

Chairman's Statement and Management Discussion and Analysis

I am pleased to report the activities of the Group for the year 2001.

REVIEW

The Group recorded turnover and loss attributable to shareholders of HK\$2.1 billion and HK\$187 million for the year ended 31 December 2001. Turnover reduced by 16% and loss rose by 1.7 times as compared to previous year. The Group encountered major challenges in the declining economic environment both locally and globally in the year 2001. As a result of the massive contraction in the turnover of Hong Kong stock market, commission income from securities brokerage and interest income from share margin financing dropped. Sales from the trading and manufacturing operations further deteriorated, toys manufacturing income was down severely as a result of reduced demand from the US market and advertising revenue fell in the consolidating advertising market. Overall within the Group considerable provisions on revaluation of investment properties and doubtful debts were made.

Brokerage and Financial Services

The total turnover of the Group's financial arm, South China Brokerage ("SCB") group, reduced by half when compared to prior year. Commission income from securities and commodities broking fell significantly and interest income from share margin operations and bank deposits dropped. This adverse result was however, partially set off by the encouraging improvement in the personal loan business. Revenue from personal loan business rose satisfactorily resulting from a four times expansion in the loan portfolio. With attractive commission incentive offered to online clients, turnover from online securities trading picked up gradually during the year. By the end of 2001, it contributed approximately 10% of the average daily turnover of SCB group. SCB recorded HK\$20.0 million net profit for the year 2001, a 15.3% reduction compared to last year.

Trading and Manufacturing

South China Industries ("SCI") group's performance suffered a serious set back in the year 2001. Its net result dived to a loss of HK\$137 million, the first year of recording net loss since its incorporation. SCI was adversely affected by the disappointing result of its major subsidiary, Wah Shing International Holdings Limited ("Wah Shing Toys") which was due to the slowdown of the US economy that slackened its customer demand but combined with high material and logistics costs. Keen competition from other manufacturers further drove down profit margin. The reason for the exceptional loss this year was a one-off restructuring cost of HK\$17.7 million and a tax provision of HK\$32.6 million for settlement with the Hong Kong Inland Revenue Department on its transfer pricing policy for prior years.

SCI's electronics operations, Wah Shing Electronic Company Limited ("Wah Shing Electronic"), reported satisfactory net profit of HK\$16.3 million, benefiting from its competitive edge on toy production technology and manufacturing process. The associate, Nority International Group Limited ("Nority"), which engages in manufacturing of shoes, turned around from loss to a profit attributable to shareholders of HK\$16.6 million, as a result of effective cost control.

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Information and Technology

SCIT group recorded a surge in turnover of 77% to HK\$112.6 million for the year ended 31 December 2001, of which 97% was attributable to information technology ("IT") and related businesses.

Property Development and Investment

A full marketing scheme has been launching since July 2001 after the property development project, "The Centrium", a Grade A commercial/office building at Arbuthnot Road/ Wyndham Street in Central district obtained the official occupation permit on 29 June 2001. At present, all of the ground floor shops and around 25% of the total office areas have been leased out.

As a result of the declining property market, the Group has made HK\$35.2 million provisions on investment in property projects, HK\$3.4 million deficit on property revaluation and HK\$40.3 million on self-use properties, fixed assets and land pending for development.

Travel and Related Services

During the year, the Group disposed of all its equity interest in Fourseas.com Limited ("Fourseas"). However, the Group still maintained its participation in the travel and related businesses by acquiring 49% equity interest in Fourseas' travel business subsidiaries.

Media and Publications

During the first six months of 2001, South China Media's 12 magazines experienced mild growth in both circulation and advertising. The event of September 11th and Hong Kong's weak economy, led to sudden slashes in advertising budgets, and circulation income suffered from falling consumer spending. Mature titles continued to be profitable. Foreseeing extremely difficult times ahead, a series of cost-cutting exercises were undertaken to reduce overall costs to more competitive levels, and focus was put on improving the editorial contents of our titles to strengthen reader loyalty.

Other Investments in the PRC

By the end of 2001 the Group had planted over 500,000 lychee trees in total covering a land area of approximately 22,000 mu and are making it one of the largest famous farms in the PRC. The pharmaceutical joint venture in Shenyang started its expansion plan, which involves relocating the production site to the high technology zone where it will increase its production capacity by two to three fold. Its research and development teams made satisfactory progress and two brand new products obtained the Certificate of New Medicine from the State Drug Administration of the PRC.

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FINANCIAL RESOURCES AND GEARING RATIO

As at 31 December 2001, the Group had a current ratio of 1.09 and a gearing ratio (long-term liabilities of approximately HK\$178 million to equity of approximately HK\$767 million) of 0.23. The Group's operations continue to be financed by internal resources and bank borrowings.

CAPITAL STRUCTURE

In August 2001, a share subdivision proposal for all the ordinary shares of the Company was approved at an extraordinary general meeting of shareholders. Each of the ordinary shares of HK\$0.10 each in the share capital of the Company was subdivided into four ordinary shares of HK\$0.025 each.

During the year, the Company issued 750,624 ordinary shares upon exercise of warrants. All outstanding warrants of the Company had expired on 22 November 2001.

