1 SIGNIFICANT ACCOUNTING POLICIES

(a) Statement of compliance

These financial statements have been prepared in accordance with all applicable Statements of Standard Accounting Practice and Interpretations issued by the Hong Kong Society of Accountants ("HKSA"), accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. These financial statements also comply with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited. A summary of the significant accounting policies adopted by the Group is set out below.

(b) Basis of preparation of the financial statements

The measurement basis used in the preparation of the financial statements is historical cost modified by the revaluation of investment properties and land and buildings as explained in the accounting policies set out below.

The Company and the Group had net current liabilities as at 31 December 2001 and sustained substantial losses for the year then ended. In addition, subsequent to the year end, convertible noteholders have demanded early redemption of the US dollar convertible notes of $70.2 million, details of which are set out in note 22. Notwithstanding the foregoing, the directors of the Company are of the opinion that the Company and the Group are able to continue as going concerns and to meet their obligations as and when they fall due after taking into account the following:

(i) loan facilities totalling $200 million made available to the Company from a financial institution; and

(ii) continuing financial support received from the ultimate holding company.

The directors believe that the Group will have sufficient cash resources to satisfy its future working capital and other financing requirements. Accordingly, it is appropriate that these financial statements should be prepared on a going concern basis and do not include any adjustments that would be required should the Company and the Group be unable to continue as going concerns.

The auditors have referred to this matter as a fundamental uncertainty in their audit report, however, their opinion is not qualified in this respect.

1 SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(c) Subsidiaries

A subsidiary is an enterprise controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities.

An investment in a subsidiary is consolidated into the consolidated financial statements, unless it is acquired and held exclusively with a view to subsequent disposal in the near future or operates under severe long-term restrictions which significantly impair its ability to transfer funds to the Group, in which case, it is stated in the consolidated balance sheet at fair value with changes in fair value recognised in the consolidated profit and loss account as they arise.

Intra-group balances and transactions, and any unrealised profits arising from intra-group transactions, are eliminated in full in preparing the consolidated financial statements. Unrealised losses resulting from intra-group transactions are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

In the Company's balance sheet, an investment in a subsidiary is stated at cost less any impairment losses (see note 1(i)), unless it is acquired and held exclusively with a view to subsequent disposal in the near future or operates under severe long-term restrictions which significantly impair its ability to transfer funds to the Company, in which case, it is stated at fair value with changes in fair value recognised in the profit and loss account as they arise.

(d) Associates

An associate is an entity in which the Group or the Company has significant influence, but not control or joint control, over its management, including participation in the financial and operating policy decisions.

An investment in an associate is accounted for in the consolidated financial statements under the equity method and is initially recorded at cost and adjusted thereafter for the post-acquisition change in the Group's share of the associate's net assets, unless it is acquired and held exclusively with a view to subsequent disposal in the near future or operates under severe long-term restrictions that significantly impair its ability to transfer funds to the investor, in which case it is stated at fair value with changes in fair value recognised in the consolidated profit and loss account as they arise. The consolidated profit and loss account reflects the Group's share of the post-acquisition results of the associates for the year, including any amortisation of positive or negative goodwill charged or credited during the year in accordance with note 1(e).

Unrealised profits and losses resulting from transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associate, except where unrealised losses provide evidence of an impairment of the asset transferred, in which case they are recognised immediately in the consolidated profit and loss account.

1 SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(d) Associates *(continued)*

In the Company's balance sheet, its investments in associates are stated at cost less impairment losses (see note 1(i)), unless it is acquired and held exclusively with a view to subsequent disposal in the near future or operates under severe long-term restrictions that significantly impair its ability to transfer funds to the investor, in which case, it is stated at fair value with changes in fair value recognised in the profit and loss account as they arise.

(e) Goodwill

Positive goodwill arising on consolidation represents the excess of the cost of the acquisition over the Group's share of the fair value of the identifiable assets and liabilities acquired. In respect of subsidiaries:

– for acquisitions before 1 January 2001, positive goodwill is eliminated against reserves and is reduced by impairment losses (see note 1(i)); and

– for acquisitions on or after 1 January 2001, positive goodwill is amortised to the consolidated profit and loss account on a straight-line basis over its estimated useful life. Positive goodwill is stated in the consolidated balance sheet at cost less any accumulated amortisation and any impairment losses (see note 1(i)).

In respect of acquisitions of associates, positive goodwill is amortised to the consolidated profit and loss account on a straight-line basis over its estimated useful life. The cost of positive goodwill less any accumulated amortisation and any impairment losses (see note 1(i)) is included in the carrying amount of the interest in associates.

On disposal of a subsidiary or an associate during the year, any attributable amount of purchased goodwill not previously amortised through the consolidated profit and loss account or which has previously been dealt with as a movement on group reserves is included in the calculation of the profit or loss on disposal.

(f) Fixed assets

(i) Fixed assets are stated in the balance sheet on the following bases:

– investment properties with an unexpired lease term of more than 20 years are stated in the balance sheet at their open market value which is assessed annually by external qualified valuers;

– land and buildings held for own use are stated in the balance sheet at their revalued amount, being their open market value at the date of revaluation less any subsequent accumulated depreciation (see note 1(h)). Revaluations are performed by qualified valuers with sufficient regularity to ensure that the carrying amount of these assets does not differ materially from that which would be determined using fair values at the balance sheet date; and

1 SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(f) Fixed assets *(continued)*

– plant, machinery and other fixed assets are stated in the balance sheet at cost less accumulated depreciation (see note 1(h)) and impairment losses (see note 1(i)).

(ii) Changes arising on the revaluation of investment properties and land and buildings held for own use are generally dealt with in reserves. The only exceptions are as follows:

– when a deficit arises on revaluation, it will be charged to the profit and loss account, if and to the extent that it exceeds the amount held in the reserve in respect of that same asset, or, solely in the case of investment properties, the portfolio of investment properties, immediately prior to the revaluation; and

– when a surplus arises on revaluation, it will be credited to the profit and loss account, if and to the extent that a deficit on revaluation in respect of that same asset, or, solely in the case of investment properties, the portfolio of investment properties, had previously been charged to the profit and loss account.

(iii) Subsequent expenditure relating to a fixed asset that has already been recognised is added to the carrying amount of the asset when it is probable that future economic benefits, in excess of the originally assessed standard of performance of the existing asset, will flow to the Group. All other subsequent expenditure is recognised as an expense in the period in which it is incurred.

(iv) Gains or losses arising from the retirement or disposal of a fixed asset are determined as the difference between the estimated net disposal proceeds and the carrying amount of the asset and are recognised in the profit and loss account on the date of retirement or disposal.

1 SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(g) Leased assets

Leases of assets under which the lessee assumes substantially all the risks and benefits of ownership are classified as finance leases. Leases of assets under which the lessor has not transferred all the risks and benefits of ownership are classified as operating leases.

(i) Assets acquired under finance leases

Where the Group acquires the use of assets under finance leases, the amounts representing the fair value of the leased asset, or, if lower, the present value of the minimum lease payments, of such assets are included in fixed assets and the corresponding liabilities, net of finance charges, are recorded as obligations under finance leases. Depreciation is provided at rates which write off the cost of the assets in equal annual amounts over the term of the relevant lease or, where it is likely the Group will obtain ownership of the asset, the life of the asset, as set out in note 1(h). Impairment losses are accounted for in accordance with the accounting policy as set out in note 1(i). Finance charges implicit in the lease payments are charged to the profit and loss account over the period of the leases so as to produce an approximately constant periodic rate of charge on the remaining balance of the obligations for each accounting period. Contingent rentals are written off as an expense of the accounting period in which they are incurred.

(ii) Operating lease charges

Where the Group has the use of assets under operating leases, payments made under the leases are charged to the profit and loss account in equal instalments over the accounting periods covered by the lease term, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased asset. Lease incentives received are recognised in the profit and loss account as an integral part of the aggregate net lease payments made. Contingent rentals are charged to the profit and loss account in the accounting period in which they are incurred.

(h) Amortisation and depreciation

(i) No depreciation is provided on investment properties with an unexpired lease term of over 20 years.

(ii) Depreciation is calculated to write off the cost or valuation of other fixed assets over their estimated useful lives as follows:

– leasehold land is depreciated on a straight-line basis over the remaining term of the lease;

– buildings are depreciated on a straight-line basis over the shorter of their estimated useful lives, being 30 years from the date of completion, and the unexpired terms of the leases; and

1 **SIGNIFICANT ACCOUNTING POLICIES** *(continued)*

(h) Amortisation and depreciation *(continued)*

– other fixed assets are depreciated on a straight-line basis over their estimated useful lives as follows:

Leasehold improvements	over the unexpired term of the lease
Machinery and equipment	3 – 10 years
Furniture, fixtures, office equipment and motor vehicles	1 – 10 years
Moulds and tools	2 – 10 years

(i) Impairment of assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired or an impairment loss previously recognised no longer exists or may have decreased:

– property, plant and equipment (other than properties carried at revalued amounts);

– investments in subsidiaries and associates (except for those accounted for at fair value under notes 1(c) & (d); and

– positive goodwill (whether taken initially to reserves or recognised as an asset).

