



To the members

Fairyoung Holdings Limited

(Incorporated in Bermuda with limited liability)

We have audited the financial statements on pages 20 to 62 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Company's directors are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

BASIS OF OPINION

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

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 our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. However, the evidence available to us was limited as follows:

1. Scope limitation - Provision against long term deposits

Included in the consolidated profit and loss account for the year ended 31st December, 2000 is a provision of HK\$67 million made against certain long term deposits (the "Deposits"). As more fully explained in note 18 to the financial statements, the Deposits were remitted by the Group to certain companies established in Mainland China in 1998 and were intended to be used to finance future investment projects of the Group. The Deposits are refundable and the recoverability thereof has been guaranteed by a former chairman and director of the Company. To date, neither the intended investment projects have crystallised, nor have the Deposits been refunded and a full provision has been made by the Group during the year. However, we were unable to obtain sufficient information to assess the recoverability of the Deposits and to satisfy ourselves as to whether the provision made is appropriate. Any adjustment to the provision would have a consequential impact on the Company's and the Group's net assets as at 31st December, 2000 and the Group's loss for the year then ended.

Report of the Auditors

BASIS OF OPINION *(continued)*

2. Scope limitation - Completeness of books and records for review of subsequent events

Certain of the underlying books and records of the Group have not been fully updated subsequent to the balance sheet date and we have not been able to obtain access to all the records required for us to carry out the necessary audit procedures to complete our review of subsequent events from the balance sheet date up to the date of this report. Such procedures might have resulted in the identification of adjustments to the amounts reported in and/or disclosed as notes to the financial statements. Furthermore, the scope of our work in assessing the appropriateness of preparing the financial statements on a going concern basis was consequentially limited because we have been unable to determine as to whether management's plans to address the going concern issue (such as we have been able to identify or otherwise determine such) are based on complete information about the Group's current financial position and, therefore, are adequate.

3. Scope limitation - Fundamental uncertainty - Going concern basis of the Group

In forming our opinion, we have considered the adequacy of the disclosures made in the financial statements concerning the basis of their preparation by the directors. As more fully explained in note 1 to the financial statements, the Group's financial statements have been prepared on a going concern basis, the validity of which is dependent upon the successful outcome of the measures currently being undertaken by the directors to ensure that adequate cash resources are available to the Group to enable it to meet its future working capital and financial requirements. The financial statements do not include any adjustments that would result from the failure of such measures.

In determining the appropriateness of adopting the going concern basis of presentation, we have only been provided with detailed projections and information for the period up to 31st December, 2001. We consider this insufficient for the purposes of forming our opinion. Furthermore, as explained in paragraph 2 above, we have been unable to determine as to whether management's plans to address the going concern issue as provided to us are based on complete information about the Group's current financial position and, therefore, are adequate. Accordingly, we have disclaimed our opinion in this respect.

DISCLAIMER OF OPINION

On account of the significance of each of (a) the fundamental uncertainty relating to the going concern basis; and (b) the possible effects of the limitation in evidence available to us as set out in paragraph 2 in the basis of opinion section of this report, we are unable to form an opinion as to whether the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31st December, 2000 and of the loss and cash flows of the Group for the year then ended and as to whether the financial statements have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Had we not disclaimed our opinion in respect of the matters described above, we would otherwise have qualified our opinion in respect of the limitation in evidence relating to the provision against the long term deposits set out in paragraph 1 in the basis of opinion section of this report.

In respect alone of the limitations on our work as set out in the basis of opinion section of this report:

- (i) we have not obtained all the information and explanations that we considered necessary for the purpose of our audit; and
- (ii) we were unable to determine whether proper books of account had been kept.

Ernst & Young
Certified Public Accountants

Hong Kong
30th October, 2001