

The board of directors of the Company is pleased to present its report together with the audited accounts of the Group for the Year.

1. Principal Activities

The Company is an investment holding company. The Group is principally engaged in the production and sale of urban purified water, the development and sale of real estate, the investment in a joint venture which is principally engaged in the production and sale of electricity and heat and has equity interests in a business venture which is principally engaged in high-tech investment projects.

The analysis of the Group's results by segment for the Year is set out in note 3 to the accounts.

2. Subsidiaries and Joint Ventures

Shenyang Water, a subsidiary of the Company, was incorporated in Mo Chou Hu Street, Shenyang Economic and Technological Development Zone, Shenyang, the PRC. Its registered capital is RMB754,830,000. The Company holds 99.37% equity interests in the subsidiary. To date, no debt securities were issued by the subsidiary.

Real Estate Company, a subsidiary of the Company, was incorporated in Mo Chou Hu Street, Shenyang Economic and Technological Development Zone, Shenyang, the PRC. Its registered capital is RMB35,000,000. The Company holds 99.00% equity interests in the subsidiary. To date, no debt securities were issued by the subsidiary.

Shenhai Co-generation, a joint venture of the Company, was incorporated in No. 352 Zhulin Road, Dadong District, Shenyang, the PRC. Its registered capital is US\$35,388,000. The Company holds 22.50% equity interests in the joint venture. To date, no debt securities were issued by the joint venture.

3. Other Investments

The Company has equity interests in QTIL. Its registered capital is RMB250,000,000. The Company holds 8% equity interests in QTIL. To date, no debt securities were issued by the QTIL.

4. Holding Company

The holding company of the Company is SPUG which was established on 26th November 1998. SPUG is controlled by Shenyang Municipal Government and is also a major investment company of Shenyang Municipal Government. SPUG is engaged in the development and investment in public utilities. Shenyang Urban Infrastructure Facility Construction Investment Development Company Limited ("Shenyang Urban Construction Company"), Shenyang State-owned Assets Management Company Limited ("Shengyang Asset Company") and Shenyang State-owned Real Estate Assets Management Company Limited hold 73.3%, 22.8% and 3.9% equity interests in SPUG respectively. On 25th June, 2001, SPUG has convened an extraordinary general meeting at which it was resolved to split SPUG. The registered capital of SPUG after splitting would be reduced to RMB1,056,530,000. The new shareholder Shenyang Urban Construction Company and Shengyang Asset Company hold 84.46% and 15.54% equity interests in SPUG respectively. These two companies are all controlled by Shenyang Municipal Government and they hold equity interests in SPUG on behalf of the government.

5. Results, Financial Position and Analysis of Results

The Group's results for the Year are set out in the consolidated profit and loss account on page 40.

The Group's financial position for the Year is set out in the consolidated balance sheet on page 41.

The Group's cash flow for the Year is set out in the consolidated cash flow statement on page 43.

Analysis of the results of the Group for the Year is set out in the Management Discussion and Analysis section on pages 14 to 19.

6. Interim Dividend

At the Board of Directors meeting of the Company held on 24th August 2001, it was resolved to declare the distribution of an interim dividend of RMB0.07 per share in cash, totalling RMB71,428,000 for 2001. The dividend was distributed on 18th October 2001 to those shareholders whose names appeared as registered members of the Company at the close of business on 28th September 2001.

7. Final Dividend

As the Company is actively pursuing investment opportunities in new projects and a substantial amount of capital is expected to be incurred in relation thereto in 2002, the Board of Directors of the Company resolved that no final dividend would be declared for 2001 in the long-term interest of the Company. Such resolution is subject to approval at the 2001 Annual General Meeting of the Company to be held on 7th June 2002.

8. Reserves

Details of the reserves of the Group and the movements therein during the Year are set out in note 26 on page 65.

9. Properties under Development for Sale and Completed Properties held for Sale

As at 31st December 2001, the Group held the following properties for sale:

Name of properties	Address	Area (<i>'000 sq.m.</i>)	Intended Usage	Current Position	Group's interest
Hongji Garden	No.71-75, Da Bei Guan Street, Da Dong District, Shenyang	46	Commercial and residential	Construction of residential units completed and sale is in progress	99%
Huanggu Warehouse Land	No. 36, Huaihe Steet, Huanggu District, Shenyang	53	Commercial and residential	Construction not yet begun and design is in progress	99%
Water Source Land	No. 31, Wenhua East Road, Dongling District, Shenyang	161	Commercial and residential	Construction not yet begun and design is in progress	99%

10. Donation

During the Year, the Group did not make any donations to charities.

11. Fixed Assets

Details of the movements in the fixed assets of the Group during the Year are set out in note 14 on page 59.

12. Share Capital

During the Year, the share capital structure of the Company was as follows:

Types of shares	Number of shares	Percentage
Domestic invested shares	600,000,000	58.80%
H shares	<u>420,400,000</u>	<u>41.20%</u>
Total	<u><u>1,020,400,000</u></u>	<u><u>100%</u></u>

There was no change in the share capital structure of the Company during the Year.

13. Taxation

Details of the Group's taxation is described in Note 9 to the accounts on page 56.

- (1) The Group expects that the results of the Group will be affected if the taxation preferential policy mentioned thereon is cancelled in 2002.
- (2) No tax reduction and exemption was enjoyed by holders of the listed securities of the Company for their holding of such securities.

14. Staff Quarters

The Group did not have any balance of house revolving funds which was carried forward in its accounts upon its incorporation in 1999, and no staff quarters were constructed, purchased or sold to staff.

Pursuant to the "Housing Reserves Management Ordinance" stipulated by the PRC government and the Shenfangweihiufa [2000] No.3 document issued by Shenyang Municipal Government on 28th December 2000, the basis of contribution for the housing reserves was the average monthly salary income in the Previous Year, of which the ratio of contribution by the Group was 8% from 1st January 2001 onwards.

15. Distributable Reserves

Pursuant to relevant PRC regulations and the Articles of Association of the Company, profit available for distribution to shareholders shall be the lower of the accumulated distributable profits determined in accordance with PRC accounting standards and regulations as stated in the PRC statutory accounts and the accumulated distributable profits adjusted in accordance with HK GAAP. In the PRC statutory accounts and the HKGAAP accounts as at 31st December 2001, retained earnings after appropriation available to be carried forward for distribution to shareholders in future years amounted to RMB260,881,000 (2000:RMB135,700,000) and RMB175,467,000 (2000: RMB81,166,000) respectively. As such, distributable reserves of the Company as at 31st December 2001 amounted to RMB175,467,000 (2000: RMB81,166,000).

16. Five-Year Financial Highlights

Highlights of the results and assets and liabilities of the Group during the Year and the past years are set out on pages 4 to 5.

17. