stable sales of the existing contactless IC card chips and other segment products, the Group expects further development of the business and steady growth of the profit in the coming year.

APPRECIATION

On behalf of the board of directors (the "Board"), I would like to thank our shareholders and business associates for their unfailing supports. Our independent non-executive director Mr. Xu Juyan will retire and will be leaving the Board soon and I thank him for his services rendered to the Company during the past years. I would like to take this opportunity to thank my fellow directors and all the Group's staff for their hard workings and dedication.

Jiang Guoxing
Chairman

Shanghai, the People's Republic of China
21 March 2006

Management Discussion and Analysis

BUSINESS REVIEW

In the year under review, the global demands for ASIC and IC chips slow down, however, the domestic market in the PRC kept growing as a result of the country's steady economy development. The Group benefited from the continuous growth of the PRC market and together with the new released advance technology products that were well accepted by the market, the turnover was therefore recorded with an increase of 59% as compared to the previous year. Although the turnover was higher, the overall gross profit rate was dropped from 35.7% in the previous year to 25.5%. Part of the reasons was due to the price adjustment on the Group's high-weighted product of contactless IC card chips to keep its market share.

An analysis of the performance of the Group's various business segments during the year is as follows:

IC Card

IC card products were still our core business. Though its segment sales were the highest of the Group and accounted for approximately half of the Group's total turnover, however, its sales weighting began to drop due to the Group's implementation of product diversification. As explained above, the gross profit rate of overall products dropped accordingly but still kept within a reasonable level. The Group's self-developed circuits of contactless IC card products have been released to Shanghai railways transport project and broadly used in other aspects and remains as the Group's main source of sales and profit contribution.

Power Electronics

In the market of power electronics products, the Group's main products were own-developed earth leakage current detector circuit and multi-fee power control meters. However, such products have been launched in the market for quite a while and the sales began to slow down. The turnover and gross profit rate for these products were slightly decreased during the year.

Motor and Mobile Electronics

Motor and mobile electronic products were not major developing projects, in addition to the fierce market competition, the Group has reduced its investment in this aspect and products were a few. The turnover and gross margin were decreased as compared to the previous year.

Telecommunication Electronics

In view of market saturation and keen market competition, the Group has limited its resources in this business. There was considerable increase in the turnover; however, the contribution to the profits was insignificant due to very few types of products released in the market.

Consumer Electronics

With leading technology and design, the multimedia processors chips that are applicable to terminals like mobile phone etc. were released in the third quarter of the year and were enthusiastically accepted by the market, in addition, new products commonly generate comparatively high profit, contributed the Group with significant turnover and earnings. At the end of year, the electronic label has been launched into market and promoted to other applicable areas. The turnover of this segment has been significantly increased almost 10 times as compared to the previous year and the gross profit rate also increased accordingly.

IC Testing

The IC testing business was operated by the Company's subsidiary, Sino IC Technology Co., Ltd. ("Sino IC") and being well performed. Sales of the company have increased by 10% during the year with long term contribution made to the Group.

FINANCE REVIEW

For the year ended 31 December 2005, the Group recorded a turnover of approximately RMB211,211,000 (2004: RMB132,710,000), an increase of approximately 59% as compared to the previous year. The audited profit attributable to shareholders was approximately RMB8,037,000 and increased by 189% as compared to the previous year RMB2,780,00 (after excluding an extraordinary gain from the disposal of the Company's interest in an associate). The basic earnings per share was RMB1.29 cents (2004: RMB1.16 cents).

The increase in the turnover was attributable to the ideal sales performance of newly released self-developed consumer electronic IC chips. Overall gross profit rate has dropped down from 35.7% in the last year to 25.5%. Other than the aforesaid price adjustment to maintain market share, the provision for inventories amounted to RMB3,740,000 and slightly increase in production cost also have an adverse impact on the gross profit rate.

There was slightly increase in other revenue and gains. During the year, there were royalty fee income of RMB2,044,000 (2004: nil); rental income of RMB404,000 (2004: nil); deed tax refund amounted to RMB421,000 (2004: nil); subsidy income and sundry income increased by RMB994,000 and RMB719,000 respectively, which can be compared with the extraordinary gain of RMB4,459,000 on disposal of interest in an associate in last year.

Despite the increase in turnover, the selling and distribution costs ascended slightly due to the effective control. Administrative expenses increased by 20%, of which largely attributable to the rise of salaries and allowances resulting from fierce human resource competition. Other administrative expenses were maintained to a low level with efficient cost control. Other operating expenses were similar to the previous year, the research and development costs were reduced because of subsidies of RMB3,233,000 were granted by relevant government authorities; and there was a loss on deemed disposal of equity interest in Sino IC amounted to RMB2,583,000 as a result of the adoption of human resource capital contribution plan implemented by the relevant authority of Shanghai Pu Dong District; whereas, the provision for bad and doubtful debt increased by RMB159,000 only and thanks for the strong credit risk management.

Management Discussion and Analysis

MATERIAL ACQUISITION AND DISPOSALS OF SUBSIDIARIES

During the year under review, other than the change in equity interest of Sino IC set out in the section headed "Finance review" above, there was no material change in the subsidiaries of the Group.

FUTURE PLANS FOR MATERIAL INVESTMENTS

The Company will actively keep on looking for strategic cooperative partners and has no material investment plan at the moment.

TECHNOLOGICAL COOPERATION

The Group still co-operated the IC Engineering Technology Centre and the ASIC System Laboratory jointly with the Shanghai Fudan University and the University of Science & Technology of China respectively, and has enjoyed their advanced technological supports through out the year.

FINANCIAL RESOURCES AND LIQUIDITY

As at 31 December 2005, net assets of the Group amounted to approximately RMB234,552,000 (2004: RMB226,765,000); current assets amounted to approximately RMB259,760,000 (2004: RMB189,141,000), of which approximately RMB136,633,000 (2004: RMB110,672,000) were cash and bank deposits.

The Group's financial resources are internally generated to meet its operation needs. The Group's liquidity is in a healthy status and is able to meet its ordinary course of business and future development.

As at 31 December 2005, except a deposit of RMB1,639,000 (2004: RMB772,000) pledged as security for letters of credit and project tender issued by the Company, the Group has not pledged its assets to any third parties (2004: nil).

CAPITAL STRUCTURE

During the year, there was no change in the capital structure of the Company. The capital of the Company comprises of ordinary shares.

GEARING RATIO

As at 31 December 2005, the Group's current liabilities amounted to approximately RMB89,234,000 (2004: RMB35,545,000) and non-current liabilities of approximately RMB3,615,000 (2004: RMB5,615,000). The net assets value per share of the Group was approximately RMB0.38 (2004: RMB0.36). The Group's ratio of current liabilities over current assets was approximately 34.4% (2004: 18.8%) and the gearing ratio was approximately 39.6% (2004: 18.2%) on the basis of total liabilities over net assets. As at 31 December 2005, the Group had no bank or other borrowings (2004: nil).

INTEREST AND FOREIGN EXCHANGE RISK

The Group has transactional currency exposures. Such exposures arise from sales or purchases by operating units in currencies other than the units' functional currency. Approximately 38% (2004: 16%) of the Group's sales are denominated in currencies other than the functional currency of the operating units making the sale, whilst almost 60% (2004: 87%) of costs are denominated in the unit's functional currency. It is the Group's policy not to enter into forward contracts until a firm commitment is in place.

The Group has maintained a conservative policy on management of interest and foreign exchange risk. In order to minimize the risk of interest and foreign exchange, most of the Group's deposits are in local currency with different fixed periods and rates to cover the cash flows of its business operations and fluctuation in interest rates. During the reporting period, the fluctuations in foreign exchange have no material effect on the Group's operations and cash flows.

CREDIT RISK

The Group's sales are made to several major customers and there is concentration of credit risks. The Group seeks to maintain strict control over its outstanding receivables and closely monitor the collection to minimise credit risk.

CAPITAL COMMITMENTS

As at 31 December 2005, the Group had capital commitments amounted to approximately RMB170,000 (2004: RMB590,000). The capital commitments relate primarily to acquisitions of land and buildings and plant and equipment.

CONTINGENT LIABILITIES

As at 31 December 2005, the Group had no contingent liabilities (2004: nil).

USE OF CAPITAL AND FUNDING

The Group currently has a stable financial position and sufficient working capital which will be applied for research and development of new products and identifying of cooperative partners as appropriate.

STAFF

As at 31 December 2005, the Group employed approximately 314 (2004: 279) staff. The salary levels of employees are determined by their performance, qualifications, experience and contribution to the Group with reference to general market trend. In accordance with the Company Law of the PRC and the Group's articles of association, the Group will allocate its reserves to the statutory public welfare fund as staff welfare.

The total staff costs of the Group charged to the income statement for the year ended 31 December 2005 amounted to approximately RMB21,737,000 (2004: RMB18,900,000).

Corporate Information

BOARD OF DIRECTORS

Executive Directors

Mr. Jiang Guoxing *(Chairman)*
Mr. Shi Lei *(Managing Director)*
Mr. Yu Jun *(Deputy Managing Director)*
Ms. Cheng Junxia
Mr. Wang Su

Non-executive Directors

Mr. Cheng Xiaohong
Ms. Zhang Qianling
Mr. He Lixing
Mr. Shen Xiaozu

Independent Non-executive Directors

Mr. Leung Tin Pui
Mr. Xu Juyan
Mr. Cheung Wing Keung *FCCA, CPA*

COMPANY SECRETARY

Mr. Li Wing Sum, Steven *FCCA, FCPA, FTIHK*

QUALIFIED ACCOUNTANT

Mr. Li Wing Sum, Steven *FCCA, FCPA, FTIHK*

COMPLIANCE OFFICER

Mr. Wang Su

AUTHORISE REPRESENTATIVES

Mr. Shi Lei
Mr. Wang Su

AUDIT COMMITTEE

Mr. Leung Tin Pui *(Chairman)*
Mr. Xu Juyan
Mr. Cheung Wing Keung

SUPERVISORS' COMMITTEE

Mr. Li Wei
Mr. Ding Shengbiao
Mr. Xu Lenian

REMUNERATION COMMITTEE

Mr. Leung Tin Pui *(Chairman)*
Mr. Cheung Wing Keung

NOMINATION COMMITTEE

Mr. Leung Tin Pui *(Chairman)*
Mr. Cheung Wing Keung

AUDITORS

Ernst & Young
Certified Public Accountants

REGISTERED OFFICE

No. 220, Handan Road
Shanghai
People's Republic of China

PLACE OF BUSINESS IN HONG KONG

Flat 12, 7/F., East Ocean Centre
98 Granville Road, Tsimshatsui East
Kowloon

SHARE REGISTRAR AND TRANSFER OFFICE

Tengis Limited
26th Floor, Tesbury Centre
28 Queen's Road East
Wanchai, Hong Kong

PRINCIPAL BANKERS

Shanghai Pudong Development Bank
Shanghai branch

Industrial and Commercial Bank of China
Shanghai branch

STOCK CODE

8102

Directors and Senior Management Biographies

Biographical details of the directors and the senior management of the Company are set out below:

DIRECTORS

Executive directors

Mr. Jiang Guoxing, aged 52, is the Chairman of the Company. He is primarily responsible for leadership of the Board, the Group's strategic planning and its corporate governance. Mr. Jiang is a professor grade senior engineer and graduated with a degree in computer science from Shanghai Fudan University (Fudan University). Mr. Jiang joined the Company at the time of its establishment in July 1998. He is the managing director of Fudan Enterprise Development Company Limited and Fudan Venture Capital Limited, chairman of Fudan Water Works Technology Limited and Fudan Technology Zone (UK) Limited, companies invested by Fudan University. He is also the non-executive director of Shanghai Fudan-Zhangjiang Bio-Pharmaceutical Co., Ltd., a company listed on the GEM.

Mr. Shi Lei, aged 39, is the Managing Director of the Company and is responsible for the management of corporate strategy, business development and daily operations. He is an economist and graduated with a bachelor degree in management from China University of Technology and a Master's degree in management from Fudan University. Mr. Shi joined the Company at the time of its establishment in July 1998. Prior to that, Mr. Shi was the deputy manager in the Development Division of Shanghai Agricultural Investments Company and the general manager of Pacific Business Trust Company.

Mr. Yu Jun, aged 38, is the Deputy Managing Director of the Company. He has a Master's degree and is a senior engineer. Mr. Yu is the deputy director of the Research Institute for Integrated Circuit Designs of Fudan University, and has extensive knowledge and experience in the design of integrated circuits and systems. He was previously the chief engineer of Fudan High Tech. He joined the Company in July 1998.

Ms. Cheng Junxia, aged 59, is the Chief Engineer of the Company. She is a professor at Fudan University and has extensive knowledge and experience in the design and manufacture of integrated circuits. She was previously the general manager of Fudan High Tech and the director of the Research Institute for Integrated Circuit Designs of Fudan University. She joined the Company in July 1998.

Mr. Wang Su, aged 52, is the Financial Controller of the Company. He is an accountant. He was previously a fund manager as well as the deputy manager of the Finance Department of Shanghai Commerce and Invest (Group) Corporation and the financial controller of Shanghai Pacific Commercial Trust Company Limited. He joined the company in July 1998.

Directors and Senior Management Biographies

Non-executive directors

Mr. Chen Xiaohong, aged 48, is a senior economist and has a Master's degree in economics. He was previously the deputy director of the Corporate Finance Department of the Finance Bureau of Shanghai, the director of the Finance Department of the Finance and Trade Office of the Shanghai Municipal Government, the chief economist of the Shanghai Commerce Committee, the assistant inspector of the Shanghai Economic and Trade Committee. He is the chairman of Shanghai Commerce and Invest (Group) Corporation and managing director of Shanghai AJ Corporation, a company listed on the Shanghai Stock Exchange. He joined the Company in July 1998.

Ms. Zhang Qianling, aged 69, is a principal professor and tutor to doctorate students at Fudan University. She is a distinguished academic on the study of integrated circuits and a promoter and first director of the Special National Laboratories Center for Integrated Circuits and Systems of Fudan University. She joined the Company in July 1998.

Mr. He Lixing, aged 71, is a senior economist. He was previously the chief economist of Shanghai Commerce and Investment (Group) Corporation and director of the Finance Department of the Finance and Trade Office of the Shanghai Municipal Government. He joined the Company in July 1998.

Mr. Shen Xiaozu, aged 56, was previously the assistant to the general manager of Shanghai Commerce and Invest (Group) Corporation, the deputy general manager Shanghai Xinlian Real Estate Company, the deputy general manager of Shanghai General Electric Machinery Corporation and the headmaster of Shanghai Mechanical Engineering Industrial College. He is a senior economist and joined the Company in July 1998.

Independent non-executive directors

Mr. Leung Tin Pui, aged 60, he was appointed on 19 July 2000. Mr. Leung has been appointed Vice-president of The Hong Kong Polytechnic University since January 1995. He was previously the Head and Professor of Department of Mechanical Engineering and Dean of Engineering of The Hong Kong Polytechnic University. Professor Leung is keen on public services, he was the President of the Hong Kong Institution of Engineers and the Hong Kong Association for the Advancement of Science and Technology. Mr. Leung is also a member of several advisory boards of the Government of the Hong Kong Special Administrative Region. Professor Leung was awarded by the Hong Kong Government Justice of Peace and awarded the Bronze Bauhinia Star.

Mr. Xu Juyan, aged 71, he was appointed on 12 June 2002 and holds two bachelor degrees. He is the researcher of the Wuxi Microelectronics Research Institute under the Ministry of Information Industry and a doctorate supervisor for Southeast University. He was elected as a fellow member of the PRC Engineering Institute. He was previously the advisor to the Electronics Development Leadership Group of the State Council; members of the executive committee of Electronics Engineering Department and Association of Electronics of the PRC°Fthe researcher at 13th Research Institute of the 3rd Engineering Division, and director and chief engineer of the 24th Research Institute of the 4th Engineering Division. He is also the advisor of several semi-conductor and electronics associations.

Directors and Senior Management Biographies

Mr. Cheung Wing Keung, aged 40, he is a fellow member of the Association Chartered Certified Accountants and an associate member of the Hong Kong Institute of Certified Public Accountants. He has over 20 years' working experience in auditing, accounting, corporate management and consultancy. He has worked in accounting firms and the Hong Kong Inland Revenue Department and has held senior positions in certain Hong Kong's private group companies.

SUPERVISORS

Mr. Li Wei, aged 34, is the Technical Officer of the Company. He has a Master's degree. Mr. Li specializes in integrated circuit design, and has conducted in-depth research on the coding and integrated protocol bases. He joined the Company in July 1998.

Mr. Ding Shengbiao, aged 43, is the Chief Economist of the Company. He has a bachelor degree and is an economist. He was previously the manager of the Loans Department of the Shanghai Interbank Loan Centre of the People's Bank of China, and the division head of the Planning Department of the People's Bank of China, Shanghai Branch. He joined the Company in July 1998.

Mr. Xu Lenian, aged 54, is the chairman of Shanghai Pacific Business Trust Company, and the assistant to the general management of Shanghai Commerce and Invest (Group) Corporation. He has post-secondary qualification and is a senior economist. He was the head of the International Affairs Department and General Affairs Department of China Agricultural Bank Pudong branch. He Joined the Company in July 1998.

SENIOR MANAGEMENT

Mr. Li Wei, (see personal details set out in the paragraph headed "Supervisors" above).

Mr. Ding Shengbiao, (see personal details set out in the paragraph headed "Supervisors" above).

Mr. Ma Fubin, aged 38, is the Operation Officer of the Company. He joined the Company in October 1999 and holds a Master's degree in business administration and is a certified public accountant of the PRC. Before joining the Company, he has worked in Zhejiang Province Village Development Investment Group Limited as assistant to investment manager.

Ms. Ji Lanhua, aged 55, is the Production Officer of the Company, and has a bachelor degree. She was engaged in the design and development of the Company's motorcycle ignition controller circuits and telephone transmission circuits. Ms. Ji is very experienced in the design and sales of integrated circuits. She was previously the sales manager of Fudan High Tech. She joined the Company in July 1998.

Mr. Li Wing Sum Steven, aged 49, the Qualified Accountant and Company Secretary of the Company. He has over 25 years' experience in auditing, accounting, taxation and financial management. He has worked in an international accounting firm and been employed as group financial controller of a listed company in Hong Kong and a multi-national organization. He is a fellow member respectively of the Association of Chartered Certified Accountants, the Hong Kong Institute of Certified Public Accountants and the Taxation Institute of Hong Kong. He joined the Company in July 2000. He is also the executive director of a company listed on the main board of the Stock Exchange.

Corporation Governance Report

The Company has implemented its own code of corporate governance practices by adopting the code provisions set out in the Code on Corporate Governance Practices (the "CCGP") contained in Appendix 15 of the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "GEM Listing Rules"), which became effective on 1 January 2005. In the opinion of the directors, the Company has met the code provisions set out in the CCGP contained in Appendix 15 of the GEM Listing Rules.

DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted a code of conduct regarding Directors' securities transactions on terms no less exacting than the required standard of dealings as set out in Rules 5.48 to 5.67 of the GEM Listing Rules. Having made specific enquiry to all Directors, the Directors have complied with such code of conduct and the required standard of dealings and its code of conduct regarding securities transactions by the Directors throughout the year ended 31 December 2005.

BOARD OF DIRECTORS AND BOARD MEETING

Board of Directors

The Board comprises five executive Directors, four non-executive directors and three independent non-executive directors. The Board members have no financial, business, family or other material/relevant relationships with each other. The Board's composition is formed to be well balanced to ensure strong independence exists across the Board. The biographies of the Directors are set out on pages 10 to 12, with details of diversity of skills, expertise, experience and qualifications concerning the Directors.

The Board is responsible for the leadership and management of the Group's businesses as well as its strategic planning and performances. The Management was delegated the authority and responsibility by the Board for the management of the Group. In addition, the Board has also delegated various responsibilities to the Board Committees. Details of these committees are set out in this report.

The Company has received annual confirmations of independence from the three independent non-executive directors in accordance with Rule 5.09 of the GEM Listing Rules and considers them to be independent.

Board Meeting

The board of Directors held four full board meetings in each year and meets as and when required. During the financial year ended 31 December 2005, the attendances of the directors at the board meetings are as follows:

Directors	**Number of attendance**
Mr. Jiang Guoxing	4/4
Mr. Shi Lei	4/4
Mr. Yu Jun	4/4
Ms. Cheng Junxia	4/4
Mr. Wang Su	4/4
Mr. Cheng Xiaohong	0/4
Ms. Zhang Qianling	4/4
Mr. He Lixing	4/4
Mr. Shen Xiaozu	4/4
Mr. Leung Tin Pui	3/4
Mr. Xu Juyan	0/4
Mr. Cheung Wing Keung	4/4
Mr. Tsai Kao Chung (resigned on 31 March 2005)	0/1
Mr. David Yung (resigned on 31 March 2005)	0/1

The Directors will receive details of agenda items for decision and minutes of committee meetings in advance of each board meeting.

Board Minutes are kept by the Company Secretary of the Company and are sent to the Directors for records and are open for inspection by the Directors.

Chairman and Managing Director

The Company has, since the early stage of its incorporation in 1998, segregated the duties of the chairman of the Board and managing director. The Chairman of the Board and the Managing Director are separately held by Mr. Jiang Guoxing and Mr. Shi Lei in order to preserve independence and have a balanced judgement of views. The Chairman of the Board has the responsibilities to lead the Board and make sure it works effectively and discharges its responsibilities and that all key and appropriate issues are discussed by the Board in a timely manner. The Managing Director has the responsibilities to manage and execute the Group's business directions and operation decisions. In addition, the Board also comprises of independent non-executive directors who can provide the Board with independent judgements, knowledge and experience.

Corporation Governance Report

Non-Executive Directors

The four non-executive directors have entered into service contracts with the Company with effect from 19 July 2003 for a term of 3 years and shall continue thereafter unless and until terminated in accordance with the terms of her service contract or by either party giving to the other not less than 3 calendar months' prior notice in writing.

The three independent non-executive directors have entered into service contracts with the Company with effect from 27 May 2005 and expire at the forthcoming annual general meeting.

In accordance with article 87 of the Company's articles of association, all the seven non-executive directors shall retire and being eligible, other than the independent non-executive director Mr. Xu Juyan who will not offer himself for re-election due to personal reasons, offer themselves for re-election at the forthcoming annual general meeting of the Company.

Remuneration of Directors

The Company has set up a remuneration committee in December 2004 and the members of which are the independent non-executive directors Mr. Leung Tin Pui and Mr. Cheung Wing Keung.

The roles and functions of the remuneration committee included the determination of the remuneration packages of all executive directors, including their benefits in kind, pension rights and compensation payments, any compensation payable for loss or termination of their office or appointment, and make recommendations to the Board for the remuneration of non-executive directors. The remuneration committee also considers factors such as salaries of comparable companies, time commitment and responsibilities of the directors, employment conditions within the Group and performance.

During the period under review, a meeting of the remuneration committee was held in May 2005 and details of the attendance are as follows:

Directors	Number of attendance
Mr. Leung Tin Pui	1/1
Mr. Cheung Wing Keung	1/1

The remuneration committee of the Company has considered and reviewed the existing terms of employment contracts of the executive Directors and considers that the existing terms of employment contracts of the executive Directors are fair and reasonable.

Nomination of Directors

Before the effective of the new CCGP, all the Company's directors were appointed for a specific term and subject to article 87 of the Company's articles of association, executive directors and non-executive directors are subject to rotation and re-election for every 3 years. In addition, independent non-executive directors have entered into service contracts and subject to retirement on every annual general meeting. In view of the new CCGP, a special resolution to amend the Company's articles of association will be proposed in the forthcoming annual general meeting of the Company to be held on 19 May 2006 that directors shall be elected at the shareholders' general meeting each for a term of not more than 3 years and one-third of the directors shall retire from office at the annual general meeting. Every director (including directors with fixed terms of appointment) shall be subject to retirement by rotation at least once every 3 years; and that any director appointed as an addition or to fill a casual vacancy on the Board shall be subject to re-election by shareholders at the first general meeting after his appointment.

The Company has established a nomination committee in May 2005 and the members of the nomination committee are the independent non-executive directors Mr. Leung Tin Pui and Mr. Cheung Wing Keung. The main roles and functions of the nomination committee included the appointment and removal of directors, reviews the past performance, qualification, general market conditions and the Company's articles of association in selecting and recommending candidates for directorship. The Committee also identifies suitable candidates who can add value to the management through their contributions in the relevant strategic business areas and which appointments will result on the constitution of strong and diverse Board.

The Nomination Committee has not hold any meeting during the year under review.

Auditors' Remuneration

The audit committee of the Company is responsible for considering the appointment of the external auditors and reviewing any non-audit functions performed by the external auditors, including whether such non-audit functions could lead to any potential material adverse effect on the Company. During the year under review, except the statutory audit fee, the Group has not paid fees to the external auditors for any other non-audit services.

Audit Committee

The audit committee comprises three independent non-executive directors, Mr. Leung Tin Pui (Chairman), Mr. Xu Juyan and Mr. Cheung Wing Keung. All of them are well experienced in management, IC and electronic industries and the accounting profession.

Corporation Governance Report

The audit committee held 4 meetings during the year under review and details of its attendance are as follows:

Directors	Number of attendance
Mr. Leung Tin Pui	4/4
Mr. Xu Juyan	4/4
Mr. Cheung Wing Keung	4/4
Mr. David Yung (resigned on 31 March 2005)	0/1

Full minutes of audit committee meetings are kept by the Company Secretary. Draft and final versions of minutes of the audit committee meetings were sent to all members of the committee for their comments and records respectively within a reasonable time after the meeting.

The Audit Committee meets the external auditors at least once a year to discuss issues concerning the audits. The Audit Committee reviews the quarterly results, interim and annual reports before submission to the Board. The Committee focuses not only on the impact of the changes in accounting policies and practices but also on the compliance with accounting standards, the GEM Listing Rules and the legal requirements in the review of the Group's quarterly results, interim and annual reports.

Internal Control

The Company and its subsidiaries have to conduct a review of its system of internal control once a year to ensure the effective and adequate internal control system including finance, operations and risk management. The reports and findings prepared by the internal audit team have to be circulated to the relevant committee delegated by the Board. If necessary, the internal audit team will submit their findings and the proposed audit plan to the Audit Committee for its approval. A review of system of internal control has been undergone by the end of 2005 and will be completed in due course.

Shareholders' Relations

The Company has made announcements of all its annual, interim and quarterly reports in time in accordance with the GEM Listing Rules. In addition to the post of spokesman established to liaise with shareholders, the Company also provides the most updated information on its website to maintain a different communicate channel with its shareholders. Besides, all executive directors have presented in the annual general meeting of the Company to communicate and answer to the questions raised by shareholders and significant issues were put as separate proposed resolutions.

Voting By Poll

The Company informs the shareholders (in its circulars convening a general meeting) the procedures for voting by poll and the rights of shareholders to demand a poll to ensure compliance with the requirements on the poll voting procedures.