If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset exceeds its recoverable amount.

(i) Calculation of recoverable amount

The recoverable amount of an asset is the greater of its net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

(ii) Reversals of impairment losses

In respect of assets other than goodwill, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss in respect of goodwill is reversed only if the loss was caused by a specific external event of an exceptional nature that is not expected to recur, and the increase in recoverable amount relates clearly to the reversal of the effect of that specific event.

A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. Reversals of impairment losses are credited to the profit and loss account in the year in which the reversals are recognised.

1 **SIGNIFICANT ACCOUNTING POLICIES** *(continued)*

(j) Revenue recognition

Provided it is probable that the economic benefits will flow to the Group and the revenue and costs, if applicable, can be measured reliably, revenue is recognised in the profit and loss account as follows:

(i) Sale of goods

Revenue is recognised when goods are delivered at the customers' premises which is taken to be the point in time when the customer has accepted the goods and the related risks and rewards of ownership. Revenue excludes value added or other sales taxes and is after deduction of any trade discounts.

(ii) Internet-related services income

Income from Internet-related services is recognised over the period during which the services are rendered to customers.

(iii) Interest income

Interest income from bank deposits is accrued on a time-apportioned basis by reference to the principal outstanding and at the rate applicable.

(k) Inventories

Inventories are carried at the lower of cost and net realisable value.

Cost is calculated using the first-in, first-out cost formula and comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

When inventories are sold, the carrying amount of those inventories is recognised as an expense in the period in which the related revenue is recognised. The amount of any write-down of inventories to net realisable value and all losses of inventories are recognised as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realisable value, is recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

(l) Deferred taxation

Deferred taxation is provided using the liability method in respect of the taxation effect arising from all material timing differences between the accounting and tax treatment of income and expenditure, which are expected with reasonable probability to crystallise in the foreseeable future.

Future deferred tax benefits are not recognised unless their realisation is assured beyond reasonable doubt.

1 SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(m) Translation of foreign currencies

Foreign currency transactions during the year are translated into Hong Kong dollars at the exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated into Hong Kong dollars at the exchange rates ruling at the balance sheet date. Exchange gains and losses are dealt with in the profit and loss account.

The results and balance sheet items of enterprises outside Hong Kong are translated into Hong Kong dollars at the rates of exchange ruling at the balance sheet date. The resulting exchange differences are dealt with as a movement in reserves.

On disposal of an enterprise outside Hong Kong, the cumulative amount of the exchange differences which relate to that enterprise is included in the calculation of the profit or loss on disposal.

(n) Retirement costs

Contributions to the Mandatory Provident Funds as required under the Hong Kong Mandatory Provident Fund Schemes Ordinance in respect of employees in Hong Kong are charged to the profit and loss account when incurred.

Subsidiaries incorporated in the People's Republic of China ("PRC") participate in the retirement schemes organised by the local authorities for employees in the PRC. The subsidiaries are required to contribute, based on a certain percentage of the basic payroll, to the retirement schemes to fund the benefits. The only obligation of the Group with respect to the retirement schemes is to make the required contributions under the schemes. Such contributions are charged to the profit and loss account when incurred.

(o) Borrowing costs

Borrowing costs are expensed in the profit and loss account in the period in which they are incurred.

(p) Related parties

For the purposes of these financial statements, parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence. Related parties may be individuals or other entities.

(q) Cash equivalents

Cash equivalents are short-term, highly liquid investments which are readily convertible into known amounts of cash without notice and which were within three months of maturity when acquired. For the purposes of the cash flow statement, cash equivalents would also include bank overdrafts and advances from banks repayable within three months from the date of the advance.

1 SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(r) Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

In accordance with the Group's internal financial reporting, the Group has chosen business segment information as the primary reporting format and geographical segment information as the secondary reporting format.

Segment revenue, expenses, results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis to that segment. Segment revenue, expenses, assets and liabilities are determined before intra-group balances and intra-group transactions are eliminated as part of the consolidation process, except to the extent that such intra-group balances and transactions are between group enterprises within a single segment. Inter-segment pricing is based on similar terms as those available to other external parties.

Segment capital expenditure is the total cost incurred during the period to acquire segment assets (both tangible and intangible) that are expected to be used for more than one period.

Unallocated items mainly comprise financial and corporate assets, interest-bearing loans, borrowings, corporate and financing expenses and minority interests.

2 TURNOVER

The principal activity of the Company is investment holding. The principal activities of the Group are the manufacture and sale of healthcare and household products, provision of Internet-related services and the development and sale of enterprise applications software.

Turnover represents the aggregate of sales value of goods supplied to customers less goods returned, trade discounts and business tax, and revenue from the provision of Internet-related services less business tax. The amount of each significant category of revenue recognised in turnover during the year is as follows:

	2001	2000
	$'000	*$'000*
Manufacture and sale of healthcare and household products	**92,503**	77,531
Provision of Internet-related services	**29,185**	6,300
Sale of enterprise applications software *(note 14)*	**2,746**	–
	124,434	83,831

3 OTHER REVENUE AND OTHER NET INCOME

	2001 $'000	2000 $'000
Other revenue		
Interest income	8,076	3,474
Income from scrap sales	4,799	3,494
Rental income	319	528
Consultancy income	–	3,801
	13,194	11,297
Other net income		
Loss on disposal of fixed assets	(555)	(3,299)
Gain on settlement of amount due to a former director *(note 29(c))*	1,138	–
Profit on disposal of a subsidiary *(note 14)*	2,125	–
Exchange gain	289	468
Others	1,260	3,508
	4,257	677

4 LOSS FROM ORDINARY ACTIVITIES BEFORE TAXATION

Loss from ordinary activities before taxation is arrived at after charging:

		2001 $'000	2000 $'000
(a)	Finance costs:		
	Interest on bank advances and other borrowings repayable within five years	**10,272**	4,519
	Interest on other loans	**227**	717
	Finance charges on obligations under finance leases	**33**	191
		10,532	5,427
(b)	Other items:		
	Cost of inventories #	**84,114**	71,806
	Staff costs (including retirement costs of $917,000 (2000: $243,000)) #/*	**34,091**	32,047
	Amortisation of positive goodwill	**4,778**	–
	Auditors' remuneration	**982**	904
	Research and development costs *	**2,639**	6,555
	Depreciation #		
	– owned assets	**18,895**	7,562
	– assets held under finance leases	**547**	1,325
	Operating lease charges		
	– land and buildings	**6,198**	2,091
	Impairment loss on fixed assets	**21,000**	–
	Fixed assets written off	**8,769**	3,493
	Other assets written off	**1,053**	1,576
	Provision for bad and doubtful debts	**4,105**	4,899

\# *Cost of inventories includes $13,894,000 (2000: $14,755,000) relating to staff costs and depreciation expenses, which amount is also included in the respective total amounts disclosed separately above for each of these types of expenses.*

* *Research and development costs include $2,189,000 (2000: $1,620,000) relating to staff costs which amount is also included in staff costs disclosed separately above.*

5 TAXATION

(a) Taxation in the consolidated profit and loss account represents:

	2001 $'000	2000 $'000
Underprovision for Hong Kong Profits Tax in respect of prior years	**–**	1,330

No provision for Hong Kong Profits Tax and PRC income tax has been made in the financial statements as the Company and the Group did not generate any assessable profits for taxation purposes during the year.

The provision for Hong Kong Profits Tax is calculated at 16% of the estimated assessable profits for the year ended 31 December 2000.

(b) Taxation in the consolidated balance sheet represents:

	2001 $'000	2000 $'000
Balance of Profits Tax provisions relating to prior years	**2,309**	979
Underprovision for Hong Kong Profits Tax relating to prior years	**–**	1,330
	2,309	2,309
Less: Tax Reserve Certificates	**(920)**	–
	1,389	2,309
Balance of provision for taxation outside Hong Kong relating to prior years	**3,663**	3,660
	5,052	5,969

As at 31 December 2001, Tax Reserve Certificates totalling $920,000 were purchased by a subsidiary pending the agreement with the Hong Kong Inland Revenue Department ("IRD") of the offshore claim in relation to the Group's manufacturing operations for the years of assessment 1994/95 to date. The directors have made provisions which they consider to be adequate after taking into account the enquiries raised by the IRD and the bases adopted in preparing the Profits Tax returns in prior years.

