

Chairman's Statement

The Board of Directors of the Company is pleased to announce that the Group recorded a net profit attributable to shareholders of RMB144 million for 2001 (2000: RMB182 million), representing a decrease of approximately 20.9% when compared with that of 2000. The consolidated turnover for the Group was RMB656 million (2000: RMB634 million), representing an increase of approximately 3.5% over that of 2000. In order to facilitate the long-term development of the Group, the Board of Directors does not recommend the payment of a final dividend for the year in order to retain the Group's resources to expedite the progress of the projects on hand.

BUSINESS REVIEW

Review of operation

During 2001, a total of 40,442 tons (2000: 43,787 tons) of pre-oriented yarn ("POY"), drawn and textured yarn ("DTY") and fully-drawn yarn ("FDY") were produced by the Group. This was at a similar level as the corresponding period of 2000. Following the completion of the production line of polyester chips in October 2001, the Group produced a total of 14,932 tons (2000: nil) of polyester chips in 2001.

Sales and processing volume of POY, DTY and FDY were 40,578 tons (2000: 31,074 tons) and 721 tons (2000: 12,990 tons) respectively. In addition, the Group recorded sales of polyester chips of 4,474 tons (2000: nil) which contributed approximately RMB21 million (2000: nil) sales revenue in 2001.

Consolidated turnover for the year under review increased slightly by 3.5% when compared with that of last year. This is mainly due to contribution made by Dalian Huayang Engineering Co., Ltd. ("Dalian Huayang") which was acquired in 2000. For the sales and processing volume of chemical fibre, the business was relative stable during the year 2001.

The prices of domestic chemical fibre decreased during the year 2001. The Group's gross profit margin for the year was approximately 33.3% (2000: 39.8%). The Group has been successfully sheltered from the price drop which is mainly due to the following:

- (i) Although the domestic chemical fibre market as a whole was not very good in 2001, the demand of differential chemical fibre was relative stable. Consequently, the Group's products only experienced a moderate drop in selling prices;
- (ii) The Group has taken initiative to adjust its product mix to include products with higher added-value. In 2001, over 90% of the Group's sales were differential chemical fibre while in 2000, it only accounted for 76%; and
- (iii) The prices of the major raw materials used in production, such as polyester chips, POY, purified terephthalic acid and mono ethylene glycol, decreased in 2001.

It is the Group's long-term strategy to decrease the processing operation in the future because the Directors believe that the competition in processing business is very keen in the future and such business is not stable as it depends on other manufacturers' performance. By replacing the processing operation by sales of the Group's products, the Directors believe that the Group could response more quickly to the market and could maintain a more stable earnings in the future, thus increasing the competitive edge of the Group. Consequently, the processing volume decreased substantially during the year.

Chairman's Statement

BUSINESS REVIEW (continued)

Change of Company's name

The name of the Company was changed from Heshun Holdings Company Limited to Heshun Specialised Fibre Holdings Limited with effect from 12 December 2001. For the purpose of identification, the Chinese name of the Company was changed from “和順控股有限公司” to “和順特種纖維控股有限公司”. The change of name is intended to better reflect the main business activities of the Group and to enable the investors to have an easy recognition of the business of the Group.

On 23 April 2002, the Board proposed to change the name of the Company to China Specialised Fibre Holdings Limited. For identification purpose, the Chinese name was also proposed to change to “中國特種纖維控股有限公司”. The new proposed name is intended to better reflect the Group being one of the largest differential fibre manufacturers in the People's Republic of China (the “PRC”) and to enable the investors to have easy recognition of the Group's business operation and market being focused in the PRC. The proposed change of name is subject to the passing of a special resolution at the forthcoming Annual General Meeting on 30 May 2002.

Spandex project

The construction of the factory premises was commenced on 19 January 2002. It is the largest Spandex project in the PRC approved by the State Development and Planning Commission. According to the Group's plan, it is expected that the construction will be completed by the end of the first quarter of 2003. The shipment of the machinery is expected to be in the second quarter of 2003 and installation will be in middle of 2003. Trial production is scheduled in the third quarter of 2003. The Group is currently arranging banking facilities and other financing for the Spandex project.