NOTICE IS HEREBY GIVEN that the annual general meeting (the "AGM") of Shanghai Fudan Microelectronics Company Limited (the "Company") will be held at Building 4, Lane 127, Guotai Road, Shanghai, the People's Republic of China (the "PRC") on 19 May 2006 at 10:00 a.m. for the following purposes:–

1. To receive and consider the audited consolidated financial statements and the Reports of the Directors and the Auditors for the year ended 31 December 2005;

2. To re-elect directors and to authorise the board of directors ("Board") to fix their remuneration;

3. To appoint an independent non-executive director;

4. To appoint auditors and to authorise the Board to fix their remuneration;

To consider, if thought fit, pass with or without amendments, the following resolutions:

SPECIAL RESOLUTIONS

5. **"THAT:**

(a) subject to paragraphs (c), (d) and (e) below, the exercise by the Board during the Relevant Period (as defined in paragraph (f) below) of all the powers of the Company separately or concurrently to allot, issue and deal with the domestic invested shares of RMB0.10 each in the share capital of the Company ("Domestic Shares") and/or the foreign invested shares of RMB0.10 each in the share capital of the Company ("H Shares") be and is hereby approved;

(b) the approval in paragraph (a) above shall authorise the Board to make an offer or agreement or grant an option during the Relevant Period which would or might require Domestic Shares and/or H Shares to be allotted and issued either during or after the end of the Relevant Period;

(c) the aggregate nominal value of Domestic Shares to be allotted and issued or agreed to be allotted and issued (whether pursuant to an option or otherwise) by the Board pursuant to the approval in paragraphs (a) and (b) above, otherwise than pursuant to (i) a rights issue (as defined in paragraph (f) below); (ii) the exercise of the conversion rights under the terms of any securities which are convertible into such shares; (iii) the exercise of rights of subscription under the terms of any warrants issued by the Company; or (iv) any scrip dividend or similar arrangement providing for the allotment of such shares in lieu of the whole or part of a dividend on such shares in accordance with the articles of association of the Company, shall not exceed 20% of the aggregate nominal value of the Domestic Shares then in issue at the date of the passing of this resolution;

(d) the aggregate nominal value of H Shares to be allotted and issued or agreed to be allotted and issued (whether pursuant to an option or otherwise) by the Board pursuant to the approval in paragraphs (a) and (b) above, otherwise than pursuant to (i) a rights issue (as defined in paragraph (f) below); (ii) the exercise of the conversion rights under the terms of any securities which are convertible into such shares; (iii) the exercise of rights of subscription under the terms of any warrants issued by the Company; or (iv) any scrip dividend or similar arrangement providing for the allotment of such shares in lieu of the whole or part of a dividend on such shares in accordance with the articles of association of the Company, shall not exceed 20% of the aggregate nominal value of the H Shares then in issue at the date of the passing of this resolution;

(e) the approval in paragraph (a) above shall be conditional upon the approval of the China Securities Regulatory Commission (or their respective successor authorities) being obtained by the Company;

(f) for the purpose of this resolution:

"**Relevant Period**" means the period from the passing of this resolution until whichever is the earlier of:

(i) the conclusion of the next annual general meeting of the Company following the passing of this resolution;

(ii) the expiration of a period of twelve months following the passing of this resolution; or

(iii) the date on which the authority set out in this special resolution is revoked or varied by a special resolution of the members of the Company in general meeting.

"**rights issue**" means an offer of shares open for a period fixed by the directors of the Company to holders of shares of the Company on the register of members of the Company on a fixed record date and, where appropriate, the holders of the other equity securities of the Company entitled to be offered therein, in proportion to their then holdings of such shares or other equity securities (subject to such exclusions or other arrangements as the directors of the Company may deem necessary or expedient in relation to fractional entitlements or having regard to any restrictions or obligations under the laws of any relevant jurisdiction, or the requirements of any regulatory body or any stock exchange); and

(g) the Board be and is hereby authorised to make such amendments to articles 15, 16 and 19 of the articles of association of the Company as it thinks fit so as to increase the registered share capital and to reflect the new capital structure of the Company as a result of the allotment and issuance of shares of the Company pursuant to the approval granted under paragraph (a) above."

6. **"THAT:**

(a) subject to the paragraphs (b) and (c) below, the Relevant Period (as defined in paragraph 5(f) above) during which the board of directors may exercise all the powers of the Company to repurchase H Shares in issue of the Company on the Stock Exchange, subject to and in accordance with all applicable laws, rules and regulations and/or requirements of the governmental or regulatory body of securities in the PRC, the Stock Exchange or of any other governmental or regulatory body he and is hereby approved;

(b) the aggregate nominal value of H Shares authorised to be repurchased pursuant to the approval in paragraph (a) above during the Relevant Period shall not exceed 10 percent of the aggregate nominal value of H Shares in issue of the Company as at the date of the passing of this resolution;

(c) the approval in paragraph (a) above shall be conditional upon:

(i) the passing of a special resolution in the same terms as the resolution set out in this paragraph (except for this sub-paragraph (c)(i)) at the extraordinary general meeting for holders of H Shares of the Company ("H Shareholders' EGM") and the extraordinary general meeting for holders of domestic shares of the Company ("Domestic Shareholders' EGM") both to be held on 19 May 2006 (or on such adjourned date as may be applicable);

(ii) the approval of the China Securities Regulatory Commission and any other regulatory authorities (or their respective successor authorities) as may be required by laws, rules and regulations of the PRC being obtained by the Company if appropriate; and

(iii) the Company not being required by any of its creditors to repay or to provide guarantee in respect of any amount due to any of them (or if the Company is so required by any of its creditors, the Company having, in its absolute discretion, repaid or provided guarantee in respect of such amount) pursuant to the notification procedure set out in Article 23 of the Articles of the Company.

(d) subject to approval of all relevant governmental authorities in the PRC for the repurchase of such H Shares being granted, the Board be hereby authorised to:

(i) make such amendments to the Articles of the Company accordingly as it thinks fit so as to reduce the registered share capital of the Company and to reflect the new capital structure of the Company upon the repurchase of H Shares of the Company as contemplated in paragraph (a) above; and

(ii) file the amended Articles of the Company with the relevant governmental authorities of the PRC."

7. **"THAT:**

conditional upon special resolutions numbered 5 and 6 above and the special resolutions numbered 1 and 2 as set out in the notices of H Shareholders' EGM and Domestic Shareholders' EGM respectively, being passed, the aggregate nominal amount of H Shares of the Company which are repurchased by the Company under the authority granted to the directors of the Company as mentioned in special resolution numbered 6 above shall be added to the aggregate nominal amount of share capital that may be allotted or agreed conditionally or unconditionally to be allotted by the directors of the Company pursuant to special resolution numbered 5 above."

8. **"THAT:**

Article 87 of the Company's articles of association be amended as follows:

(i) The first paragraph be amended and entirely replaced with the following:

"Directors shall be elected at the shareholders' general meeting each for a term of not more than 3 years. One-third of the directors for the time being, or, if their number is not three or a multiple of three, then the number nearest to, but not less than, one-third, shall retire from office at the annual general meeting. Every director (including directors with fixed terms of appointment) shall be subject to retirement by rotation at least once every 3 years"; and

(ii) By adding the following:

"The Board shall have power from time to time and at any time to appoint any person as a director either to fill a casual vacancy or as an addition to the Board but so that the maximum number of directors so appointed shall not exceed the number determined from time to time by the members in general meeting. Any director so appointed shall be subject to election by shareholders at the first general meeting after his appointment."

By order of the Board
Jiang Guoxing
Chairman

Shanghai, the PRC, 21 March 2006

Notice of Annual General Meeting

Registered Office:
No. 220 Handan Road
Shanghai
The People's Republic of China

Principal place of business in Hong Kong:
Flat 12, 7/F., East Ocean Centre
98 Granville Road
Tsimshatsui East
Kowloon
Hong Kong

Notes:

1. Persons who hold shares of the Company and whose names appear on the Register of Members of the Company as at 19 April 2006 shall be entitled to attend the AGM. Further details are set out in the confirmation slip and explanation thereto.

2. Any member entitled to attend and vote at the AGM is entitled to appoint one or more person(s) as his proxy to attend and vote instead of him. A proxy need not be a member of the Company.

3. To be valid, a form of proxy, together with the power of attorney or other authority, if any, under which it is signed, or a certified copy of that power of attorney, must be deposited not less than 24 hours before the time appointed for the holding of the AGM at the Company's registered office or the Company's principal place of business in Hong Kong as stipulated in the proxy form.

4. The Register of Members of the Company will be closed from 19 April 2006 to 18 May 2006 (both dates inclusive) during which period no transfer of shares will be registered.

5. Completion and delivery of the form of proxy will not preclude a member from attending and voting in person at the AGM if the member so desires, and in such event, the instrument appointing a proxy shall be deemed to be revoked.

6. An explanatory statement containing further details regarding the proposed Resolutions nos. 2, 3, 5 to 8 set out in the above notice as required by the Rules Governing the Listing of Securities on GEM will be dispatched to shareholders together with the 2005 Annual Report of the Company.

Report of the Directors

The directors herein present their report and the audited financial statements of Shanghai Fudan Microelectronics Company Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") for the year ended 31 December 2005.

PRINCIPAL ACTIVITIES

The Company's principal activities consist of designing, developing and selling products of application-specific integrated circuits. Details of the principal activities of the Company's subsidiaries are set out in note 15 to the financial statements. There were no significant changes in the nature of the Group's principal activities during the year.

RESULTS AND DIVIDENDS

The Group's profit for the year ended 31 December 2005 and the state of affairs of the Company and the Group at that date are set out in the financial statements on pages 34 to 87.

The directors do not recommend the payment of a dividend in respect of the year.

SUMMARY FINANCIAL INFORMATION

A summary of the published results and assets, liabilities and minority interests of the Group for the last five financial years, as extracted from the audited financial statements, is set out on page 88. This summary does not form part of the audited financial statements.

PROPERTY, PLANT AND EQUIPMENT

Details of movements in the property, plant and equipment of the Company and the Group during the year are set out in note 12 to the financial statements.

SHARE CAPITAL

There were no movements in either the Company's authorised or issued share capital during the year.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's articles of association or the laws of the People's Republic of China (the "PRC") which would oblige the Company to offer new shares on a pro rata basis to existing shareholders.

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

Neither the Company, nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities during the year.

RESERVES

Details of movements in the reserves of the Company and the Group during the year are set out in note 25 to the financial statements and in the consolidated statement of changes in equity.

DISTRIBUTABLE RESERVES

According to the relevant regulations in the PRC, the amount of retained profits available for distribution is the lower of the amount determined under PRC accounting standards and the amount determined under Hong Kong Financial Reporting Standards ("HKFRSs"). At 31 December 2005, the Company had no reserves available for distribution, as calculated in accordance with the PRC accounting standards. In addition, the Company's share premium account, in the amount of RMB170,717,000, may be distributed in the form of future capitalisation issue.

MAJOR CUSTOMERS AND SUPPLIERS

In the year under review, sales to the Group's five largest customers accounted for 40% of the total sales for the year and sales to the largest customer included therein amounted to 28%. Purchases from the Group's five largest suppliers accounted for 74% of the total purchases for the year and purchases from the largest supplier included therein amounted to 31%.

None of the directors of the Company or any shareholders (which, to the best knowledge of the directors, own more than 5% of the Company's issued share capital) had any beneficial interest in the Group's five largest customers or suppliers.

Report of the Directors

DIRECTORS

The directors of the Company during the year were:

Executive directors:

Mr. Jiang Guoxing
Mr. Shi Lei
Mr. Yu Jun
Ms. Cheng Junxia
Mr. Wang Su
Mr. Tsai Kao Chung (resigned on 31 March 2005)

Non-executive directors:

Mr. Chen Xiaohong
Ms. Zhang Qianling
Mr. He Lixing
Mr. Shen Xiaozu

Independent non-executive directors:

Mr. Leung Tin Pui
Mr. Xu Juyan
Mr. Cheung Wing Keung
Mr. David Yung (resigned on 31 March 2005)

In accordance with article 87 of the Company's articles of association, executive directors and non-executive directors shall be elected at the shareholders' general meeting for a term of three years. Independent non-executive directors shall be elected at the shareholders' general meeting for a term of one year. A director may serve consecutive terms if re-elected upon the expiration of the term.

All directors will retire by rotation and, being eligible, will offer themselves for re-election at the forthcoming annual general meeting ("AGM"), except for Mr. Xu Juyan, who will not offer himself for re-election due to personal reasons.

The Company has received annual confirmations of independence from Mr. Leung Tin Pui, Mr. Xu Juyan and Mr. Cheung Wing Keung, and still considers them to be independent.

DIRECTORS' AND SENIOR MANAGEMENT'S BIOGRAPHIES

Biographical details of the directors of the Company and of the senior management of the Group are set out in the section headed "Directors' and Senior Management's Biographies" of the annual report.

DIRECTORS' SERVICE CONTRACTS

Each of the executive directors and non-executive directors has entered into a service contract with the Company for a term of three years commencing on 19 July 2003 which will continue thereafter unless terminated by three months' prior written notice to be given by either party to the other without payment of compensation.

Mr. Leung Tin Pui, Mr. Xu Juyan and Mr. Cheung Wing Keung, who are the independent non-executive directors and audit committee members of the Company, have signed letters of appointment with the Company for a period of one year commencing from 27 May 2005 until the forthcoming AGM in or about May 2006 and are subject to termination by either party giving no less than one month's written notice.

No director proposed for re-election at the forthcoming AGM has a service contract with the Company which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

DIRECTORS' REMUNERATION

The directors' fees are subject to shareholders' approval at general meetings. Other emoluments are determined by the Company's board of directors with reference to directors' duties, responsibilities and performance and the results of the Group.

DIRECTORS' INTERESTS IN CONTRACTS

No director had a material interest, either directly or indirectly, in any contract of significance to the business of the Group to which the Company or any of its subsidiaries was a party during the year.

MANAGEMENT CONTRACTS

No contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or were in existence during the year.