Apart from the above, the Group had no debt securities or other capital instruments as at 31 December 2001.

EXPOSURE TO FLUCTUATION IN EXCHANGE RATES AND RELATED HEDGES

As at 31 December, 2001, the Group had no exposure to fluctuation in exchange rates and any related hedges.

MATERIAL ACQUISITIONS AND DISPOSALS OF SUBSIDIARIES AND ASSOCIATES

In September 2001, Fourseas.com Limited ("Fourseas"), a former associate of the Group, completed its group's financial restructuring. The Group disposed all of its equity interest in Fourseas, while acquiring its entire property portfolio together with the related mortgages and 49% of its travel related businesses of Fourseas for a consideration of HK\$15 million. The Group received HK\$70 million as repayment of shareholder loan from Fourseas in its financial restructuring.

CHARGES ON GROUP ASSETS

Fixed assets, properties under development and investment properties of net book values of approximately HK\$180 million, HK\$18 million and HK\$172 million respectively were pledged as collateral for the Group's banking facilities.

STAFF

Total number of staff as at 31 December 2001 was approximately 21,000.

The Group considers its staff as its most valuable asset. In addition to salary, other fringe benefits such as medical subsidies, life insurance, provident fund and subsidised training programmes are offered to all staff members of the Group. Performance of the staff is normally reviewed on an annual basis with adjustment compatible to the market. Individual staff may also receive a discretionary bonus at the end of each year based on performance. Share options have also been granted to certain employees of the Group.

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OUTLOOK

Brokerage and Financial Services

SCB intends to offer clients more trading products like bullion, global futures and US securities and enhancing online trading platform for the expected extension of trading hours. Sales and investment trainee programs will continue to be developed for maintaining a pool of front office resources to provide quality client services. Business in the professional advisory services increased due to more companies in the PRC getting listed in Hong Kong or acquiring interests in Hong Kong companies. The personal loan portfolio continues to expand cautiously in the year 2002. Other related personal financing products and diversification opportunities will be explored.

Trading and Manufacturing

To achieve greater profitability, Wah Shing Toys is further streamlining or scaling down some of its production facilities to reduce overhead costs. The relocation of its main operations and functions to Shenzhen, the PRC will be accelerated to improve communication effectiveness and operational efficiency. Focus will be made on striking a better balance by obtaining more orders of conventional products that have a steady demand throughout the year and lower material costs. All these efforts should be seen in the year 2002.

Wah Shing Electronics is tightening cost control measures and upgrading manufacturing process to optimize and maintain its profit margins. Nority is endeavouring to seek further business development an opportunities in China through studies and market researches so as to open itself to the great market potential following China's accession to the World Trade Organisation ("WTO"). It is setting up a new company in the PRC as a foothold for its future business development.

Information and Technology

SCIT has a fine and dedicated team of employees, advanced technologies, and the resources to meet the challenges and tackle the difficulties. Thus, we feel that we are fully prepared to focus on our mission of providing leading edge, best-of-class, highest quality services to our customers in both Hong Kong and the PRC.

Property Development and Investment

Given the present stagnant property market, the leasing progress of the Grade A commercial/office building at Central, The Centrium is presently slow. The situation is anticipated to prevail until the local property market and the overall economic environment improve. Some of the existing investment properties with poor occupancy are being or will be renovated to improve leasing income.

Travel and Related Services

In view of China's accession to the WTO and the future hosting of the Olympic Games in the years to come, we believe that the Greater China area is now experiencing a continuous growth in the business and leisure travel industry. More marketing and support staff are being employed to cope with this rapidly expanding market.

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Media and Publications

Advertising revenue is expected to be weak for the first half of the year 2002, as advertisers continue to consolidate and cut spending in media. However, we expect the overall advertising market to see improvement during the year and we are making the necessary adjustments to grow our advertising income. We will continue to aggressively but prudently position and define our titles in this competitive market environment, to gain market share and improve advertising revenues. We will also place efforts in developing our magazines in the China publications market while maintaining cost efficiencies and fortifying our base in Hong Kong.

Other Investments in the PRC

The Group aims to make its fruit farms more efficient and improve the yield as well as the business logistics for fruits distribution and marketing. In February 2002, the Group entered into an agreement to set up a joint venture to farm hairy crabs in the Nanjing area.

In February 2002, the shares of Jinchang Pharmaceutical Holdings Limited comprising the pharmaceutical joint venture in Shenyang and Capital Publications Limited which publishes "Capital" magazine were distributed in specie to shareholders. The distribution will enable the shareholders to hold a direct investment and also participate in the future development of these two companies. Moreover, it is expected further such distributions will be made during the year.

Overview

The Group's businesses are well placed to benefit from an expected upturn in Hong Kong's economy especially following our substantial cuts in overheads and restructuring of some non-performing operations. The travel and related services business has already turned into profit in the first quarter and already other major operating units are performing better. It is expected that certain non-strategic investments will be disposed of during the year.

APPRECIATION

On behalf of the Board, I wish to express my gratitude to our customers and shareholders for their continued support and all our staff members for their hard work and dedicated service.

On behalf of the Board
Ng Hung Sang, Robert
Chairman

Hong Kong Special Administrative Region of the People's Republic of China
24 April 2002