Taxation for subsidiaries outside Hong Kong is charged at the appropriate current rates of taxation ruling in the relevant countries in which the subsidiaries operate.

5 TAXATION *(continued)*

(c) No deferred tax benefits have been recognised as their realisation is not assured beyond reasonable doubt. Major components of unprovided deferred tax by the Company and the Group are set out below:

	The Group Potential assets/ (liabilities) unprovided		The Company Potential assets unprovided	
	2001	2000	**2001**	2000
	$'000	*$'000*	***$'000***	*$'000*
Tax losses	**18,194**	22,644	**3,651**	2,432
Depreciation allowances in excess of related depreciation	**(419)**	(1,255)	**–**	–
	17,775	21,389	**3,651**	2,432

6 DIRECTORS' REMUNERATION

Directors' remuneration disclosed pursuant to section 161 of the Hong Kong Companies Ordinance is as follows:

	2001	2000
	$'000	*$'000*
Fees	**480**	–
Salaries and other emoluments	**6,259**	5,459
Retirement scheme contributions	**113**	–
	6,852	5,459

Included in directors' remuneration were fees of $480,000 (2000: $Nil) payable to the independent non-executive directors during the year.

The remuneration of directors is within the following bands:

	Number of directors	
	2001	2000
Nil – $1,000,000	**5**	5
$1,000,001 – $1,500,000	**–**	1
$1,500,001 – $2,000,000	**1**	–
$2,000,001 – $2,500,000	**–**	1
$3,500,001 – $4,000,000	**1**	–

7 INDIVIDUALS WITH HIGHEST EMOLUMENTS

Of the five individuals with the highest emoluments, two (2000: two) are directors whose emoluments are disclosed in note 6. The aggregate of the emoluments in respect of the other three (2000: three) individuals are as follows:

	2001	2000
	$'000	*$'000*
Salaries and other emoluments	**3,592**	2,899
Retirement scheme contributions	**110**	–
	3,702	2,899

The emoluments of the three (2000: three) individuals with the highest emoluments are within the following bands:

	Number of individuals	
	2001	2000
$Nil – $1,000,000	**1**	2
$1,000,001 – $1,500,000	**1**	1
$1,500,001 – $2,000,000	**1**	–

8 LOSS ATTRIBUTABLE TO SHAREHOLDERS

The consolidated loss attributable to shareholders includes a loss of $1,218,395,000 (2000: $84,156,000) which has been dealt with in the financial statements of the Company.

9 LOSS PER SHARE

(a) Basic loss per share

The calculation of basic loss per share is based on the loss attributable to shareholders of $1,216,597,000 (2000: $58,816,000) and the weighted average number of ordinary shares of 1,144,932,671 (2000: 951,514,287) in issue during the year.

(b) Diluted loss per share

No diluted loss per share is presented as the inclusion of the Company's share options, warrants and convertible notes in issue during the year would have an anti-dilutive effect for both the current and prior years.

10 CHANGE IN ACCOUNTING POLICY

In prior years, positive goodwill arising on acquisition of subsidiaries was eliminated against reserves. With effect from 1 January 2001, in order to comply with Statement of Standard Accounting Practice 30 ("SSAP 30") issued by the HKSA, the Group adopted a new accounting policy for goodwill as set out in note 1(e).

The Group has taken advantage of the transitional provisions set out in paragraph 88 of SSAP 30 with the effect that the new accounting policy has been adopted prospectively and no adjustments have been made to the opening balance of accumulated losses and reserves and comparative information.

11 SEGMENT REPORTING

Segment information is presented in respect of the Group's business and geographical segments. Business segment information is chosen as the primary reporting format because this is more relevant to the Group's internal financial reporting.

Business segments

The Group comprises the following main business segments:

Healthcare and household products:	The manufacture and sale of healthcare and household products
Internet-related services:	The provision of Internet-related services
Enterprise applications software:	The development and sale of enterprise applications software

	2001	2000
	$'000	*$'000*
Revenue from external customers		
– Healthcare and household products	**92,503**	77,531
– Internet-related services	**29,185**	6,300
– Enterprise applications software	**2,746**	–
Total	**124,434**	83,831
Other revenue from external customers		
– Healthcare and household products	**5,118**	4,022
Total revenue	**129,552**	87,853

11 SEGMENT REPORTING *(continued)*

	2001 $'000	2000 $'000
Segment result		
– Healthcare and household products	**(7,730)**	(26,498)
– Internet-related services	**(1,173,173)**	(3,904)
– Enterprise applications software	**(5,874)**	–
– Unallocated operating income and expenses	**(22,987)**	(18,313)
Loss from operations	**(1,209,764)**	(48,715)
Finance cost	**(10,532)**	(5,427)
Share of profit less losses of associates		
– Healthcare and household products	**1,587**	–
– Internet-related services	**(3)**	(3,344)
	1,584	(3,344)
Loss from ordinary activities before taxation	**(1,218,712)**	(57,486)
Taxation	**–**	(1,330)
Minority interests	**2,115**	–
Loss attributable to shareholders	**(1,216,597)**	(58,816)
Depreciation and amortisation		
– Healthcare and household products	**8,484**	6,500
– Internet-related services	**9,259**	1,321
– Enterprise applications software	**4,854**	–
– Unallocated	**1,623**	1,066
	24,220	8,887
Impairment loss for the year		
– Internet-related services	**1,151,621**	–

11 SEGMENT REPORTING *(continued)*

	2001 $'000	2000 $'000
Significant non-cash expenses (other than depreciation and amortisation)		
– Healthcare and household products	**6,778**	16,150
– Internet-related services	**8,700**	349
Segment assets		
– Healthcare and household products	**39,669**	71,707
– Internet-related services	**166,878**	161,920
– Enterprise applications software	**46,141**	–
– Unallocated	**86,404**	151,158
Less: Inter-segment elimination	**(3,090)**	–
Total assets	**336,002**	384,785
Segment liabilities		
– Healthcare and household products	**15,691**	44,180
– Internet-related services	**10,751**	13,294
– Enterprise applications software	**5,656**	–
– Unallocated	**226,351**	223,295
Less: Inter-segment elimination	**(3,090)**	–
Total liabilities	**255,359**	280,769
Capital expenditure incurred during the year		
– Healthcare and household products	**1,803**	6,852
– Internet-related services	**1,747**	80,460
– Enterprise applications software	**2,881**	–
	6,431	87,312

11 SEGMENT REPORTING *(continued)*

Geographical segments

The Group's business is managed on a worldwide basis, but participates in four principal economic environments. North America and Europe are major markets for the sale of healthcare and household products; PRC is a major market for the Internet-related operations.

In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of customers. Segment assets and capital expenditure are based on the geographical location of the assets.

	2001 $'000	2000 $'000
Revenue from external customers		
– North America	65,633	42,138
– Europe	13,659	21,359
– PRC	31,931	6,300
– Asia (other than PRC) and others	13,211	14,034
Total	124,434	83,831
Segment assets		
– PRC	313,027	333,377
– Hong Kong	22,975	51,408
Total assets	336,002	384,785
Capital expenditure incurred during the year		
– PRC	5,737	79,752
– Hong Kong	694	7,560
	6,431	87,312

There is no major disparity in the ratios between turnover and loss in relation to the above geographical locations, hence no analysis is given of the contributions to loss from the above geographical locations.

12 FIXED ASSETS

(a) The Group

	Investment property $'000	Leasehold land and buildings $'000	Optical fibre cable $'000	Leasehold improve-ments $'000	Plant and machinery $'000	Furniture, fixtures, equipment and motor vehicles $'000	Moulds and tools $'000	Total $'000
Cost or valuation:								
At 1 January 2001	5,100	19,307	48,457	6,353	44,083	29,657	23,855	176,812
Exchange adjustments	–	181	–	39	377	138	197	932
Additions								
– through acquisition of subsidiary	–	–	–	144	93	2,397	–	2,634
– others	–	–	–	297	424	2,139	1,143	4,003
Disposals								
– through disposal of subsidiary	(5,100)	–	–	(294)	–	(86)	–	(5,480)
– others	–	–	–	(4,199)	(9,243)	(7,983)	(7,454)	(28,879)
Deficit on revaluation	–	(3,488)	–	–	–	–	–	(3,488)
At 31 December 2001	–	16,000	48,457	2,340	35,734	26,262	17,741	146,534
Representing:								
Cost	–	–	48,457	2,340	35,734	26,262	17,741	130,534
Valuation – 2001	–	16,000	–	–	–	–	–	16,000
	–	16,000	48,457	2,340	35,734	26,262	17,741	146,534
Accumulated depreciation:								
At 1 January 2001	–	229	–	1,398	16,798	15,478	18,057	51,960
Exchange adjustments	–	2	–	12	122	35	181	352
Through acquisition of subsidiary	–	–	–	22	10	414	–	446
Charge for the year	–	638	–	2,339	7,700	5,463	3,302	19,442
Impairment loss	–	–	21,000	–	–	–	–	21,000
Through disposal of subsidiary	–	–	–	–	–	(42)	–	(42)
Written back on disposal	–	–	–	(2,513)	(6,268)	(4,090)	(6,273)	(19,144)
Written back on revaluation	–	(869)	–	–	–	–	–	(869)
At 31 December 2001	–	–	21,000	1,258	18,362	17,258	15,267	73,145
Net book value:								
At 31 December 2001	–	16,000	27,457	1,082	17,372	9,004	2,474	73,389
At 31 December 2000	5,100	19,078	48,457	4,955	27,285	14,179	5,798	124,852

During the year, the Group carried out a review of the carrying value of the optical fibre cable. Due to the spiral downturn of the market conditions for Internet and multi-media related businesses which affected the value of Internet businesses both in Hong Kong and the PRC, the directors of the Company consider that there are indications of impairment of the optical fibre cable. Based on their assessment, the carrying amount of the optical fibre cable was written down by $21 million (included in "Other operating expenses"). The estimate of the recoverable amount was by reference to the sale values of similar assets disposed of recently in the market.

12 FIXED ASSETS *(continued)*

(b) The analysis of the net book value of properties is as follows:

	The Group	
	2001	2000
	$'000	*$'000*
Outside Hong Kong – medium-term leases	**16,000**	24,178

(c) The Group's leasehold land and buildings held for own use were revalued at 31 December 2001 on an open market value basis by C S Surveyors Limited, an independent firm of professional valuers, who have among their staff Fellows of the Hong Kong Institute of Surveyors. The revaluation deficit of $2,619,000 (2000: $8,107,000 after debiting of $140,000 to land and buildings revaluation reserves) has been charged to the consolidated profit and loss account. Had the leasehold land and buildings held for own use been carried at historical cost less accumulated depreciation as at 31 December 2001, their carrying value would have been approximately $31,636,000 (2000: 40,498,000).

(d) As at 31 December 2000, the net book value of fixed assets of the Group held under finance leases amounted to $1.5 million.

13 GOODWILL

	Positive goodwill recognised as an asset $'000	Positive goodwill carried in reserves $'000
Cost:		
At 1 January 2001	–	1,130,621
Additions arising on acquisition of a subsidiary	47,780	–
At 31 December 2001	47,780	1,130,621
Accumulated amortisation:		
Charge for the year	4,778	–
Impairment loss	–	1,130,621
At 31 December 2001	4,778	1,130,621
Carrying amounts:		
At 31 December 2001	43,002	–
At 31 December 2000	–	1,130,621

Positive goodwill recognised as an asset is amortised as an expense on a straight-line basis over 10 years. The amortisation of positive goodwill for the year is included in "Other operating expenses" in the consolidated profit and loss account.

Due to significant uncertainties existing in the present market conditions both in Hong Kong and the PRC upon the occurrence of the September 11 crisis coupled with the slow down in the progress of the Group's Internet-related businesses in the PRC upon the publication of the Measures for the Administration of Telecommunications Service Operating Permits by the PRC Ministry of Information Industry in which stringent rules are imposed on the application of operating permits for Intelligent Building projects, the directors of the Company consider that there are indications of impairment of the goodwill carried in reserves arising from the acquisition of certain subsidiaries engaging in Internet-related operation ("operation"). They carried out a review of the recoverable amount of the goodwill. Based on their assessment which is by reference to the value in use of the operation and taking into account the abovementioned uncertainties surrounding the operation, a full provision for impairment loss of $1,130,621,000 has been made.

14 INVESTMENTS IN SUBSIDIARIES

	The Company	
	2001	2000
	$'000	*$'000*
Unlisted shares, at cost	**68,891**	68,891
Amounts due from subsidiaries	**1,480,750**	1,425,995
Amounts due to subsidiaries	**(1,105)**	(1,434)
	1,548,536	1,493,452
Less: Impairment loss	**(1,339,422)**	(194,011)
	209,114	1,299,441

The following list contains only the particulars of subsidiaries which principally affect the results, assets or liabilities of the Group. The class of shares held is ordinary unless otherwise stated. All of these are controlled subsidiaries as defined under note 1(c) and have been consolidated in the Group financial statements.

Amounts due from/to subsidiaries are unsecured, interest-free and have no fixed terms of repayment.

Name of company	Place of incorporation and operation	Particulars of issued and paid up capital	Proportion of ownership interest: Group's effective holding	Proportion of ownership interest: held by the Company	Proportion of ownership interest: held by subsidiary	Principal activity
Beijing Infohighway Information and Technology Ltd. *(note (b))*	PRC	Registered capital US$10,000,000	90	–	90	Provision of Internet-related consultancy services
ChinaInfohighway Hong Kong Limited (Formerly Sparkle Development Limited)	Hong Kong	1,000,000 shares of $1 each	100	–	100	Holding ISP Pnet licence and provision of virtual private network service
Cyber Info Management Limited	British Virgin Islands ("BVI")	1 share of US$1 each	100	100	–	Investment in optical fibre cable

(Expressed in Hong Kong dollars)

14 INVESTMENTS IN SUBSIDIARIES *(continued)*

Name of company	Place of incorporation and operation	Particulars of issued and paid up capital	Proportion of ownership interest: Group's effective holding	Proportion of ownership interest: held by the Company	Proportion of ownership interest: held by subsidiary	Principal activity
Dongguan Weihang Electrical Product Company Limited *(note (c))*	PRC	Registered capital US$8,107,000	100	–	100	Manufacture and trading of healthcare and household products
Dynamic Technology Limited	BVI	1 share of US$1 each	100	100	–	Trademark holding
eForce China Limited	BVI	1 share of US$1 each	100	100	–	Provision of management services
eForce Management Limited	Hong Kong	2 shares of $1 each	100	100	–	Provision of management services
Fairform Manufacturing Company Limited	Hong Kong	4,750,000 ordinary shares of $1 each and 250,000 non-voting deferred shares of $1 each	100	–	100	Manufacture and trading of healthcare and household products
Fairform Holdings Limited	Hong Kong	2 shares of $1 each	100	100	–	Name holding
Gold Fortress Holdings Ltd.	BVI	200 shares of US$1 each	100	100	–	Investment holding
Megabit Telecom Inc.	BVI	10,000 shares of US$1 each	100	–	100	Investment holding

(Expressed in Hong Kong dollars)

14 INVESTMENTS IN SUBSIDIARIES *(continued)*

Name of company	Place of incorporation and operation	Particulars of issued and paid up capital	Proportion of ownership interest Group's effective holding	held by the Company	held by subsidiary	Principal activity
Space Treasure Limited	Hong Kong	2 shares of $1 each	100	–	100	Web-site construction
Skilful Developments Limited	BVI	1 share of US$1 each	100	100	–	Investment holding
Zhuhai Tianxin Business Software Limited *(note (a))*	PRC	Registered capital of $1,000,000	100	–	100	Development and sale of enterprise applications software

Notes:

(a) On 26 October 2001, the Group acquired the entire interest in Zhuhai Tianxin Business Software Limited ("Tianxin") together with the shareholders' loans due by Tianxin from an independent third party for a total consideration of $48 million, satisfied by the issue and allotment of 21.7 million ordinary shares of $0.05 each of the Company. As a result, the Group's loss for the year has been increased and the net assets as at the year end have been reduced by $875,000.

Tianxin is a wholly foreign owned enterprise with an operating period of 10 years expiring on 19 June 2006.

(b) Beijing Infohighway Information and Technology Ltd. is a sino-foreign equity joint venture with an operating period of 20 years expiring on 21 July 2019.

(c) Dongguan Weihang Electrical Product Company Limited is a wholly foreign owned enterprise with an operating period of 30 years expiring on 10 April 2024.

(d) On 31 May 2001, the Group disposed of its entire interest in Anford International Limited which was a property holding company for a total consideration of $5 million. The Group recorded a profit on disposal of $2,125,000 in the consolidated profit and loss account. The effect on the Group's results during the year in respect of the disposal is not significant.

15 INTEREST IN ASSOCIATES

	The Group	
	2001	2000
	$'000	*$'000*
Share of net assets	**2,294**	710
Amount due to an associate	**(2,000)**	(2,000)
	294	(1,290)

Amount due to an associate is unsecured, interest-free and has no fixed terms of repayment.

The following list contains only the particulars of associates, all of which are unlisted corporate entities, which principally affect the results or assets of the Group:

Name of associate	Place of incorporation and operation	Particulars of issued and paid up capital	Proportion of ownership interest: Group's effective interest	Proportion of ownership interest: held by subsidiary	Principal activity
Esterham Enterprise Inc.	BVI	2 ordinary shares of US$1 each	50	50	Portal development
Dynasty L.L.C.	United States of America	140,000 ordinary shares of US$1 each	50	50	Dormant
Jade Ocean Surface Finishing Company Limited	Hong Kong	10,000 ordinary shares of $1 each	49	49	Dormant

16 OTHER NON-CURRENT ASSETS

	The Group	
	2001	2000
	$'000	*$'000*
Deposit *(note (a))*	**56,731**	45,102
Other receivable *(note (b))*	**1,775**	–
	58,506	45,102

Notes:

(a) The deposit represents a quality guarantee deposit paid to China Infohighway Communications Co., Ltd ("IHW") pursuant to Cooperation Agreement and Supplemental Agreements (collectively "the Agreements") entered into between the Group and IHW. Under the Agreements the Group agrees to provide certain equipment and facilities as necessary for IHW's network infrastructure for a facility fee (note 28(c)). In the event that the Group does not provide the required equipment and facilities, IHW can make use of the deposit to purchase the required equipment and facilities.

The deposit is unsecured, non-interest bearing and is repayable upon the expiry of the Agreements on 21 July 2019.

(b) Other receivable represents the long-term portion of the balance of consideration for the disposal of the Group's subsidiary. The total consideration receivable of $2,550,000 (see note 26(d)) is repayable by step-up monthly instalments with the final instalment due in November 2004. It is secured over the ordinary shares of the subsidiary disposed of and a pledge of the investment property held by the subsidiary. In the event of default, interest at prime lending rate plus 2% per annum will be charged on the overdue balance.

As at 31 December 2001, the current portion of $775,000 is included in "Other debtors, deposits and prepayments" (see note 18).

17 INVENTORIES

	The Group	
	2001	2000
	$'000	*$'000*
Raw materials	**3,355**	13,116
Work in progress	**483**	6,148
Finished goods	**398**	1,196
	4,236	20,460

18 TRADE AND OTHER RECEIVABLES

	The Group		The Company	
	2001	2000	**2001**	2000
	$'000	*$'000*	***$'000***	*$'000*
Trade debtors *(note (b))*	**31,014**	4,268	**–**	–
Other debtors, deposits and prepayments *(note (c))*	**41,981**	37,493	**197**	280
Amounts due from associates *(note 28(f))*	**19**	6,309	**–**	–
	73,014	48,070	**197**	280

Notes:

(a) All the trade and other receivables are expected to be recovered within one year.

(b) Included in trade debtors is an amount of $27,412,000 due from a related party (2000: $Nil) for the provision of consultancy services (note 28(c)).

(c) Included in other debtors, deposits and prepayments is an amount of $775,000 representing the current portion of the balance of consideration for the disposal of the Group's subsidiary (note 16).

The ageing analysis of trade debtors (net of specific provisions for bad and doubtful debts) is as follows:

	The Group	
	2001	2000
	$'000	*$'000*
Current	**2,091**	–
1 to 3 months overdue	**812**	908
More than 3 months overdue but less than 12 months overdue	**28,111**	3,360
	31,014	4,268

Trade debts are due up to 30 days from the date of billing. Debtors with balances that are more than 3 months overdue are requested to settle all outstanding balances before any further credit is granted.

19 CASH AND BANK BALANCES

	The Group		The Company	
	2001	2000	**2001**	2000
	$'000	*$'000*	***$'000***	*$'000*
Deposits with banks maturing within three months from placement	**–**	2,500	**–**	2,500
Cash at bank and in hand	**8,382**	6,284	**857**	407
	8,382	8,784	**857**	2,907

20 LOANS FROM BANKS AND OTHER FINANCIAL INSTITUTIONS

At 31 December 2001, loans from banks and other financial institutions were repayable as follows:

	The Group		The Company	
	2001	2000	**2001**	2000
	$'000	*$'000*	***$'000***	*$'000*
Within 1 year or on demand	**128,263**	32,522	**43,988**	23,088
After 1 year but within 2 years	**–**	146,422	**–**	13,088
	128,263	178,944	**43,988**	36,176

At 31 December 2001, loans from banks and other financial institutions were secured as follows:

	The Group		The Company	
	2001	2000	**2001**	2000
	$'000	*$'000*	***$'000***	*$'000*
Bank loans				
– secured *(note (a))*	**89,326**	170,981	**13,088**	36,176
Loans from other financial institutions				
– secured *(note (b))*	**8,037**	7,963	**–**	–
– unsecured	**30,900**	–	**30,900**	–
	128,263	178,944	**43,988**	36,176

Notes:

(a) At 31 December 2001, bank loans of $76 million (2000: $135 million) were secured by US dollar bank deposits of US$9.7 million (equivalent to $75 million) (2000: $138.8 million) and the remaining balance of $13 million (2000: $36 million) is secured over the Group's entire shareholding in Gold Fortress Holdings Limited and all assets held by Fairform Manufacturing Company Limited with a carrying value of approximately $16 million (2000: $45 million).

(b) The loan was secured over the Group's land and buildings held for own use situated outside Hong Kong with a carrying value of $16 million (2000: $19 million).

21 OBLIGATIONS UNDER FINANCE LEASES

At 31 December 2001, the Group had obligations under finance leases repayable as follows:

	2001	2000
	$'000	*$'000*
Present value of the minimum lease payments repayable within 1 year	**–**	931
Related interest expense	**–**	(34)
Total minimum lease payments	**–**	897

22 CONVERTIBLE NOTES

	The Group and the Company	
	2001	2000
	$'000	*$'000*
HK dollar convertible notes due January 2002 *(note (a))*	**6,500**	6,500
US dollar convertible notes due July 2004 *(note (b))*	**64,743**	–
	71,243	6,500

(a) HK dollar convertible notes

On 1 February 2000, pursuant to a placing and underwriting agreement dated 16 December 1999 ("placing agreement") entered into between the Company and independent placing agents, 4% convertible notes with an aggregate principal amount of $9 million were issued. The convertible notes are convertible to ordinary shares of $0.05 each of the Company ("ordinary shares") at any time between 1 April 2000 and 27 January 2002. The conversion price was set at $0.05 and subsequently adjusted to $0.42 upon the completion of the Company's capital reorganisation and the rights issue in 2000. There were no conversions of the convertible notes during the year (2000: $2.5 million).

Upon maturity, the Company has not repaid the convertible notes as the Company has the intention and is under negotiation with the noteholders to extend the maturity date for one year to 31 January 2003 with the other terms and conditions remaining unchanged. Consents from all the noteholders have yet to be received. Notwithstanding the foregoing, in accordance with the placing agreement, the convertible notes are already due and payable at its principal amount outstanding together with the accrued interest of approximately $6,695,000.

Assuming that the noteholders agreed to extend the maturity date as mentioned above and the outstanding convertible notes were fully converted, the Company would be required to issue a further 15,476,191 ordinary shares; otherwise, the outstanding amount would be repayable no later than 31 January 2003. The ordinary shares to be issued on any exercise of the conversion rights attaching to the convertible notes will rank pari passu in all respects with the ordinary shares in issue.

22 CONVERTIBLE NOTES *(continued)*

(b) US dollar convertible notes

On 12 July 2001, the Company entered into a subscription agreement ("the agreement") with independent third parties to issue 3% convertible notes with an aggregate principal amount of US$20 million ("the notes") and warrants ("the warrants"). The notes are convertible to ordinary shares at any time during the three years after the issue of the notes, at the conversion price as stipulated in the agreement. At the maturity date, any notes outstanding shall be redeemed in full or the Company may elect to convert the notes into ordinary shares. The ordinary shares to be issued on any exercise of the conversion rights attaching to the notes will rank pari passu in all respects with the ordinary shares in issue.

The warrants, issued together with the notes, are convertible to ordinary shares at any time during the three years after the issue of the warrants, at the exercise price as stipulated in the agreement. The ordinary shares to be issued upon conversion of the warrants shall rank pari passu in all respects with the ordinary shares in issue.

$78 million (equivalent to US$10 million) of the notes and 8,150,366 warrants were issued during the year. $13,277,000 (equivalent to US$1.7 million) and $3,900,000 (equivalent to US$500,000) of the notes were converted into 6,352,465 ordinary shares during the year and 6,050,461 ordinary shares subsequent to the year end respectively.