DIRECTORS', SUPERVISORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARES AND UNDERLYING SHARES

At 31 December 2005, the interests and short positions of the directors, supervisors and chief executive of the Company in the share capital and underlying shares of the Company or 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 by the Company pursuant to Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.46 of the GEM Listing Rules, were as follows:

Long positions in domestic shares of the Company:

	Number of issued shares held, capacity and nature of interest					Percentage of the Company's issued share capital
	Directly beneficially owned	Through spouse or minor children	Through controlled corporation	Beneficiary of a trust *(Note)*	Total	
Directors						
Mr. Jiang Guoxing	7,210,000	–	–	1,442,300	8,652,300	1.38
Mr. Shi Lei	7,210,000	–	–	12,980,000	20,190,000	3.23
Mr. Yu Jun	–	–	–	10,961,530	10,961,530	1.76
Ms. Cheng Junxia	–	–	–	8,076,920	8,076,920	1.29
Mr. Wang Su	–	–	–	7,211,530	7,211,530	1.16
Mr. Chen Xiaohong	–	–	–	7,211,530	7,211,530	1.16
Ms. Zhang Qianling	–	–	–	1,733,650	1,733,650	0.28
Mr. He Lixing	–	–	–	1,442,300	1,442,300	0.23
Mr. Shen Xiaozu	–	–	–	1,442,300	1,442,300	0.23
	14,420,000	–	–	52,502,060	66,922,060	10.72
Supervisors						
Mr. Li Wei	–	–	–	6,057,690	6,057,690	0.97
Mr. Ding Shengbiao	–	–	–	7,211,530	7,211,530	1.16
Mr. Xu Lenian	–	–	–	865,380	865,380	0.14
	–	–	–	14,134,600	14,134,600	2.27

Note:

These shares are held by the Staff Shareholding Association of the Company (the "SSAC") which is constituted by members consisting of the executive and non-executive directors, the supervisors, certain employees and ex-employees, various employees of ASIC System State-Key Laboratory of Shanghai Fudan University ("University Laboratory") and Shanghai Commerce and Invest (Group) Corporation ("SCI"), a substantial shareholder of the Company, as well as various individuals engaged in technological co-operation with the University Laboratory.

Save as disclosed above, as at 31 December 2005, none of the directors, supervisors or chief executive had registered an interest or short position in shares, underlying shares or debentures of the Company or any of its associated corporations that was required to be recorded pursuant to Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.46 of the GEM Listing Rules.

DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBENTURES

At no time during the year were rights to acquire benefits by means of the acquisition of shares in or debentures of the Company granted to any director or their respective spouse or minor children, or were any such rights exercised by them; or was the Company or any of its subsidiaries a party to any arrangement to enable the directors to acquire such rights in any other body corporate.

SUBSTANTIAL SHAREHOLDERS' AND OTHER PERSONS' INTERESTS AND SHORT POSITIONS IN SHARES AND UNDERLYING SHARES

At 31 December 2005, the following interests of 5% or more of the issued share capital of the Company were recorded in the register of interests required to be kept by the Company pursuant to Section 336 of the SFO:

Long positions in domestic shares of the Company:

Name	*Notes*	**Capacity and nature of interest**	**Number of ordinary shares held**	**Percentage of the Company's issued share capital**
SSAC		Directly beneficially owned	144,230,000	23.10
Shanghai Fudan High Tech Company	*(1)*	Directly beneficially owned	106,730,000	17.09
SCI	*(2)*	Directly beneficially owned and through a controlled corporation	95,200,000	15.25

Notes:

(1) Shanghai Fudan High Tech Company is a state-owned enterprise wholly owned by Shanghai Fudan University.

(2) SCI is a state-owned enterprise wholly owned by the Shanghai Municipal Government. Of the 95,200,000 domestic shares in which SCI is interested, 46,160,000 domestic shares are held in its own name, 34,620,000 domestic shares are held by a wholly-owned subsidiary of SCI, Shanghai Pacific Commercial Trust Company Limited, and 14,420,000 domestic shares are held by a 74.3%-owned subsidiary, Ningbo Lirong Co., Ltd. The 46,160,000 domestic shares held in its own name represent approximately 7.39% of the registered share capital of the Company.

Save as disclosed above, as at 31 December 2005, no person, other than the directors, supervisors and chief executive of the Company, whose interests are set out in the section headed "Directors', supervisors' and chief executive's interests and short positions in shares and underlying shares" above, had registered an interest or short position in the shares or underlying shares of the Company that was required to be recorded pursuant to Section 336 of the SFO.

CONNECTED TRANSACTIONS

Details of the connected transactions of the Group are set out in note 28 to the financial statements.

DIRECTORS' INTERESTS IN A COMPETING BUSINESS

During the year and up to the date of this report, none of the directors of the Company had an interest in a business which competes or is likely to compete, either directly or indirectly, with the businesses of the Group, as defined in the GEM Listing Rules.

BOARD PRACTICES AND PROCEDURES

In the opinion of the directors, the Company has complied with the requirements of board practices and procedures of Rule 5.34 of the GEM Listing Rules throughout the accounting period covered by the annual report.

A report on the principle corporate governance practices adopted by the Company is set out in the section headed "Corporate Governance Report" of the annual report.

AUDIT COMMITTEE

The Company has an audit committee which was established with written terms of reference in compliance with Rules 5.28 to 5.33 of the GEM Listing Rules. The primary duties of the audit committee are to review and supervise the financial reporting process and internal controls of the Group. The audit committee comprises the three independent non-executive directors of the Company, Mr. Leung Tin Pui, Mr. Xu Juyan and Mr. Cheung Wing Keung. The Company's and the Group's financial statements for the year ended 31 December 2005 have been reviewed by the committee, who were of the opinion that such statements complied with the applicable accounting standards, the GEM and legal requirements, and that adequate disclosures had been made. The audit committee held four meetings during 2005.

AUDITORS

Ernst & Young retire and a resolution for their reappointment as auditors of the Company will be proposed at the forthcoming annual general meeting.

ON BEHALF OF THE BOARD

Jiang Guoxing
Chairman

Shanghai, the People's Republic of China
21 March 2006

Report of the Auditors

ERNST & YOUNG

Ernst & Young
Corporate Finance Limited
12th Floor
Two International Finance Centre
8 Finance Street, Central
Hong Kong
Phone: (852) 2846 9888
Fax: (852) 2501 0343

安永企業融資顧問有限公司
香港中環金融街8號
國際金融中心2期12樓
電話：(852) 2846 9888
傳真：(852) 2501 0343

To the members
Shanghai Fudan Microelectronics Company Limited
(Incorporated in the People's Republic of China with limited liability)

We have audited the financial statements on pages 34 to 87 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Companies 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. It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion solely to you, as a body, in accordance with Section 141 of the Companies Ordinance, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

BASIS OF OPINION

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. An audit includes an 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 and the Group's circumstances, consistently applied and adequately disclosed.

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

OPINION

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2005 and of the profit and cash flows of the Group for the year then ended and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Ernst & Young
Certified Public Accountants

Hong Kong
21 March 2006

Consolidated Income Statement

Year ended 31 December 2005

	Notes	2005 RMB$'000	2004 RMB$'000
REVENUE	5	**211,211**	132,710
Cost of sales		**(157,393)**	(85,386)
Gross profit		**53,818**	47,324
Other income and gains	5	**7,341**	6,860
Selling and distribution costs		**(7,914)**	(6,292)
Administrative expenses		**(22,795)**	(19,010)
Other operating expenses		**(20,788)**	(20,491)
Share of losses of associates		**–**	(835)
PROFIT BEFORE TAX	6	**9,662**	7,556
Tax	9(a)	**(1,272)**	(57)
PROFIT FOR THE YEAR		**8,390**	7,499
Attributable to:			
Equity holders of the parent		**8,037**	7,239
Minority interests		**353**	260
		8,390	7,499
EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT			
Basic – For profit for the year	11	**1.29 cents**	1.16 cents

SHANGHAI FUDAN MICROELECTRONICS COMPANY LIMITED*

Consolidated Balance Sheet

31 December 2005

	Notes	2005 RMB$'000	2004 RMB$'000
NON-CURRENT ASSETS			
Property, plant and equipment	12	**57,834**	67,208
Construction in progress	13	**142**	138
Intangible assets	14	**9,280**	7,629
Investment in an associate	16	**–**	241
Available-for-sale equity investments/ long term investments	17	**4,500**	4,747
Total non-current assets		**71,756**	79,963
CURRENT ASSETS			
Inventories	18	**56,306**	37,487
Trade and bills receivables	19	**63,179**	34,773
Prepayments, deposits and other receivables	20	**3,642**	6,209
Pledged cash and bank balances	21	**1,639**	772
Cash and cash equivalents	21	**134,994**	109,900
Total current assets		**259,760**	189,141
CURRENT LIABILITIES			
Trade and bills payables	22	**66,629**	21,038
Other payables and accruals	23	**22,281**	14,507
Tax payable	9(b)	**324**	–
Total current liabilities		**89,234**	35,545
NET CURRENT ASSETS		**170,526**	153,596
TOTAL ASSETS LESS CURRENT LIABILITIES		**242,282**	233,559
NON-CURRENT LIABILITIES			
Long term payables	23	**2,737**	5,615
Deferred tax liabilities	9(c)	**878**	–
Total non-current liabilities		**3,615**	5,615
Net assets		**238,667**	227,944
EQUITY			
Equity attributable to equity holders of the parent			
Issued capital	24	**62,435**	62,435
Reserves	25	**172,117**	164,330
		234,552	226,765
Minority interests		**4,115**	1,179
Total equity		**238,667**	227,944

Jiang Guoxing
Director

Shi Lei
Director

SHANGHAI FUDAN MICROELECTRONICS COMPANY LIMITED*

Consolidated Statement of Changes in Equity

Year ended 31 December 2005

	Attributable to equity holders of the parent								
	Issued share capital	Share premium account	Statutory surplus reserve	Statutory public welfare fund	Exchange fluctuation reserve	Retained profits/ (accumulated losses)	Total	Minority interests	Total equity
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
	Note 24	*Note 25*	*Note 25*	*Note 25*					
At 1 January 2004	62,435	170,717	–	–	36	(13,646)	219,542	419	219,961
Exchange realignment and total income and expenses for the year recognised directly in equity	–	–	–	–	(16)	–	(16)	–	(16)
Net profit for the year	–	–	–	–	–	7,239	7,239	260	7,499
Total income and expenses for the year	–	–	–	–	(16)	7,239	7,223	260	7,483
Capital contribution from minority shareholders of a subsidiary	–	–	–	–	–	–	–	500	500
Transfer from retained profits	–	–	179	89	–	(268)	–	–	–
At 31 December 2004 and beginning of year	62,435	170,717	179	89	20	(6,675)	226,765	1,179	227,944
Exchange realignment and total income and expenses for the year recognised directly in equity	–	–	–	–	(250)	–	(250)	–	(250)
Net profit for the year	–	–	–	–	–	8,037	8,037	353	8,390
Total income and expenses for the year	–	–	–	–	(250)	8,037	7,787	353	8,140
Deemed disposal of equity interest in a subsidiary	–	–	–	–	–	–	–	2,583	2,583
Transfer from retained profits	–	–	93	47	–	(140)	–	–	–
At 31 December 2005	**62,435**	**170,717**	**272**	**136**	**(230)**	**1,222**	**234,552**	**4,115**	**238,667**

Consolidated Cash Flow Statement

Year ended 31 December 2005

	Notes	2005 RMB$'000	2004 RMB$'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit before tax		**9,662**	7,556
Adjustments for:			
Share of losses of associates		**–**	835
Interest income	6	**(1,479)**	(1,156)
(Gain)/loss on disposal of items of property, plant and equipment	6	**46**	(23)
Gain on disposal of equity interest in an associate	6	**–**	(4,459)
Loss on deemed disposal of equity interest in a subsidiary	6	**2,583**	–
Depreciation	6	**11,186**	7,927
Amortisation of deferred development costs	6	**3,201**	4,151
Impairment of deferred development costs	6	**–**	2,045
Impairment of available-for-sale equity investments/long term investments	6	**747**	716
Operating profit before working capital changes		**25,946**	17,592
Increase in inventories		**(18,819)**	(12,703)
Increase in trade and bills receivables		**(28,406)**	(4,016)
Decrease in prepayments, deposits and other receivables		**2,882**	85
Increase in trade and bills payables		**45,591**	8,469
Increase in other payables and accruals		**7,478**	1,960
Cash generated from operations		**34,672**	11,387
Hong Kong profits tax paid		**(57)**	(57)
Net cash inflow from operating activities		**34,615**	11,330

Consolidated Cash Flow Statement

Year ended 31 December 2005

	Notes	2005 RMB$'000	2004 RMB$'000
CASH FLOWS FROM INVESTING ACTIVITIES			
Decrease/(increase) in time deposits with original maturity of over three months when acquired		**(19,000)**	14,000
Interest received		**1,164**	1,156
Purchases of items of property, plant and equipment		**(4,313)**	(28,690)
Proceeds from disposal of items of property, plant and equipment		**9**	36
Receipt of government grants		**1,055**	2,332
Additions to intangible assets		**(5,908)**	(5,487)
Purchases of available-for-sale equity investments/ long term investments		**(500)**	–
Proceeds from disposal of an associate	*26*	**241**	6,000
Net cash outflow from investing activities		**(27,252)**	(10,653)
Net cash outflow from investing activities		**(27,252)**	(10,653)
CASH FLOWS FROM FINANCING ACTIVITIES			
Capital contribution from minority shareholders of a subsidiary		**–**	500
Net cash inflow from financing activities		**–**	500
NET INCREASE IN CASH AND CASH EQUIVALENTS		**7,363**	1,177
Cash and cash equivalents at beginning of year		**91,672**	90,511
Effect of foreign exchange rate changes, net		**(402)**	(16)
CASH AND CASH EQUIVALENTS AT END OF YEAR		**98,633**	91,672
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS			
Cash and bank balances	*21*	**57,363**	58,900
Cash and bank balances pledged for bank facilities	*21*	**1,639**	772
Time deposits with original maturity of less than three months when acquired	*21*	**39,631**	32,000
		98,633	91,672

Balance Sheet

31 December 2005

	Notes	2005 RMB$'000	2004 RMB$'000
NON-CURRENT ASSETS			
Property, plant and equipment	*12*	**46,210**	58,408
Construction in progress	*13*	**142**	138
Intangible assets	*14*	**7,392**	5,469
Investments in subsidiaries	*15*	**16,428**	16,428
Investment in an associate	*16*	**–**	245
Available-for-sale equity investments/ long term investments	*17*	**4,500**	4,747
Total non-current assets		**74,672**	85,435
CURRENT ASSETS			
Inventories	*18*	**41,613**	35,850
Due from subsidiaries	*15*	**8,067**	4,707
Trade and bills receivables	*19*	**43,086**	31,404
Prepayments, deposits and other receivables	*20*	**3,335**	5,084
Pledged cash and bank balances	*21*	**1,639**	772
Cash and cash equivalents	*21*	**101,261**	99,231
Total current assets		**199,001**	177,048
CURRENT LIABILITIES			
Due to subsidiaries	*15*	**365**	227
Trade and bills payables	*22*	**33,870**	21,037
Other payables and accruals	*23*	**11,341**	10,792
Total current liabilities		**45,576**	32,056
NET CURRENT ASSETS		**153,425**	144,992
TOTAL ASSETS LESS CURRENT LIABILITIES		**228,097**	230,427
NON-CURRENT LIABILITY			
Long term payables	23	**–**	5,615
Net assets		**228,097**	224,812
EQUITY			
Issued capital	24	**62,435**	62,435
Reserves	25	**165,662**	162,377
Total equity		**228,097**	224,812

Jiang Guoxing
Director

Shi Lei
Director

1. CORPORATE INFORMATION

Shanghai Fudan Microelectronics Company Limited (the "Company") is a limited liability company incorporated in Shanghai, the People's Republic of China (the "PRC"). The registered office of the Company is located at No. 220 Handan Road, Shanghai, the PRC. The Company has established a place of business in Hong Kong, which is located at Flat 12, 7/F., East Ocean Centre, 98 Granville Road, Tsimshatsui East, Kowloon.