Production line of polyester chips

The Group has commenced its production of polyester chips in October 2001. The annual production capacity of this production line is 80,000 tons. Following the commencement of this production line, the Group will improve its competitiveness by ensuring a stable supply of polyester chips with consistently high quality while at the same time reducing production cost. The excess of polyester chips required by the Group will be sold to other local manufacturers. In 2001, sales of polyester chips accounted for approximately RMB21 million (2000: nil) and would increase in the coming years.

Production line of ultra fine POY

Ultra fine POY is a new product to the Group. It is a high quality yarn having the features such as heat retention, waterproof, softness and lightness and is mainly used for the manufacture of high quality sport wears. The modification of the existing factory to adapt for the new production line is expected to be completed in early 2003. The installation of the required machinery is scheduled in the second quarter of 2003. It is expected that trial production of ultra fine POY will be commenced in middle of 2003. The planned annual production capacity of this production line is 13,000 tons.

BUSINESS REVIEW (continued)

Acquiring additional interest in Heshun (Fujian) Spandex Co., Ltd. ("Heshun Spandex") and disposal of Changle City Shunshi Group Co., Ltd. ("Changle")

In July 2001, the Group acquired a further 23% interest in Heshun Spandex by entering into the following arrangements:

- (1) The Group disposed of the 20% of the registered capital of Changle which in turn held a 60% equity interest in Heshun Spandex before the transaction mentioned in paragraph (2) below. Changle is an associated company of the Group before the disposal. Subsequent to the disposal, the Group does not have any interest in Changle. The consideration for the disposal was approximately RMB36 million which was satisfied by way of setting off and discharging the payment obligations of Heshun Spandex owing to Changle.
- (2) At the same time of the disposal mentioned above, the Group acquired a further 35% direct interest in the registered capital of Heshun Spandex from Changle. The consideration of the acquisition was RMB1.00 and the Group will be responsible for the capital contribution obligations in relation to the 35% equity interest to the registered capital of Heshun Spandex of US\$31,050,000.

After the completion of the above transactions, the Group holds a 75% interest in the equity of Heshun Spandex through Central Harvest Holdings Limited, a wholly-owned subsidiary of the Group, and the remaining 25% is being held by Changle.

The Group anticipates that the demand for spandex in the PRC would continue to grow and believes that the above acquisition would enhance its profitability in the future.

As Changle is principally an investment vehicle and the Group's business does not rely heavily on any facilities or services provided by Changle and the Group is capable of carrying on business independently of Change, the Board considers that the acquisition of further interest in Heshun Spandex will streamline the corporate structure of the Group and facilitate the progress of the project being carried out by Heshun Spandex.

Under the Listing Rules, the above transactions constitute connected transactions and further details have been set out in the circular to shareholders of the Company dated 30 July 2001.

Disposal of Dalian Huayang

The Group disposed of all the 95% equity interest in Dalian Huayang in November 2001. Dalian Huayang is principally engaged in the provision of engineering and installation services for the chemical fibre projects and the design and installation of chemical fibre production machinery and equipment. The consideration was RMB76 million and the Group recorded a profit, before relevant professional fees and related expenses, of RMB24 million and has been included in the 2001 consolidated income statement. The Board believes that the disposal is in the interest of the Group, and the Group is able to focus on its business relating to the production and distribution of differential chemical fibre products.

Chairman's Statement

BUSINESS REVIEW (continued)

Disposal of Dalian Huayang (continued)

Under the Listing Rules, the above transaction constitutes a connected transaction and further details have been set out in the circular to shareholders of the Company dated 12 December 2001.

Employees and remuneration policies

As at 31 December 2001, the Group employed a total of 591 (2000: 619) employees. Most of the employees are based in the PRC. They are remunerated according to the nature of job and market conditions in which they are employed. Other staff benefits include a mandatory provident fund scheme for all the eligible employees, medical compensation and a year-end bonus.

FINANCIAL REVIEW

Financial resources

As at 31 December 2001, the Group's cash and bank balances were approximately RMB45 million (2000: RMB42 million). The Group's current ratio as at 31 December 2001 was 40% (2000: 38%). Current assets and current liabilities were approximately RMB220 million (2000: RMB158 million) and RMB547 million (2000: RMB415 million) respectively.

As at 31 December 2001, the Group had bank and other loans in an aggregate amount of RMB424 million (2000: RMB254 million), of which 50% (2000: 71%) was denominated in Renminbi, 13% (2000: 28%) in US dollars and 37% (2000: 1%) in Hong Kong dollars respectively. During the year, the Group successfully raised a syndicated loan and term loans of HK\$85 million and HK\$29 million respectively in Hong Kong. The funds from these financing are mainly applied to Spandex project. This mainly contributes the increase in total of bank and other loans as at 31 December 2001.