Subsequent to the year end, due to the occurrence of a triggering event as stipulated in the agreement, the noteholders have requested the Company to redeem the notes of $60.8 million (equivalent to US$7.8 million) and the accrued interest thereon at a price of 115%. The aggregate amount repayable is approximately $70.2 million. In view of the foregoing, the notes have been classified under current liabilities.

23 TRADE AND OTHER PAYABLES

	The Group		The Company	
	2001	2000	**2001**	2000
	$'000	*$'000*	***$'000***	*$'000*
Trade creditors	**9,029**	26,705	**–**	–
Other creditors and accrued charges	**31,043**	42,334	**10,782**	26,317
Amount due to ultimate holding company *(note 28(b))*	**9,333**	4,076	**4,877**	–
Amounts due to associates *(note 28(f))*	**540**	6,776	**–**	–
Amounts due to directors	**702**	–	**–**	–
Amounts due to former directors and officers	**154**	7,616	**–**	–
Amount due to a related company *(note 28(c))*	**–**	952	**–**	–
	50,801	88,459	**15,659**	26,317

23 TRADE AND OTHER PAYABLES *(continued)*

Amounts due to directors and officers are unsecured, interest-free and have no fixed terms of repayment except for an amount of $5,988,000 due to officers as at 31 December 2000 which carried interest at a rate of 8.5% per annum.

The ageing analysis of trade creditors is as follows:

	The Group	
	2001	2000
	$'000	*$'000*
Due within 1 month or on demand	**5,998**	15,502
Due after 1 month but within 3 months	**3,024**	1,807
Due after 3 months but within 6 months	**7**	2,232
Due after 6 months	**–**	7,164
	9,029	26,705

24 SHARE CAPITAL

	2001	2000
	$'000	*$'000*
Authorised:		
6,000,000,000 ordinary shares of $0.05 each	**300,000**	300,000

	2001		2000	
	No. of shares	**Amount *$'000***	No. of shares	Amount *$'000*
Issued and fully paid:				
Shares of $0.05 (2000: $0.1) each at 1 January	**1,136,851,600**	**56,843**	306,851,606	30,685
Issued during the year *(notes (a) and (b)(i) to (iv))*	**32,902,465**	**1,645**	830,000,000	41,500
Share reduction *(notes b(i) and (v))*	**–**	**–**	(1,080,009,026)	(69,342)
Rights issue *(note b(v))*	**–**	**–**	1,080,009,020	54,000
Shares of $0.05 each at 31 December	**1,169,754,065**	**58,488**	1,136,851,600	56,843

24 SHARE CAPITAL *(continued)*

(a) Details of movements in the Company's issued share capital during the year

(i) Pursuant to the Company's share option scheme adopted on 2 June 1997, 55,800,000 share options were granted to certain employees of the Group on 10 July 2000. These share options are exercisable for a period commencing from 10 July 2001 to 9 July 2010 and the holders thereof are entitled to subscribe for ordinary shares of $0.05 each in the Company at a subscription price of $0.588 per share.

During the year, share options were exercised to subscribe for 4,850,000 ordinary shares of $0.05 each in the Company at a consideration of $2,852,000, of which $242,000 was credited to share capital and the balance of $2,610,000 was credited to share premium account. At 31 December 2001, the number of share options outstanding was 24,300,000 (2000: 53,800,000).

(ii) Pursuant to a conditional agreement dated 1 August 2001, the Company issued 21,700,000 ordinary shares of $0.05 each in the Company to an independent third party at a price of $2.212 per share representing a discount of approximately 7.8% to the closing price of the share of the Company on 1 August 2001 as consideration of $48 million for the acquisition of a subsidiary (see note 14). An amount of $1,085,000 and $46,915,000 was credited to the share capital and the share premium account respectively. These shares were issued under the general mandate granted to the directors at the annual general meeting on 29 May 2001 and rank pari passu in all respects with the ordinary shares in issue.

(iii) During the year, convertible notes of $13,277,000, equivalent to US$1.7 million, were converted by the noteholders at conversion prices ranging from $1.1656 to $2.2968, resulting in the issue of 6,352,465 ordinary shares of $0.05 each in the Company. An amount of $318,000 and $12,959,000 was credited to the share capital and the share premium account respectively. These ordinary shares were issued under the general mandate granted to the directors at the annual general meeting held on 29 May 2001 and rank pari passu in all respects with the ordinary shares in issue.

(b) Details of movements in the Company's authorised and issued share capital in 2000

(i) Pursuant to ordinary/special resolutions passed at a special general meeting held on 1 February 2000:

– the nominal value of the Company's issued and authorised ordinary share capital were reduced from $0.1 each to $0.05 each. The contributed surplus of $15,342,000 arising from the cancellation of an amount of $0.05 per share on the 306,851,606 ordinary shares was applied to eliminate the same amount of the accumulated losses of the Company. In addition, pursuant to the same resolution, the authorised share capital of the Company was re-designated into new ordinary shares of $0.05 each;

24 SHARE CAPITAL *(continued)*

(b) Details of movements in the Company's authorised and issued share capital in 2000 *(continued)*

- the Company's authorised share capital was increased from $100 million to $150 million by the creation of an additional 1,000 million ordinary shares of $0.05 each in the Company; and

- the Company issued and allotted 600 million ordinary shares of $0.05 each in the Company to Tees Corporation ("Tees") at par representing a discount of approximately 93.1% to the closing market price of the share of the Company on 29 October 1999, being the date of a subscription agreement between Tees and the Company. The net proceeds of approximately $30 million were used to reduce the bank borrowings of the Group and to provide additional working capital for the Group.

(ii) On 24 February 2000, arrangements were made for a private placement to independent private investors of 120 million ordinary shares of $0.05 each in the Company held by Tees, the controlling shareholder of the Company, at a price of $1.10 per share representing a discount of approximately 10.6% to the closing price of the share of the Company on 23 February 2000.

Pursuant to a placing and subscription agreement on the same date, Tees subscribed for 120 million ordinary shares in the Company at a price of $1.10 per share. The proceeds were used to finance business acquisitions and to provide additional working capital for the Group. These ordinary shares were issued under the general mandate granted to the directors at a special general meeting held on 1 February 2000 and rank pari passu in all respects with the ordinary shares in issue.

(iii) Pursuant to a sale and purchase agreement on 2 June 2000, the Company issued 60 million ordinary shares of $0.05 each in the Company to Tokatee Internet Limited at a price of $0.80 per share representing a discount of approximately 3.6% to the closing price of the share of the Company on 2 June 2000 as consideration of $48 million for the acquisition of a section of optical fibre cable in the PRC. These ordinary shares were issued under the general mandate granted to the directors at a special general meeting held on 1 February 2000 and rank pari passu in all respects with the ordinary shares in issue.

(iv) On 14 July 2000, $2.5 million convertible notes were converted by the noteholders, resulting in the issue of 50 million ordinary shares of $0.05 each in the Company. These ordinary shares were issued pursuant to an ordinary resolution passed at a special general meeting held on 1 February 2000 and rank pari passu in all respects with the ordinary shares in issue.

24 **SHARE CAPITAL** *(continued)*

(b) Details of movements in the Company's authorised and issued share capital in 2000 *(continued)*

(v) Pursuant to ordinary/special resolutions passed at a special general meeting held on 30 November 2000:

– the Company consolidated every twenty issued and unissued shares of $0.05 each in the capital of the Company into one share of $1.00 each in the Company;

– the nominal value of the Company's issued share capital was reduced from $1.00 each to $0.05 each. The contributed surplus of $54,000,000 arising from the cancellation of an amount of $0.95 per share on the 56,842,580 shares was applied to eliminate the same amount of the accumulated losses of the Company. The Company also subdivided every authorised but unissued share of $1.00 into twenty ordinary shares of $0.05 each;

– the Company's authorised share capital was increased from $150 million to $300 million by the creation of an additional 3,000 million shares of $0.05 each in the Company; and

– the Company issued 1,080,009,020 ordinary shares of $0.05 each in the Company at $1.05 per share by way of a rights issue in the proportion of nineteen rights shares for every existing share then held. The net proceeds of the rights issue of approximately $1,110 million were used to finance business acquisition and for general working capital purposes.