The principal activities of the subsidiaries are the provision of testing services for integrated circuits ("IC") products; designing, developing and selling IC testing software and products; production of probe cards; as well as the provision of research and consultancy services of IC technology.

The Company's principal activities have not been changed during the year and consist of designing, developing and selling products of application-specific IC.

2.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") (which also include Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for available-for-sale equity investments, as further disclosed in the accounting policies below. These financial statements are presented in Renminbi ("RMB") and all values are rounded to the nearest thousand (RMB'000) except when otherwise indicated.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended 31 December 2005. Adjustments are made to bring into line any dissimilar accounting policies that may exist. The results of subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. All significant intercompany transactions and balances within the Group are eliminated on consolidation.

The acquisition of subsidiaries during the year has been accounted for using the purchase method of accounting. This method involves allocating the cost of the business combinations to the fair value of the assets acquired, and liabilities and contingent liabilities assumed at the date of acquisition. The cost of the acquisition is measured at the aggregate of the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition.

Minority interests represent the interests of outside shareholders in the results and net assets of the Company's subsidiaries.

2.2 IMPACT OF NEW AND REVISED HKFRSs

The following new and revised HKFRSs affect the Group and are adopted for the first time for the current year's financial statements:

HKAS 1	Presentation of Financial Statements
HKAS 2	Inventories
HKAS 7	Cash Flow Statements
HKAS 8	Accounting Policies, Changes in Accounting Estimates and Errors
HKAS 10	Events after the Balance Sheet Date
HKAS 12	Income Taxes
HKAS 14	Segment Reporting
HKAS 16	Property, Plant and Equipment
HKAS 17	Leases
HKAS 18	Revenue
HKAS 19	Employee Benefits
HKAS 20	Accounting for Government Grants and Disclosure of Government Assistance
HKAS 21	The Effects of Changes in Foreign Exchange Rates
HKAS 24	Related Party Disclosures
HKAS 27	Consolidated and Separate Financial Statements
HKAS 28	Investments in Associates
HKAS 32	Financial Instruments: Disclosure and Presentation
HKAS 33	Earnings per Share
HKAS 36	Impairment of Assets
HKAS 38	Intangible Assets
HKAS 39	Financial Instruments: Recognition and Measurement
HKAS 39 Amendment	Transition and Initial Recognition of Financial Assets and Financial Liabilities

Other than HKAS 1, the adoption of the HKASs above have had no material impact on the accounting policies of the Group and the Company and the methods of computation in the Group's and the Company's financial statements.

HKAS 1 has affected the presentation of minority interests on the face of the consolidated balance sheet, consolidated income statement, consolidated statement of changes in equity and other disclosures.

2.3 IMPACT OF ISSUED BUT NOT YET EFFECTIVE HKFRSs

The Group has not applied the following new and revised HKFRSs, that have been issued but are not yet effective, in these financial statements. Unless otherwise stated, these HKFRSs are effective for annual periods beginning on or after 1 January 2006:

HKAS 1 Amendment	Capital Disclosures
HKAS 19 Amendment	Actuarial Gains and Losses, Group Plans and Disclosures
HKAS 21 Amendment	Net Investment in a Foreign Operation
HKAS 39 Amendment	Cash Flow Hedge Accounting of Forecast Intragroup Transactions
HKAS 39 Amendment	The Fair Value Option
HKAS 39 & HKFRS 4 Amendments	Financial Guarantee Contracts
HKFRSs 1 & 6 Amendments	First-time Adoption of Hong Kong Financial Reporting Standards and Exploration for and Evaluation of Mineral Resources
HKFRS 6	Exploration for and Evaluation of Mineral Resources
HKFRS 7	Financial Instruments: Disclosures
HK(IFRIC)-Int 4	Determining whether an Arrangement contains a Lease
HK(IFRIC)-Int 5	Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds
HK(IFRIC)-Int 6	Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment
HK(IFRIC)-Int 7	Applying the Restatement Approach under HKFRS 29 Financial Reporting in Hyperinflationary Economics (effective on or after 1 March 2006)

The HKAS 1 Amendment shall be applied for annual periods beginning on or after 1 January 2007. The revised standard will affect the disclosures about qualitative information about the Group's objective, policies and processes for managing capital; quantitative data about what the Company regards as capital; and compliance with any capital requirements and the consequences of any non-compliance.

HKFRS 7 will replace HKAS 32 and has modified the disclosure requirements of HKAS 32 relating to financial instruments. This HKFRS shall be applied for annual periods beginning on or after 1 January 2007.

Except as stated above, the Group expects that the adoption of the other pronouncements listed above will not have any significant impact on the Group's financial statements in the period of initial application.

2.4 CHANGE OF ACCOUNTING POLICY

In prior years, the Group classified its investments in unlisted equity investments as long term investments, which were held for non-trading purposes and were stated at their estimated fair values with adjustments to the estimated fair values, if any, to the long term investment revaluation reserve. The estimated fair values of unlisted investments were determined by the directors having regard to comparison of price/earnings ratios and investment yields of the securities with those of similar listed securities, with allowance made for the lower liquidity of the unlisted securities.

Effective from 1 January 2005, unlisted securities are stated at cost less any impairment losses, on an individual basis. An impairment loss is recognised only if the carrying amount exceeds its recoverable amount and is charged to the income statement in the period in which it arises. This is a change in the accounting policy for available-for-sale equity investments/long term investments in non-trading unlisted equity securities from the prior years, as the directors consider information to be applied in the valuation techniques cannot be reliably obtained on a continuous basis, and the fair value of unlisted equity securities cannot be reliably measured. As this change does not have any significant impact on the financial statements for the current and prior years, there is no restatement to the comparative amounts.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Subsidiaries

A subsidiary is an entity whose financial and operating policies the Company controls, directly or indirectly, so as to obtain benefits from its activities. The results of subsidiaries are included in the Company's income statement to the extent of dividends received and receivable. The Company's investments in subsidiaries are stated at cost less any impairment losses.

Associates

An associate is an entity, not being a subsidiary or a jointly-controlled entity, in which the Group has a long term interest of generally not less than 20% of the equity voting rights and over which it is in a position to exercise significant influence.

The Group's share of the post-acquisition results and reserves of associates is included in the consolidated income statement and consolidated reserves, respectively. The Group's interests in associates are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting, less any impairment losses.

The results of associates are included in the Company's income statement to the extent of dividends received and receivable. The Company's investments in associates are treated as non-current assets and are stated at cost less any impairment losses.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(Continued)

Impairment of assets

Where an indication of impairment exists, or when annual impairment testing for an asset is required (other than inventories and financial assets), the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as the higher of the asset's or cash-generating unit's value in use and its fair value less costs to sell, and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. 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. An impairment loss is charged to the income statement in the period in which it arises.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss of an asset other than goodwill is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation), had no impairment loss been recognised for the asset in prior years. A reversal of such impairment loss is credited to the income statement in the period in which it arises.

Related parties

A party is considered to be related to the Group if:

(a) the party, directly or indirectly through one or more intermediaries, (i) controls, is controlled by, or is under common control with, the Group; (ii) has an interest in the Group that gives it significant influence over the Group; or (iii) has joint control over the Group;

(b) the party is an associate;

(c) the party is a jointly-controlled entity;

(d) the party is a member of the key management personnel of the Group or its parent;

(e) the party is a close member of the family of any individual referred to in (a) or (d); or

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Related parties *(Continued)*

(f) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e).

Property, plant and equipment and depreciation

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and any impairment losses. When an item of property, plant and machinery is classified as held for sale or when it is part of a disposal group classified as held for sale, it is not depreciated and is accounted for in accordance with HKFRS 5. The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the income statement in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment, and where the cost of the item can be measured reliably, the expenditure is capitalised as an additional cost of that asset or as a replacement.

Depreciation is calculated on the straight-line basis to write off the cost of each item of property, plant and equipment to its residual value over its estimated useful life. The principal annual rates used for this purpose are as follows:

Buildings	1.9%
Machinery and office equipment	19%
Motor vehicles	19%

Where parts of an item of property, plant and equipment have different useful lives, the cost of that item is allocated on a reasonable basis among the parts and each part is depreciated separately.

Residual values, useful lives and depreciation method are reviewed, and adjusted if appropriate, at each balance sheet date.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Property, plant and equipment and depreciation *(Continued)*

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss on disposal or retirement recognised in the income statement in the year the asset is derecognised is the difference between the net sales proceeds and the carrying amount of the relevant asset.

Construction in progress represents machinery and other items of property, plant and equipment under construction or installation, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction, installation and testing during the period of construction. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

Intangible assets

The useful lives of intangible assets of the Group are assessed to be finite. Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each balance sheet date.

Changes in the expected useful life or expected pattern of consumption of future economic benefits embodies in the asset is accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the income statement in the expense category consistent with the function of the intangible asset.

Research and development costs

All research costs are charged to the income statement as incurred.

Expenditure incurred on projects to develop new products is capitalised and deferred only when the Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the project and the ability to measure reliably the expenditure during the development. Product development expenditure which does not meet these criteria is expensed when incurred.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(Continued)

Research and development costs *(Continued)*

Deferred development costs are stated at cost less any impairment losses and are amortised using the straight-line basis over the expected commercial lives of the underlying products, not exceeding three years, commencing from the date when the products are put into commercial production.

Operating leases

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Group is the lessor, assets leased by the Group under operating leases are included in non-current assets, and rentals receivable under the operating leases are credited to the income statement on the straight-line basis over the lease terms. Where the Group is the lessee, rentals payable under the operating leases are charged to the income statement on the straight-line basis over the lease terms.

Investments and other financial assets

Applicable to the year ended 31 December 2004:

The Group classified its equity investments, other than subsidiaries and associates, as long term investments.

Long term investments are non-trading investments in listed and unlisted equity securities intended to be held on a long term basis.

Listed securities are stated at their fair values on the basis of their quoted market prices at the balance sheet date, on an individual investment basis. Unlisted securities are stated at their estimated fair values, on an individual basis. The estimated fair values of unlisted investments are determined by the directors having regard to comparison of price/earnings ratios and investment yields of the securities with those of similar listed securities, with allowance made for the lower liquidity of the unlisted securities.

The gains or losses arising from changes in the fair value of a security are dealt with as movements in the long term investment revaluation reserve, until the security is sold, collected, or otherwise disposed of, or until the security is determined to be impaired, when the cumulative gain or loss derived from the security recognised in the long term investment revaluation reserve, together with the amount of any further impairment, is charged to the income statement in the period in which the impairment arises.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Investments and other financial assets *(Continued)*

Applicable to the year ended 31 December 2005:

Financial assets in the scope of HKAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments and available-for-sale financial assets, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at the balance sheet date.

All regular way purchases and sales of financial assets are recognised on the settlement date, i.e., the date that the assets are being delivered to or by the Group. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Financial assets at fair value through profit or loss

Financial assets classified as held for trading are included in the category "financial assets at fair value through profit or loss". Financial assets are classified as held for trading if they are acquired for the purpose of sale in the near term. Gains or losses on investments held for trading are recognised in the income statement.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in the income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Investments and other financial assets *(Continued)*

Applicable to the year ended 31 December 2005: (Continued)

Held-to-maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity when the Group has the positive intention and ability to hold to maturity. Investments intended to be held for an undefined period are not included in this classification. Other long term investments that are intended to be held to maturity, such as bonds, are subsequently measured at amortised cost. Amortised cost is computed as the amount initially recognised minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initially recognised amount and the maturity amount. This calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums and discounts. For investments carried at amortised cost, gains and losses are recognised in the income statement when the investments are derecognised or impaired, as well as through the amortisation process.

Available-for-sale financial assets

Available-for-sale financial assets are non-derivative financial assets in listed and unlisted equity securities that are designated as available for sale or are not classified in any of the other three categories. After initial recognition, available-for-sale financial assets are measured at fair value, with gains or losses recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the income statement.

When the fair value of unlisted equity securities cannot be reliably measured because (a) the variability in the range of reasonable fair value estimates is significant for that investment or (b) the probabilities of the various estimates within the range cannot be reasonably assessed and used in estimating fair value, such securities are stated at cost less any impairment losses.

Fair value

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business at the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; a discounted cash flow analysis; and option pricing models.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(Continued)

Impairment of financial assets (applicable to the year ended 31 December 2005)

The Group assesses at each balance sheet date whether there is any objective evidence that a financial asset or a group of financial assets is impaired.