Included in current liabilities, there were short-term bank loans amounted to RMB289 million (2000: RMB251 million). It is the normal practice of the PRC banks to grant short-term loans which are renewed on a yearly basis, and consequently, the short-term bank loans of the Group account for 68% (2000: 95%) of the total borrowings. Although there is no assurance that these short-term loans will be extended in the future upon maturity within a year, however, the Directors are in the opinion that the Group would be able to renew these loans on a yearly basis taking into the long-term relationship between the banks and the Group.

During the financial year 2001, the Company did not issue any new shares or other securities. As at 31 December 2001, the Company has issued 1,860 million (2000: 1,860 million) shares. The gearing ratio of the Group (total of short-term and long-term bank loans over the shareholders' equity) was 48% (2000: 35%). The increase is attributable to the recent arrangement of a syndicated term loan and term loans in Hong Kong to finance the development of Spandex project.

At present, the Group is negotiating with certain banks in Hong Kong and the PRC to raise funds for Spandex project and the production line of ultra fine POY and the management will closely monitor the level of gearing of the Group as a whole.

FINANCIAL REVIEW (continued)

Exchange exposure

Due to the fact that the Group's transactions (including the sale of chemical fibre, purchases of raw materials and bank financing) are denominated in Hong Kong dollars, US dollars or Renminbi, and the related exchange rates are considered relative stable, and accordingly, the exposure to fluctuations in exchange rate is minimal.

Capital commitments

A significant portion of capital commitments is attributable to Spandex project. The Group will finance the construction of factory and production facilities of Spandex project and ultra fine POY in the coming years from the cash inflows from operation, bank and other financing.

Contingent liabilities

Details of the Company's contingent liabilities are set out in note 36 to the financial statements.

The Group did not have any material contingent liabilities as at year-end.

Pledges of assets

As at 31 December 2001, land and buildings, plant and machinery and motor vehicles of the Group with net book value of RMB414 million (2000: RMB84 million) were pledged as securities for bank and other loans and finance lease granted to the Group.

FUTURE PLAN AND PROSPECTS

Looking forward, the market for differential chemical fibre will more or less remain stable. The Board anticipates that the economy of the PRC will continue to thrive in the coming year. It is estimated that the PRC's economic growth will reach approximately 7% in 2002. The improvement in living standards, the growth in household income together with the increase in demand for export of textiles and garments and further decrease in raw material costs as a result of the entry of the PRC into World Trade Organisation, will provide further room for the growth of differential chemical fibre market.

The PRC government will continue to regulate the domestic chemical fibre market, such as anti-dumping, sanitation and environmental protection. In addition, the PRC government has planned, through structural reform and technological innovation, to increase the proportion of differential chemical fibre produced from the existing 20% level to 40% of the total production of chemical fibre in the PRC by the end of 2005. This indicates there exists a huge room for the growth in differential chemical fibre market. At present, most of the domestic manufacturers including some PRC state-owned enterprises are currently focusing on increasing their scale of production and are just beginning to undergo technical modifications, the strategy of the Group is to produce high quality fibre. The Directors believe that the Group has competitive advantages over other domestic manufacturers owing to the superior quality of its products and its quality customer service. The Group is committed to the research and development of new products and continuous improvement of production technology. The Board believes that due to the intensive market competition, the marketability of brand names and types of products are becoming increasingly important.

Chairman's Statement

FUTURE PLAN AND PROSPECTS (continued)

With the completion of the Spandex project and the production line of ultra fine POY, the Board believes that the competitive edge over the other manufacturers in the PRC will surely increase and would contribute substantial sales revenue to the Group in years to come. In addition, the Group will be the only manufacturer that has the capability to produce polyester chips, ultra fine POY, differential chemical fibre and spandex fibre in the PRC.

APPRECIATION

On behalf of the Board of Directors, I would like to express our appreciation to all management and staff members for their dedication and contribution, and to thank shareholders, customers and suppliers for their continuing support to the Group. The Board will make every endeavor to explore potential opportunities for our business growth and to create a promising future for the Group as well as our shareholders.

By order of the Board

Chen Shunli

Chairman & Chief Executive Officer

Shenzhen, the People's Republic of China

26 April 2002