25 RESERVES

(a) The Group

	Share premium $'000	Contributed surplus $'000	Exchange reserves $'000	Land and buildings revaluation reserves $'000	Accumulated losses $'000	Total $'000
At 1 January 2000	29,303	12,401	(3,315)	140	(96,383)	(57,854)
Arising on issue of shares *(notes 24(b)(ii), (iii) and (v))*	1,251,009	–	–	–	–	1,251,009
Expenses incurred in connection with rights issue	(28,718)	–	–	–	–	(28,718)
Share reductions *(notes 24(b)(i) and (v))*	–	69,342	–	–	–	69,342
Transfer between reserves	–	(81,743)	–	–	81,743	–
Goodwill	–	–	–	–	(1,130,621)	(1,130,621)
Written back on disposal	–	–	–	(140)	–	(140)
Exchange differences on translation of the financial statements of subsidiaries outside Hong Kong	–	–	(421)	–	–	(421)
Loss for the year	–	–	–	–	(58,816)	(58,816)
At 31 December 2000	1,251,594	–	(3,736)	–	(1,204,077)	43,781
At 1 January 2001	1,251,594	–	(3,736)	–	(1,204,077)	43,781
Arising on issue of shares *(note 24(a))*	62,484	–	–	–	–	62,484
Expenses incurred in connection with rights issue	(91)	–	–	–	–	(91)
Exchange differences on translation of the financial statements of subsidiaries outside Hong Kong	–	–	592	–	–	592
Impairment loss on goodwill	–	–	–	–	1,130,621	1,130,621
Loss for the year	–	–	–	–	(1,216,597)	(1,216,597)
At 31 December 2001	1,313,987	–	(3,144)	–	(1,290,053)	20,790

25 RESERVES *(continued)*

(a) The Group *(continued)*

Included in the figure for the accumulated losses is an amount of $254,000 (2000: $1,838,000), being the accumulated losses attributable to associates.

Under the Bye-laws of the Company, the share premium is not distributable.

The exchange reserves and land and buildings revaluation reserves have been set up and will be dealt with in accordance with the accounting polices adopted for foreign currency translation and the revaluation of investment properties and land and buildings held for own use (note 1).

The contributed surplus of the Group arose as a result of the Group's reorganisation carried out on 31 May 1997 and represents the difference between the nominal value of the shares of the subsidiaries acquired pursuant to the Group's reorganisation, over the nominal value of the Company's shares issued in exchange therefore.

(b) The Company

	Share premium *$'000*	**Contributed surplus** *$'000*	**Accumulated losses** *$'000*	**Total** *$'000*
At 1 January 2000	29,303	68,691	(128,679)	(30,685)
Arising on issues of shares *(notes 24(b)(ii), (iii) and (v))*	1,251,009	–	–	1,251,009
Expenses incurred in connection with rights issue	(28,718)	–	–	(28,718)
Share reductions *(notes 24(b)(i) and (v))*	–	69,342	–	69,342
Transfer between reserves	–	(128,679)	128,679	–
Loss for the year	–	–	(84,156)	(84,156)
At 31 December 2000	1,251,594	9,354	(84,156)	1,176,792
At 1 January 2001	1,251,594	9,354	(84,156)	1,176,792
Arising on issues of shares *(note 24(a))*	62,484	–	–	62,484
Expenses incurred in connection with rights issue	(91)	–	–	(91)
Loss for the year	–	–	(1,218,395)	(1,218,395)
At 31 December 2001	1,313,987	9,354	(1,302,551)	20,790

25 RESERVES *(continued)*

(b) The Company *(continued)*

The contributed surplus of the Company arose as a result of the above Group reorganisation scheme and represents the excess of the then combined net assets of the subsidiaries acquired, over the nominal value of the Company's shares issued in exchange therefor.

Pursuant to the board resolution dated 29 December 2000, the directors of the Company approved a transfer of the accumulated losses as at 1 January 2000 to the contributed surplus.

Under The Companies Act 1981 of Bermuda (as amended), the Company may make distributions to its members out of the contributed surplus under certain circumstances which the company is currently unable to meet.

26 NOTES ON THE CONSOLIDATED CASH FLOW STATEMENT

(a) Reconciliation of loss from operations to net cash outflow from operating activities

	2001 *$'000*	2000 *$'000*
Loss from operations	(1,209,764)	(48,715)
Interest income	(8,076)	(3,474)
Profit on disposal of a subsidiary	(2,125)	–
Gain on settlement of loans due to a former director	(1,138)	–
Depreciation	19,442	8,887
Impairment loss on goodwill	1,130,621	–
Impairment loss on fixed assets	21,000	–
Amortisation on goodwill	4,778	–
Deficit arising from revaluation and investment property of leasehold land and buildings	2,619	8,107
Loss on disposal of fixed assets	555	3,299
Fixed assets written off	8,769	3,493
Provision for amounts due from associates	–	349
Increase in non-current asset	(11,629)	–
Decrease/(increase) in inventories	16,224	(6,624)
Decrease in trade debtors	923	6,677
Increase in net amount due from a related company	(28,364)	–
Decrease in other debtors, deposits and prepayments	648	3,689
Increase in net amounts due to/from associates	54	(6,309)
Decrease in trade creditors	(13,402)	(120)
(Decrease)/increase in other creditors and accrued charges	(16,271)	905
Increase in amount due to ultimate holding company	5,257	4,076
Increase in amounts due to directors	702	–
Decrease in amounts due to former directors and officers	(6,324)	(1,846)
Foreign exchange	918	–
Net cash outflow from operating activities	(84,583)	(27,606)

26 NOTES ON THE CONSOLIDATED CASH FLOW STATEMENT *(continued)*

(b) Purchase of subsidiaries

	2001	2000
	$'000	*$'000*
Net liabilities acquired:		
Fixed assets	**2,188**	27,287
Other investments	**–**	45,102
Cash and bank balances	**1,006**	141,287
Trade debtors	**257**	909
Other debtors, deposits and prepayments	**636**	34,694
Trade creditors	**(21)**	(931)
Other creditors and accrued charges	**(3,683)**	(23,874)
Shareholder's loan	**–**	(83,235)
Bank loans	**–**	(133,333)
Finance lease	**–**	(43)
Tax payable	**–**	(193)
Amount due to a related company	**–**	(952)
Amount due to an associate	**–**	(6,776)
Minority interests	**–**	(3,392)
	383	(3,450)
Share of pre-acquisition losses	**–**	3,640
Share of other pre-acquisition reserves	**–**	288
Positive goodwill arising on consolidation	**47,780**	1,130,621
	48,163	1,131,099
Consideration including acquisition costs of $163,000 (2000: $1,099,000) satisfied by:		
Shares allotted	**48,000**	–
Cash	**163**	1,131,099
	48,163	1,131,099

The effect on the cash flows of the Group for the year in respect of the subsidiary acquired during the year is not significant.

26 NOTES ON THE CONSOLIDATED CASH FLOW STATEMENT *(continued)*

(b) Purchase of subsidiaries *(continued)*

Pursuant to the agreements for sale and purchase in connection with the acquisition of the subsidiaries last year, certain debts amounted to $35.3 million were assigned to the Group upon the acquisition of a 100% interest in Space Treasure Limited, trading as Chinacon.net and the acquisition of a 20% interest in Megabit Telecom Inc., which were included in the above account captions appropriately.

(c) Analysis of net inflow/(outflow) of cash and cash equivalents in respect of the purchase of subsidiaries

	2001 *$'000*	2000 *$'000*
Cash consideration	**(163)**	(1,131,099)
Cash at bank and in hand acquired	**1,006**	141,287
Pledged deposits with banks	**–**	(138,807)
Net inflow/(outflow) of cash and cash equivalents in respect of the purchase of subsidiaries	**843**	(1,128,619)

(d) Disposal of a subsidiary

	$'000
Net assets disposed of:	
Fixed assets	**5,438**
Other receivables	**677**
Other creditors and accrued charges	**(3,240)**
	2,875
Profit on disposal	**2,125**
Disposal proceeds net of expenses	**5,000**
Set off against trade creditors	**(2,100)**
Consideration receivable *(note 16)*	**(2,550)**
Net cash inflow from disposal of the subsidiary	**350**

The effect on the cash flows of the Group for the year in respect of the subsidiary disposed of during the year is not significant.