Assets carried at amortised cost

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced either directly or through the use of an allowance account. The amount of the impairment loss is recognised in the income statement.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. Any subsequent reversal of an impairment loss is recognised in the income statement, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date.

Assets carried at cost

If there is objective evidence that an impairment loss on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Impairment losses on these assets are not reversed.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(Continued)

Available-for-sale financial assets

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in profit or loss, is transferred from equity to the income statement. Impairment losses on equity instruments classified as available for sale are not reversed through profit or loss.

Derecognition of financial assets (applicable to the year ended 31 December 2005)

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired;
- the Group retains the rights to receive cash flows from the asset, but has assumed an obligation to pay in full without material delay to a third party under a "pass-through" arrangement; or
- the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Group's continuing involvement is the amount of the transferred asset that the Group may repurchase, except in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, where the extent of the Group's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(Continued)

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on the weighted average basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour and an appropriate proportion of overheads. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

Cash and cash equivalents

For the purpose of the consolidated cash flow statement, cash and cash equivalents comprise cash on hand and demand deposits, and short term highly liquid investments which are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired, less bank overdrafts which are repayable on demand and form an integral part of the Group's cash management.

For the purpose of the balance sheet, cash and cash equivalents comprise cash on hand and at banks, including term deposits and assets similar in nature to cash, which are not restricted as to use.

Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the income statement, or in equity if it relates to items that are recognised in the same or a different period directly in equity.

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the balance sheet date.

Deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences, except:

- where the deferred tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of taxable temporary differences associated with investments in subsidiaries and associates, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(Continued)

Income tax *(Continued)*

Deferred tax assets are recognised for all deductible temporary differences, carryforward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax credits and unused tax losses can be utilised except:

- where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and,

- in respect of deductible temporary differences associated with investments in subsidiaries and associates, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Conversely, previously unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Government grants

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the periods necessary to match the grant on a systematic basis to the costs that it is intended to compensate. Where the grant relates to an asset, the fair value is deducted from the carrying amount of the assets and released to the income statement by way of a reduced depreciation charge.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(Continued)

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

(a) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;

(b) from the rendering of services, in the period in which services are rendered;

(c) rental income, on a time proportion basis over the lease terms;

(d) royalty fee income, when the significant risks and rewards of ownership have been transferred to the licensee, under assignment of rights for a fixed fee or non refundable guarantee under a non-cancelable contract which permit the licensee to exploit those rights freely and the licensor has no remaining obligations to perform; and

(e) interest income, on an accrual basis using the effective interest method by applying the rate that discounts the estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset.

Pension schemes

The employees of the Company and its subsidiary which operates in Mainland China are required to participate in a central pension scheme operated by the local municipal government. The Company and its subsidiary are required to contribute 22.5% of its payroll costs to the central pension scheme. The contributions are charged to the income statement as they become payable in accordance with the rules of the central pension scheme.

The Group's subsidiary in Hong Kong operates a defined contribution Mandatory Provident Fund retirement benefits scheme (the "MPF Scheme") under the Mandatory Provident Fund Schemes Ordinance, for all of its employees who are eligible to participate in the MPF Scheme. Contributions are made based on a percentage of the employees' basic salaries and are charged to the income statement as they become payable in accordance with the rules of the MPF Scheme. The assets of the MPF Scheme are held separately from those of the Group in an independently administered fund. The Group's subsidiary contributions vest fully with the employees when contributed into the MPF Scheme.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(Continued)

Foreign currencies

These financial statements are presented in Renminbi ("RMB"), which is the Company's functional and presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Foreign currency transactions are initially recorded using the functional currency rates ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rates of exchange ruling at the balance sheet date. All differences are taken to profit or loss. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

The functional currency of the Group's subsidiary in Hong Kong is not the RMB. As at the balance sheet date, the assets and liabilities of the entity are translated into the presentation currency of the Company at the exchange rates ruling at the balance sheet date and, its income statement is translated into RMB at the weighted average exchange rate for the year. The resulting exchange differences are included in a separate component of equity. On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the income statement.

For the purpose of the consolidated cash flow statement, the cash flows of the overseas subsidiary are translated into RMB at the exchange rates ruling at the dates of the cash flows. Frequently recurring cash flows of the overseas subsidiary which arise throughout the year are translated into RMB at the weighted average exchange rates for the year.

4. SEGMENT INFORMATION

Segment information is presented by way of two segment formats: (i) on a primary segment reporting basis, by business segment; and (ii) on a secondary segment reporting basis, by geographical segment.

The Group's operating businesses are structured and managed separately according to the nature of their operations and the products and services they provide. Each of the Group's business segments represents a strategic business unit that offers products and services which are subject to risks and returns that are different from those of the other business segments. Summary details of the business segments are as follows:

- the design, development and sale of IC products segment ("Design, development and sale of IC products"); and
- the provision of testing services for IC products segment ("Testing services for IC products").

In determining the Group's geographical segments, revenues are attributed to the segments based on the location of the customers, and assets are attributed to the segments based on the location of the assets.

Intersegment sales and transfers are transacted with reference to the selling prices used for sales made to third parties at the then prevailing market prices.

4. SEGMENT INFORMATION *(Continued)*

(a) Business segments

The following table presents revenue, profit and certain asset, liability and expenditure information for the Group's business segments for the years ended 31 December 2005 and 2004.

	Design, development and selling of IC products		Testing services for IC products		Eliminations		Consolidated	
	2005 RMB'000	2004 RMB'000	**2005 RMB'000**	2004 RMB'000	**2005 RMB'000**	2004 RMB'000	**2005 RMB'000**	2004 RMB'000
Segment revenue:								
Sales to external customers	**204,563**	126,623	**6,648**	6,087	**–**	–	**211,211**	132,710
Intersegment sales	**–**	–	**1,605**	2,710	**(1,605)**	(2,710)	**–**	–
Total	**204,563**	126,623	**8,253**	8,797	**(1,605)**	(2,710)	**211,211**	132,710
Segment results	**1,632**	(852)	**607**	2,342	**82**	41	**2,321**	1,531
Interest income and unallocated gains							**7,341**	6,860
Share of losses of associates							**–**	(835)
Profit before tax							**9,662**	7,556
Tax							**(1,272)**	(57)
Profit for the year							**8,390**	7,499
Assets and liabilities								
Segment assets	**230,551**	198,515	**18,834**	14,601	**–**	–	**249,385**	213,116
Interest-bearing time deposits	**77,631**	51,000	**–**	–	**–**	–	**77,631**	51,000
Interests in an associate	**–**	241	**–**	–	**–**	–	**–**	241
Available-for-sale equity investments/Long term investments	**4,500**	4,747	**–**	–	**–**	–	**4,500**	4,747
Total assets	**312,682**	254,503	**18,834**	14,601	**–**	–	**331,516**	269,104
Segment liabilities	**87,374**	38,346	**5,475**	2,814	**–**	–	**92,849**	41,160
Total liabilities	**87,374**	38,346	**5,475**	2,814	**–**	–	**92,849**	41,160
Other segment information:								
Capital expenditure	**11,625**	34,419	**572**	5,482	**–**	–	**12,197**	39,901
Impairment losses recognised in the income statement	**747**	2,761	**–**	–	**–**	–	**747**	2,761
Depreciation	**8,430**	5,780	**2,756**	2,147	**–**	–	**11,186**	7,927
Amortisation of intangible assets	**3,201**	4,151	**–**	–	**–**	–	**3,201**	4,151
Other non-cash expenses	**3,765**	1,404	**134**	–	**–**	–	**3,899**	1,404

4. SEGMENT INFORMATION *(Continued)*

(b) Geographical segments

The following table presents revenue and certain asset and expenditure information for the Group's geographical segments for the years ended 31 December 2005 and 2004.

	Year ended 31 December 2005				
	Mainland China RMB'000	**Asia Pacific RMB'000**	**Others RMB'000**	**Eliminations RMB'000**	**Consolidated RMB'000**
Segment revenue:					
Sales to external customers	**132,546**	**87,106**	**5,570**	**(14,011)**	**211,211**
Other segment information:					
Segment assets	**283,098**	**64,332**	**–**	**(15,914)**	**331,516**
Capital expenditure	**6,141**	**6,056**	**–**	**–**	**12,197**

	Year ended 31 December 2004				
	Mainland China RMB'000	Asia Pacific RMB'000	Others RMB'000	Eliminations RMB'000	Consolidated RMB'000
Segment revenue:					
Sales to external customers	129,514	14,019	6,954	(17,777)	132,710
Other segment information:					
Segment assets	267,728	13,925	–	(12,549)	269,104
Capital expenditure	39,901	–	–	–	39,901

5. REVENUE, OTHER INCOME AND GAINS

Revenue, which is also the Group's turnover, represents the net invoiced value of goods sold, after allowances for returns and trade discounts; the value of services rendered and gross rental income received.

An analysis of revenue, other income and gains is as follows:

	2005 RMB'000	2004 RMB'000
Revenue		
Sale of goods	**204,563**	126,623
Rendering of services	**6,648**	6,087
	211,211	132,710
Other income and gains		
Bank interest income	**1,479**	1,156
Royalty fee income	**2,044**	–
Value-added tax refunds	**1,054**	996
Deed tax refunds	**421**	–
Subsidy income	**1,210**	216
Gross rental income	**404**	–
Gain on disposal of equity interest in an associate	**–**	4,459
Gain on disposal of items of property, plant and equipment	**–**	23
Others	**729**	10
	7,341	6,860

6. PROFIT BEFORE TAX

The Group's profit before tax is arrived at after charging/(crediting):

	2005 RMB'000	2004 RMB'000
Cost of inventories sold	**154,648**	82,813
Cost of services provided	**2,745**	2,573
Depreciation	**11,186**	7,927
Research and development costs:		
Deferred expenditures amortised*	**3,201**	4,151
Current year expenditures	**18,365**	19,570
Less: Government grants released**	**(5,295)**	(2,062)
	16,271	21,659
Minimum lease payments under operating leases:		
Land and buildings	**2,160**	2,034
Auditors' remuneration	**750**	650
Employees benefit expenses (excluding directors' remuneration – *(note 7)*):		
Wages and salaries	**20,991**	17,933
Pension scheme contributions	**2,085**	1,926
	23,076	19,859
Less: Amounts capitalised as development costs	**(3,046)**	(2,494)
	20,030	17,365
Foreign exchange difference, net	**327**	105
Impairment of deferred development costs*	**–**	2,045
Impairment of available-for-sale equity investments/long term investments	**747**	716
(Reversal of)/provision for bad and doubtful debts	**159**	(87)
Write-down of inventories to net realisable value	**3,740**	1,491
Loss on deemed disposal of equity interest in a subsidiary	**2,583**	–
Loss on disposal of items of property, plant and equipment	**46**	–
Gross rental income	**(404)**	–
Bank interest income	**(1,479)**	(1,156)
Value-added tax refunds	**(1,054)**	(996)
Deed tax refunds	**(421)**	–
Royalty fee income	**(2,044)**	–
Subsidy income	**(1,210)**	(216)
Gain on disposal of equity interest in an associate	**–**	(4,459)
Gain on disposal of items of property, plant and equipment	**–**	(23)

6. PROFIT BEFORE TAX *(Continued)*

* *The amortisation and impairment of deferred development costs for the year is included in "Other operating expenses" on the face of the consolidated income statement.*

** *Various government grants have been received for setting up research activities in Shanghai, Mainland China, to support domestic technology development. The government grants released have been deducted from the research and development costs to which they relate. Government grants received for which related expenditure has not yet been undertaken are included in other liabilities in the balance sheet. There are no unfulfilled conditions or contingencies relating to these grants.*

7. DIRECTORS' REMUNERATION

Directors' remuneration for the year, disclosed pursuant to the Rules Governing the Listing of Securities on the GEM and Section 161 of the Companies Ordinance, is as follows:

	Group	
	2005	2004
	RMB'000	RMB'000
Fees for two independent non-executive directors	**170**	147
Other emoluments:		
Salaries, allowances and benefits in kind	**1,537**	1,388
	1,707	1,535

(a) Independent non-executive directors

The fees, salaries, allowances and benefits in kind paid to independent non-executive directors during the year were as follows:

	Fees		Salaries, allowances and benefits in kind	
	2005	2004	**2005**	2004
	RMB'000	RMB'000	**RMB'000**	RMB'000
Mr. Leung Tin Pui	**126**	128	**–**	–
Mr. Xu Juyan	**–**	–	**38**	38
Mr. Cheung Wing Keung	**44**	19	**–**	–
Mr. David Yung	**–**	–	**–**	–
	170	147	**38**	38

There were no other emoluments payable to the independent non-executive directors during the year (2004: Nil).

7. DIRECTORS' REMUNERATION *(Continued)*

(b) Executive directors and non-executive directors:

	Salaries, allowances and benefits in kind RMB'000	Pension schemes contribution RMB'000	Other benefits received RMB'000	Total remuneration RMB'000
2005				
Executive directors:				
Mr. Jiang Guoxing	300	–	–	300
Mr. Shi Lei	341	–	–	341
Mr. Yu Jun	288	–	–	288
Ms. Cheng Junxia	285	–	–	285
Mr. Wang Su	285	–	–	285
Mr. Tsai Kao Chung	–	–	–	–
	1,499	–	–	1,499
Non-executive directors:				
Mr. Chen Xiaohong	–	–	–	–
Ms. Zhang Qianling	–	–	–	–
Mr. He Lixing	–	–	–	–
Mr. Shen Xiaozu	–	–	–	–
	–	–	–	–
	1,499	–	–	1,499

7. DIRECTORS' REMUNERATION *(Continued)*

(b) Executive directors and non-executive directors: *(Continued)*

	Salaries, allowances and benefits in kind RMB'000	Pension schemes contribution RMB'000	Other benefits received RMB'000	Total remuneration RMB'000
2004				
Executive directors:				
Mr. Jiang Guoxing	300	–	–	300
Mr. Shi Lei	300	–	–	300
Mr. Yu Jun	250	–	–	250
Ms. Cheng Junxia	250	–	–	250
Mr. Wang Su	250	–	–	250
Mr. Tsai Kao Chung	–	–	–	–
	1,350	–	–	1,350
Non-executive directors:				
Mr. Chen Xiaohong	–	–	–	–
Ms. Zhang Qianling	–	–	–	–
Mr. He Lixing	–	–	–	–
Mr. Shen Xiaozu	–	–	–	–
	–	–	–	–
	1,350	–	–	1,350

There was no arrangement under which a director waived or agreed to waive any remuneration during the year.

8. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the year included four (2004: four) directors, details of whose remuneration are set out in note 7 above. Details of the remuneration of the remaining one (2004: one) non-director, highest paid employee of the Group for the year are as follows:

	2005 RMB'000	2004 RMB'000
Salaries, allowances and benefits in kind	403	355
Pension scheme contributions	13	13
	416	368

The number of non-director, highest paid employees whose remuneration fell within the following band is as follows:

	Number of employees 2005	2004
Nil to HK$1,000,000	1	1

During the year, no emoluments were paid by the Group to the directors or the highest paid employees either as an inducement to join the Group, or as compensation for loss of office.

9. TAX

Under the Income Tax Law of the PRC, the Company is subject to income tax at a base rate of 33%. Pursuant to an approval document dated 15 January 2004 issued by the local municipal tax bureau, the Company was subject to a preferential income tax rate of 15% from 1 January 2004 to 31 December 2004. The Company is seeking approval of the relevant tax authorities for its continued application of the aforesaid preferential income tax rate. For the financial year ended 31 December 2005, the Company had no assessable income and no provision for income tax was made accordingly.

Under the Income Tax Law of the PRC, the Company's subsidiary, Sino IC Technology Co., Ltd. ("Sino IC") is subject to a preferential income tax rate of 15%. Pursuant to an approval document dated 8 October 2004 issued by the Shanghai Pu Dong New Area Tax Bureau, with effect from 1 January 2004, Sino IC is exempt from corporate and local income tax for its first two profit making years and is entitled to a 50% tax reduction for the succeeding three years. Sino IC is in its second profit making year for the financial year ended 31 December 2005 and thus is exempt from income tax.

9. TAX *(Continued)*

Hong Kong profits tax has been provided at the rate of 17.5% (2004: 17.5%) on the estimated assessable profits arising in Hong Kong during the year.

	2005	2004
	RMB'000	RMB'000
Group:		
Current – Hong Kong	**381**	57
Deferred	**891**	–
Total tax charge for the year	**1,272**	57

(a) Income tax expense

A reconciliation of the tax expense applicable to profit before tax using the statutory rates for the countries in which the Company and its subsidiaries are domiciled to the tax expense at the effective tax rates, and a reconciliation of the applicable rates (i.e., the statutory tax rates) to the effective tax rates, are as follows:

Group – 2005

	Mainland China		**Hong Kong**		**Total**	
	RMB'000	**%**	**RMB'000**	**%**	**RMB'000**	**%**
Profit before tax	**2,302**		**7,360**		**9,662**	
Tax at the applicable tax rates	**345**	**15.0**	**1,288**	**17.5**	**1,633**	**16.9**
Income not subject to tax	**(59)**	**(2.6)**	**(17)**	**(0.2)**	**(76)**	**(0.8)**
Tax concession	**(235)**	**(10.2)**	**–**	**–**	**(235)**	**(2.4)**
Expenses not deductible for tax	**714**	**31.0**	**1**	**–**	**715**	**7.4**
Tax losses utilised from previous periods	**(765)**	**(33.2)**	**–**	**–**	**(765)**	**(7.9)**
Tax charge at the Group's effective rate	**–**	**–**	**1,272**	**17.3**	**1,272**	**13.2**

9. TAX *(Continued)*

(a) Income tax expense *(Continued)*

Group – 2004

	Mainland China		Hong Kong		Total	
	RMB'000	%	RMB'000	%	RMB'000	%
Profit before tax	7,236		320		7,556	
Tax at the applicable tax rates	1,085	15.0	56	17.5	1,141	15.1
Income not subject to tax	(835)	(11.5)	(1)	(0.3)	(836)	(11.1)
Tax concession	(878)	(12.1)	–	–	(878)	(11.6)
Expenses not deductible for tax	1,047	14.4	2	0.6	1,049	13.9
Tax losses utilised from previous periods	(419)	(5.8)	–	–	(419)	(5.5)
Tax charge at the Group's effective rate	–	–	57	17.8	57	0.8

The Group has tax losses, primarily incurred by the Company, of RMB73,000 (2004: RMB5,171,000) that are available for offsetting against future taxable profits.

Deferred tax assets have not been recognised in respect of these losses and temporary differences arising from provisions of the Company, as it is uncertain as to whether the Company will be able to fully utilise the unused tax losses which can only be carried forward for a maximum period of five years and after considering tax incentives arising from the additional deductible allowance for qualified research and development expense to be incurred by the Company.

(b) Income tax payable in the consolidated balance sheet represents:

	2005	2004
	RMB'000	RMB'000
Hong Kong profits tax payable at beginning of year	**–**	–
Provision for the year	**381**	57
Payment during the year	**(57)**	(57)
Hong Kong profits tax payable at end of year	**324**	–

9. TAX *(Continued)*

(c) Deferred tax liabilities at 31 December relate to the following:

	Consolidated balance sheet		Consolidated income statement	
	2005	2004	**2005**	2004
	RMB'000	RMB'000	**RMB'000**	RMB'000
Depreciation of property, plant and equipment	**878**	–	**891**	–

10. NET PROFIT FROM ORDINARY ACTIVITIES ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT

The net profit from ordinary activities attributable to equity holders of the parent for the year ended 31 December 2005 dealt with in the financial statements of the Company was RMB3,285,000 (2004: net loss of RMB4,326,000) (note 25).

11. EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT

The calculation of basic earnings per share amounts is based on the net profit for the year attributable to ordinary equity holders of the parent, and the weighted average number of ordinary shares in issue during the year.

The calculation of basic earnings per share is based on:

	2005	2004
	RMB'000	RMB'000
Earnings		
Net profit attributable to ordinary equity holders of the parent, used in the basic earnings per share calculation	**8,037**	7,239

11. EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT *(Continued)*

	2005	2004
Shares		
Weighted average number of ordinary shares in issue ('000) during the year used in the basic earnings per share calculation	**624,354**	624,354

Diluted earnings per share for the year ended 31 December 2005 and the comparative diluted earnings per share for the year ended 31 December 2004 have not been presented as no diluting events existed during these years.

12. PROPERTY, PLANT AND EQUIPMENT

Group

	Buildings RMB'000	Machinery and office equipment RMB'000	Motor vehicles RMB'000	Total RMB'000
2005				
Cost:				
At beginning of year	37,409	46,577	1,531	85,517
Additions	–	6,668	–	6,668
Transfers from construction in progress	–	673	–	673
Disposals	–	(8,595)	–	(8,595)
At 31 December 2005	37,409	45,323	1,531	84,263
Accumulated depreciation:				
At beginning of year	757	16,972	580	18,309
Provided during the year	963	9,932	291	11,186
Disposals	–	(3,066)	–	(3,066)
At 31 December 2005	1,720	23,838	871	26,429
Net book value:				
At 31 December 2005	35,689	21,485	660	57,834
At 31 December 2004	36,652	29,605	951	67,208

12. PROPERTY, PLANT AND EQUIPMENT *(Continued)*

Group *(Continued)*

	Buildings RMB'000	Machinery and office equipment RMB'000	Motor vehicles RMB'000	Total RMB'000
2004				
Cost:				
At beginning of year	18,795	28,926	1,312	49,033
Additions	–	13,638	120	13,758
Transfers from construction in progress	18,614	4,037	199	22,850
Disposals	–	(24)	(100)	(124)
At 31 December 2004	37,409	46,577	1,531	85,517
Accumulated depreciation:				
At beginning of year	120	9,946	427	10,493
Provided during the year	637	7,042	248	7,927
Disposals	–	(16)	(95)	(111)
At 31 December 2004	757	16,972	580	18,309
Net book value:				
At 31 December 2004	36,652	29,605	951	67,208
At 31 December 2003	18,675	18,980	885	38,540

12. PROPERTY, PLANT AND EQUIPMENT *(Continued)*

Company

	Buildings RMB'000	Machinery and office equipment RMB'000	Motor vehicles RMB'000	Total RMB'000
2005				
Cost:				
At beginning of year	37,409	32,835	1,016	71,260
Additions	–	1,075	–	1,075
Transfers from construction in progress	–	213	–	213
Disposals	–	(8,587)	–	(8,587)
At 31 December 2005	37,409	25,536	1,016	63,961
Accumulated depreciation:				
At beginning of year	757	11,657	438	12,852
Provided during the year	963	6,807	193	7,963
Disposals	–	(3,064)	–	(3,064)
At 31 December 2005	1,720	15,400	631	17,751
Net book value:				
At 31 December 2005	35,689	10,136	385	46,210
At 31 December 2004	36,652	21,178	578	58,408

12. PROPERTY, PLANT AND EQUIPMENT *(Continued)*

Company *(Continued)*

	Buildings RMB'000	Machinery and office equipment RMB'000	Motor vehicles RMB'000	Total RMB'000
2004				
Cost:				
At beginning of year	18,795	20,347	1,116	40,258
Additions	–	11,042	–	11,042
Transfers from construction in progress	18,614	1,470	–	20,084
Disposals	–	(24)	(100)	(124)
At 31 December 2004	37,409	32,835	1,016	71,260
Accumulated depreciation:				
At beginning of year	120	6,734	340	7,194
Provided during the year	637	4,939	193	5,769
Disposals	–	(16)	(95)	(111)
At 31 December 2004	757	11,657	438	12,852
Net book value:				
At 31 December 2004	36,652	21,178	578	58,408
At 31 December 2003	18,675	13,613	776	33,064

13. CONSTRUCTION IN PROGRESS

	Group	Company
	RMB'000	RMB'000
2005		
At beginning of year	138	138
Additions	677	217
Transferred to property, plant and equipment	(673)	(213)
At 31 December 2005	**142**	**142**
2004		
At beginning of year	–	–
Additions	22,988	20,222
Transferred to property, plant and equipment	(22,850)	(20,084)
At 31 December 2004	138	138

14. INTANGIBLE ASSETS

	Deferred development costs	
	Group	Company
	RMB'000	RMB'000
2005		
Cost:		
At beginning of year	22,306	20,146
Additions	4,852	4,276
At 31 December 2005	**27,158**	**24,422**
Accumulated amortisation and impairment:		
At beginning of year	14,677	14,677
Amortisation provided during the year	3,201	2,353
Impairment during the year recognised in the income statement	–	–
At 31 December 2005	**17,878**	**17,030**
Net book value:		
At 31 December 2005	**9,280**	**7,392**
At 31 December 2004	7,629	5,469

14. INTANGIBLE ASSETS *(Continued)*

	Deferred development costs	
	Group	Company
	RMB'000	RMB'000
2004		
Cost:		
At beginning of year	19,151	16,968
Additions	3,155	3,178
At 31 December 2004	22,306	20,146
Accumulated amortisation and impairment:		
At beginning of year	8,481	8,481
Amortisation provided during the year	4,151	4,151
Impairment during the year recognised in the income statement	2,045	2,045
At 31 December 2004	14,677	14,677
Net book value:		
At 31 December 2004	7,629	5,469
At 31 December 2003	10,670	8,487

During the year ended 31 December 2005, the Group received government grants aggregately amounting to RMB1,055,000 (2004: RMB2,332,000). These cash grants were non-recurring in nature and were designated for the purpose of developing certain of the Group's products. The cash grants received have been deducted from the deferred development costs in arriving at their carrying amount. There were no unfulfilled conditions or contingencies relating to these grants.

15. INVESTMENTS IN SUBSIDIARIES

	Company	
	2005	2004
	RMB'000	RMB'000
Unlisted shares, at cost	**16,428**	16,428
Due from subsidiaries	**8,067**	4,707
Due to subsidiaries	**(365)**	(227)
	24,130	20,908

The amounts due from and to subsidiaries included in the Company's current assets and current liabilities of RMB8,066,639 (2004: RMB4,707,137) and RMB364,550 (2004: RMB227,200), respectively, are unsecured, interest-free and have no fixed terms of repayment. The carrying amounts of these amounts due from/to subsidiaries approximate to their fair values.

Particulars of the subsidiaries are as follows:

Name	Place and date of incorporation/ registration and operations	Nominal value of registered/ issued ordinary share capital	Percentage of equity directly attributable to the Company	Principal activities
Sino IC	Mainland China 28 April 2001	RMB13,000,000*	69.2**	Provision of testing services for IC Products; designing, developing and selling of IC testing software; production of probe cards; and the provision of research and consultancy services of IC technology
Shanghai Fudan Microelectronics (HK) Limited	Hong Kong 23 January 2002	HK$7,000,000	100	Developing and selling of IC products

15. INVESTMENTS IN SUBSIDIARIES *(Continued)*

* *Sino IC is registered as a contractual joint venture company under the PRC law.*

** *Pursuant to the resolution of the shareholders' general meeting held on 10 July 2005, the registered capital of Sino IC was increased from RMB10 million to RMB13 million. The additional RMB3 million represents human resource capital contributed by six individual investors on 12 September 2005. As a consequence, the Company's equity interest in Sino IC diluted from 90% to 69.2%, which gave rise to a deemed disposal loss of RMB2,583,000.*

16. INVESTMENT IN AN ASSOCIATE

	Group		Company	
	2005	2004	**2005**	2004
	RMB'000	RMB'000	**RMB'000**	RMB'000
Unlisted shares, at cost	**–**	–	**–**	245
Share of net assets	**–**	241	**–**	–
	–	241	**–**	245

The Company's 49%-owned associate, Shanghai Fu En Electronics Company Limited ("Fu En") was largely dormant since its incorporation on 23 May 2003. Pursuant to a resolution dated 8 November 2004, the directors resolved to liquidate Fu En in the current year and the liquidation process was completed in 2005.

17. AVAILABLE-FOR-SALE EQUITY INVESTMENTS/LONG TERM INVESTMENTS

	Group and Company	
	2005	2004
	RMB'000	RMB'000
Unlisted equity investments, at cost	**5,963**	5,463
Impairment provision	**(1,463)**	(716)
	4,500	4,747

17. AVAILABLE-FOR-SALE EQUITY INVESTMENTS/LONG TERM INVESTMENTS *(Continued)*

The Group's investments in unlisted equity securities is changed from the estimated fair value stated in prior years to cost less impairment losses with effect from 1 January 2005, as the directors consider information to be applied in the valuation techniques cannot be reliably obtained on a continuous basis, and the fair value of unlisted equity securities cannot be reliably measured. As this change does not have any significant impact on the financial statements for the current and prior years, there is no restatement to the comparative amounts.

18. INVENTORIES

	Group		Company	
	2005	2004	**2005**	2004
	RMB'000	RMB'000	**RMB'000**	RMB'000
Raw materials:				
At cost	**25,047**	9,825	**14,995**	8,968
At net realisable value	**22**	182	**22**	182
Work in process:				
At cost	**8,463**	5,036	**8,463**	5,036
At net realisable value	**235**	100	**235**	100
Finished goods:				
At cost	**21,210**	21,257	**16,569**	20,477
At net realisable value	**1,329**	1,087	**1,329**	1,087
	56,306	37,487	**41,613**	35,850

19. TRADE AND BILLS RECEIVABLES

The Group's trading terms with its customers are mainly on credit, except for new customers, where payment in advance is normally required. The credit period is generally up to 90 days. The Group's sales are made to several major customers and there is concentration of credit risks. The Group seeks to maintain strict control over its outstanding receivables and closely monitor the collection to minimise credit risk. Overdue balances are reviewed regularly by senior management. Trade receivables are non-interest-bearing.

19. TRADE AND BILLS RECEIVABLES *(Continued)*

An aged analysis of the trade and bills receivables as at the balance sheet date, based on the invoice date, is as follows:

	Group		Company	
	2005	2004	**2005**	2004
	RMB'000	RMB'000	**RMB'000**	RMB'000
Within 3 months	**46,954**	19,338	**27,104**	15,989
3 to 6 months	**9,594**	11,100	**9,366**	11,100
6 to 12 months	**5,021**	3,713	**5,016**	3,713
Over 12 months	**1,610**	622	**1,600**	602
	63,179	34,773	**43,086**	31,404

20. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

	Group		Company	
	2005	2004	**2005**	2004
	RMB'000	RMB'000	**RMB'000**	RMB'000
Prepayments	**2,504**	5,145	**2,490**	4,647
Deposits and other receivables	**1,138**	1,064	**845**	437
	3,642	6,209	**3,335**	5,084

21. CASH AND CASH EQUIVALENTS AND PLEDGED CASH AND BANK BALANCES

	Group		Company	
	2005	2004	**2005**	2004
	RMB'000	RMB'000	**RMB'000**	RMB'000
Cash and bank balances	**59,002**	59,672	**25,269**	49,003
Time deposits with original maturity of less than three months when acquired	**39,631**	32,000	**39,631**	32,000
Time deposits with original maturity of over three months when acquired	**38,000**	19,000	**38,000**	19,000
Cash and cash equivalents	**136,633**	110,672	**102,900**	100,003
Less: Cash and bank balances pledged for bank facilities	**(1,639)**	(772)	**(1,639)**	(772)
	134,994	109,900	**101,261**	99,231

Cash at bank earns interest at floating rates based on daily bank deposit rates. Short term time deposits are made for varying periods of between one day and three months depending on the immediate cash requirements of the Group, and earn interest at respective short term time deposit rates. The carrying amounts of cash and cash equivalents and the pledged cash and bank balances approximate to their fair values.

22. TRADE AND BILLS PAYABLES

An aged analysis of the trade and bills payables as at the balance sheet date, based on the invoice date, is as follows:

	Group		Company	
	2005	2004	**2005**	2004
	RMB'000	RMB'000	**RMB'000**	RMB'000
Within 3 months	**54,135**	21,038	**21,376**	21,037
3 to 6 months	**12,494**	–	**12,494**	–
	66,629	21,038	**33,870**	21,037

The trade and bills payables are non-interest-bearing and are normally settled on 90-day terms.

23. OTHER PAYABLES AND ACCRUALS

	Group		Company	
	2005	2004	**2005**	2004
	RMB'000	RMB'000	**RMB'000**	RMB'000
Payable for purchases of software	**5,474**	8,056	**–**	8,056
Portion classified as long term	**(2,737)**	(5,615)	**–**	(5,615)
Current portion	**2,737**	2,441	**–**	2,441
Accruals	**2,410**	2,462	**2,119**	2,156
Other payables	**17,134**	9,604	**9,222**	6,195
	22,281	14,507	**11,341**	10,792

Other payables are non-interest-bearing and have an average term of three months.

24. SHARE CAPITAL

	2005 RMB'000	2004 RMB'000
Authorised, issued and fully paid:		
375,000,000 (2004: 375,000,000) unlisted domestic shares of RMB0.10 each	**37,500**	37,500
249,354,000 (2004: 249,354,000) H shares of RMB0.10 each	**24,935**	24,935
	62,435	62,435

There was no movement in the Company's authorised or issued capital during the year.

25. RESERVES

Group

The amounts of the Group's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity on page 36 of the financial statements.

Company

	Share premium account RMB'000	**Accumulated losses** RMB'000	**Total** RMB'000
At 1 January 2004	170,717	(4,014)	166,703
Net loss for the year	–	(4,326)	(4,326)
At 31 December 2004 and beginning of year	170,717	(8,340)	162,377
Net profit for the year	–	3,285	3,285
At 31 December 2005	**170,717**	**(5,055)**	**165,662**

25. RESERVES

In accordance with the Company Law of the PRC and the articles of association of the Company and its subsidiary in Mainland China, the Company and the subsidiary are required to allocate 10% of their profits after tax (after deducting accumulated losses incurred in previous years), as determined in accordance with the applicable PRC accounting standards and regulations (the "PRC accounting standards"), to the Statutory Surplus Reserve (the "SSR") until such reserve reaches 50% of the registered capital of the respective company. Subject to certain restrictions set out in the Company Law of the PRC and the articles of association, the SSR may be capitalised as share capital, provided that the remaining balance after the capitalisation is not less than 25% of the registered capital.

In accordance with the Company Law of the PRC, the Company and the subsidiary are required to transfer 5% to 10% of their profits after tax (after deducting accumulated losses incurred in previous years), as determined in accordance with the PRC accounting standards, to the statutory Public Welfare Fund (the "PWF") which is a non-distributable reserve other than in the event of liquidation of the Company or the subsidiary. The PWF must be used for capital expenditure on staff welfare facilities and these facilities remain as the property of the Company and the subsidiary.

The directors of Sino IC have proposed to transfer RMB93,000 and RMB47,000 to the SSR and the PWF, respectively (2004: RMB179,000 and RMB89,000, respectively). The transfers represent 10% and 5% of Sino IC's profit after tax, respectively, as determined in accordance with the PRC accounting standards. The transfers have been incorporated in the financial statements.

At 31 December 2005, in accordance with the Company Law of the PRC, approximately RMB170,717,000 (2004: RMB170,717,000) standing to the credit of the Company's share premium account was available for distribution by way of future capitalisation issue.

According to the relevant regulations in the PRC, the amount of retained profits available for distribution is the lower of the amount determined under the PRC accounting standards and the amount determined under HKFRSs.

As the Company reported accumulated losses in the PRC statutory accounts, the Company had no reserve available for distribution as at 31 December 2005 and 2004.

26. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

Winding-up of an associate:

Net assets disposed of:

	2005 RMB'000
Cash and bank balances	241
Other receivables	250
	491
Group's share of net assets	241
Loss on disposal of the associate	–
Proceeds received in cash	241

As detailed in note 16, the Company's associate, Fu En, was liquidated during the year. This gave rise to the cash inflow of RMB241,000 during the year.

27. COMMITMENTS

The Group and the Company had the following commitments at the balance sheet date:

(a) Capital commitments

	Group		Company	
	2005 RMB'000	2004 RMB'000	**2005 RMB'000**	2004 RMB'000
Contracted, but not provided for:				
Land and buildings	**150**	–	**150**	–
Plant and machinery	**20**	590	**20**	590
	170	590	**170**	590

27. COMMITMENTS *(Continued)*

(b) The Group leases certain of its office properties under operating lease arrangements. Leases for properties are negotiated for terms of one to three years.

At 31 December 2005, the Group and the Company had total future minimum lease payments under non-cancellable operating leases falling due as follows:

	Group		Company	
	2005	2004	**2005**	2004
	RMB'000	RMB'000	**RMB'000**	RMB'000
Within one year	**1,362**	922	**501**	198
In the second to fifth years, inclusive	**1,367**	80	**62**	28
	2,729	1,002	**563**	226

28. RELATED PARTY TRANSACTIONS

(a) In addition to the transaction and balances detailed elsewhere in these financial statements, the Group had the following material transaction with the related party during the year:

Name of related party	**Relationship with the Group**	**Nature of transaction**	**2005**	2004
			RMB'000	RMB'000
Shanghai Fudan University ("SFU")	Owner of Fudan High Tech Company	Technical and equipment support fee	**–**	255

On 8 March 2000, the Company and SFU entered into an agreement ("the Agreement") under which the Company was required to pay a fee of RMB800,000 to SFU per annum for the provision of technical and equipment support.

On 12 August 2003, the Company and SFU entered into an agreement to terminate the Agreement and with effect from 1 January 2004 onwards, all technical and equipment support service provided by SFU will be charged based on a price mutually agreed by the two parties.

28. RELATED PARTY TRANSACTIONS *(Continued)*

(b) In 2004, the Group disposed of its 20% equity interest in Shanghai Fudan Communication Co., Ltd., an associate of the Group to Shanghai Investment Enterprise Holdings Limited ("SCIE") at a cash consideration of RMB6,000,000. SCIE is 90% held by Shanghai Commerce and Invest (Group) Corporation, a substantial shareholder of the Company.

In the opinion of the independent non-executive directions, the above related party transactions were entered into in the ordinary course of the Group's business and were in accordance with the terms of the arrangements governing the transactions.

29. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments comprise cash and short term deposits. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets and liabilities such as trade and bills receivables, prepayments, deposits and other receivables, trade and bills payables and other payables and accruals, which arise directly from its operations.

It is, and has been, throughout the year under review, the Group's policy that no trading in financial instruments shall be undertaken.

The main risks arising from the Group's financial instruments are foreign currency risk and credit risk. The board reviews and agrees policies for managing each of these risks and they are summarised below.

Foreign currency risk

The Group has transactional currency exposures. Such exposures arise from sales or purchases by operating units in currencies other than the units' functional currency. Approximately 38% (2004: 16%) of the Group's sales are denominated in currencies other than the functional currency of the operating units making the sale, whilst almost 60% (2004: 87%) of costs are denominated in the unit's functional currency. It is the Group's policy not to enter into forward contracts until a firm commitment is in place.

Credit risk

The Group's sales are made to several major customers and there is concentration of credit risks. The Group seeks to maintain strict control over its outstanding receivables and closely monitor the collection to minimise credit risk. The Group trades only with recognised and creditworthy third parties. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis and the Group's exposure to bad debts is not significant. For transactions that are not denominated in the functional currency of the relevant operating unit, the Group does not offer credit terms without the specific approval of the management.

29. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

Credit risk *(Continued)*

The credit risk of the Group's other financial assets, which comprise cash and cash equivalents and available-for-sale equity investments, arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments.

Since the Group trades only with recognised and creditworthy third parties, there is no requirement for collateral.

Fair value

The fair values of cash and short term deposits, trade and bills receivables, prepayments, deposits and other receivables, trade and bills payable and other payables and accruals are not materially different from their carrying amounts.

Fair value estimates are made at a specific point in time and are based on relevant market information and information about the financial instruments. These estimates are subjective in nature and involved uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

30. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 21 March 2006.

Five Year Financial Summary

A summary of the results and of the assets, liabilities and minority interests of the Group for the last five financial years, as extracted from the published audited financial statements, is set out below.

	Year ended 31 December				
	2005	2004	2003	2002	2001
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
RESULTS					
REVENUE	**211,211**	132,710	97,456	62,003	44,133
Cost of sales	**(157,393)**	(85,386)	(62,938)	(44,173)	(33,330)
Gross profit	**53,818**	47,324	34,518	17,830	10,803
Other income and gains	**7,341**	6,860	2,907	2,946	7,086
Selling and distribution costs	**(7,914)**	(6,292)	(5,875)	(4,170)	(3,608)
Administrative expenses	**(22,795)**	(19,010)	(17,512)	(13,876)	(10,361)
Other operating expenses	**(20,788)**	(20,491)	(15,092)	(7,504)	(4,976)
Share of losses of associates	**–**	(835)	(5,228)	(2,637)	–
PROFIT/(LOSS) BEFORE TAX	**9,662**	7,556	(6,282)	(7,411)	(1,056)
Tax	**(1,272)**	(57)	(72)	96	(402)
PROFIT/(LOSS) FOR THE YEAR	**8,390**	7,499	(6,354)	(7,315)	(1,458)
Attributable to:					
Equity holders of the parent	**8,037**	7,239	(6,550)	(7,135)	(1,362)
Minority interests	**353**	260	196	(180)	(96)
	8,390	7,499	(6,354)	(7,315)	(1,458)
ASSETS, LIABILITIES AND MINORITY INTERESTS					
TOTAL ASSETS	**331,516**	269,104	242,636	242,116	133,381
TOTAL LIABILITIES	**(92,849)**	(41,160)	(22,675)	(15,836)	(10,688)
MINORITY INTERESTS	**(4,115)**	(1,179)	(419)	(224)	(404)
	234,552	226,765	219,542	226,056	122,289