26 NOTES ON THE CONSOLIDATED CASH FLOW STATEMENT *(continued)*

(e) Analysis of changes in financing

	Loans from banks and other financial institutions $'000	Finance lease obligations $'000	Other loans $'000	Share capital and premium (including contributed surplus) $'000	Convertible notes $'000
At 1 January 2000	54,453	3,071	–	72,389	–
Cash flows from financing	(8,842)	(2,217)	(83,235)	1,267,291	9,000
Arising from acquisition of subsidiaries	133,333	43	83,235	–	–
Arising from capital reduction applied to offset against accumulated losses	–	–	–	(81,743)	–
Arising from acquisition of optical fibre cable	–	–	–	48,000	–
Issue of shares on exercise of convertible notes	–	–	–	2,500	(2,500)
At 31 December 2000	178,944	897	–	1,308,437	6,500
At 1 January 2001	178,944	897	–	1,308,437	6,500
Cash flows from financing	(51,430)	(897)	–	2,761	77,923
Arising from acquisition of subsidiaries	–	–	–	48,000	–
Issue of shares on exercise of convertible notes	–	–	–	13,277	(13,277)
Exchange adjustment	749	–	–	–	97
At 31 December 2001	128,263	–	–	1,372,475	71,243

(f) Major non-cash transactions

(i) During the year ended 31 December 2001, holders of $13,277,000 (2000: $2.5 million) convertible notes exercised the right to convert into 6,352,465 (2000: 50 million) ordinary shares of $0.05 each of the Company (note 22(b)).

(ii) During the year ended 31 December 2001, the Group acquired a subsidiary by the issue and allotment of ordinary shares of the Company (note 14).

(iii) During the year ended 31 December 2000, the Group acquired a section of the optical fibre cable for an amount of $48 million which was satisfied by the issue and allotment of 60 million ordinary shares of $0.05 each of the Company (note 24(b)(iii)).

27 COMMITMENTS

(a) At 31 December 2001, the Group had the following capital commitments outstanding and not provided for in the financial statements:

	2001 $'000	2000 $'000
Contracted for:		
Quality guarantee deposit	5,700	16,380
Purchases of fixed assets	–	603
	5,700	16,983

(b) At 31 December 2001, the total future minimum lease payments under non-cancellable operating leases in respect of land and buildings of the Group are payable as follows:

	2001 $'000	2000 $'000
Within 1 year	3,326	4,591
After 1 year but within 5 years	842	8,407
After 5 years	8,807	9,122
	12,975	22,120

28 MATERIAL RELATED PARTY TRANSACTIONS

(a) A wholly-owned subsidiary of the Company, eForce Management Limited ("eForce Management") entered into a lease agreement with the ultimate holding company to lease an office space for a period of 7 months commencing from 1 January to 31 July 2001 at a monthly rental of $142,800. The total rental payable to the ultimate holding company for the year ended 31 December 2001 amounted to $999,600 (2000: $961,000). The lease was entered into on normal commercial terms. The Company is aware that this constituted a connected transaction by virtue of Mr. Leung Chung Shan's interest in the ultimate holding company but was exempted under Rule 14.24(5) of The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Listing Rules").

On 1 August 2001, eForce Management entered into an assignment agreement with the ultimate holding company, whereby the ultimate holding company agreed to assign its rights and obligations under the lease dated 15 December 1999 between the ultimate holding company and a third party ("the landlord") relating to a property ("the lease") to eForce Management at nil consideration. The property is used as the principal place of business of the Group in Hong Kong. The assignment agreement has been negotiated on terms favourable to the eForce Management and the ultimate holding company has provided a guarantee in favour to the landlord for eForce Management's obligations under the lease. As the assignment agreement constituted a connected transaction under the Listing Rules, the Company has made an announcement pursuant to Rule 14.25(1) of the Listing Rules on 2 August 2001.

28 MATERIAL RELATED PARTY TRANSACTIONS *(continued)*

(b) During the year ended 31 December 2001, the Group was granted financial assistance from the ultimate holding company. At 31 December 2001, the amount due to the ultimate holding company of $9,333,000 (2000: $4,076,000) is unsecured, interest-free and has no fixed terms of repayment.

(c) During the year ended 31 December 2001, consultancy and facility fees charged by Beijing Infohighway Information and Technology Ltd. ("BIHW") to China Infohighway Communications Co., Ltd ("IHW"), a substantial shareholder of BIHW, amounted to approximately $30,026,000 (2000: $106,000). In accordance with the Cooperation Agreement and Supplemental Agreements (collectively "the Agreements"), consultancy fee was calculated with reference to the costs (defined in the Agreements) incurred by BIHW for its services provided to IHW plus a 30% premium on such costs; facility fee was charged based on the depreciation expenses of the equipment and facilities provided by BIHW. The provision of services and facilities by BIHW to IHW under the Agreements constitutes ongoing connected transactions of the Company under the Listing Rules ("Ongoing Connected Transactions"). The Company has been granted a conditional waiver from strict compliance with the disclosure requirements as stipulated in Chapter 14 of the Listing Rules in connection with the Ongoing Connected Transactions on each occasion they arise.

At 31 December 2001, amount due from IHW of $27,412,000 (2000: due to IHW of $952,000) is unsecured, interest-free and has no fixed terms of repayment.

(d) On 4 October 2000, the Company granted a loan to an associate, Megabit Telecom Inc. ("Megabit") for an amount of $15 million. The loan was unsecured and carried interest at a fixed rate of 10% per annum. Interest charged to the associate amounted to $366,000 during the year ended 31 December 2000. On 21 December 2000, Megabit became a wholly-owned subsidiary of the Group and the amount outstanding as at the balance sheet date had been eliminated on consolidation.

(e) During the year ended 31 December 2000, prior to BIHW becoming a subsidiary of the Group, pursuant to a management agreement entered into between eForce Management and BIHW on 1 April 2000 and subsequently revised on 16 October 2000, management fees of $3,801,000 had been charged during the year ended 31 December 2000.

(f) During the year ended 31 December 2000, the Group provided portal development services to an associate of the Group who in turns provided portal development services to BIHW under the same terms as those provided to other customers. Portal development income for the year ended 31 December 2000 receivable from the associate amounted to $6,300,000.

Amounts due from/to associates are unsecured, interest-free and have no fixed terms of repayment.

29 LITIGATION

(a) In October 1999, Mersongate Holdings Limited, an independent third party (the "Plaintiff") commenced an action against (1) Mr Huen Raico Hing Wah, a former director of the Company; (2) Central Growth Limited and Bridal Path Corporation, former substantial shareholders of the Company and (3) the Company (collectively the "Defendants"), alleging that the Defendants have agreed to certain arrangements in relation to the share capital of the Company, including certain rights of the Plaintiff to participate in the share capital of the Company, and that the Defendants have failed to perform their respective obligations under the arrangements, and claiming specific performance or, alternatively, damages. The Company has no knowledge of and is not a party to the alleged arrangements. The Company has filed a defence against the claim and the directors of the Company consider that no provision for the claim is necessary.

(b) On 23 February 2001, Winsmooth Holdings Limited ("Winsmooth"), a supplier of Fairform Manufacturing Company Limited ("Fairform"), a wholly-owned subsidiary of the Group, instituted proceedings against Fairform, claiming an amount of $252,450 being an amount which Winsmooth alleged was due for goods sold and delivered by Winsmooth to Fairform. Fairform had filed a defence against the claim. Subsequent to the year end, both parties to the proceedings mutually agreed an out of court settlement of $200,000 being payable by Fairform for full and final settlement of the proceedings.

(c) On 26 May 2000, Mr Wong Fu Keung ("Mr Wong"), a former director of the Company, instituted proceedings against Fairform, claiming repayment of a sum of $3,183,951 which Mr Wong made a payment under a guarantee provided to a bank for banking facilities granted to Fairform. A defence was filed by Fairform on 26 July 2000. In accordance with a Deed of Settlement dated 20 June 2001 entered into between Mr Wong and Fairform, the claim was settled and a gain of approximately $1.1 million was recorded.

(d) On 31 May 2000, Top Harvest Industrial Limited ("Top Harvest"), a wholly-owned subsidiary of the Group, instituted proceedings against Pentagon (EMI) Shielding Limited ("Pentagon") claiming an amount of $7,661,017 being the outstanding amount due to Top Harvest for goods sold and delivered by Top Harvest to Pentagon.

On 23 June 2000, Pentagon instituted proceedings against Fairform claiming an amount of $3,548,448 being an amount which Pentagon alleged was due for work done and services applied and for goods sold and delivered by Pentagon to Fairform. In accordance with a Deed of Settlement dated 20 June 2001 entered into between Top Harvest, Fairform, Pentagon and certain companies of the Group ("the group companies"), all the above claims, together with other balances due between the group companies and Pentagon, were settled with an insignificant loss incurred.

30 ULTIMATE HOLDING COMPANY

The directors consider the ultimate holding company at 31 December 2001 to be Tees Corporation, which is incorporated in the British Virgin Islands.

31 COMPARATIVE FIGURES

Classification of certain income/expenses in the consolidated profit and loss account has been changed to conform with the current year's presentation as follows:

(i) "Other income" for 2000 has been restated as "Other revenue" and "Other net income".

(ii) Loss of disposal of fixed assets totalling $3,299,000 which was included in "Other operating expenses" in the 2000 financial statements have been reclassified under "Other net income".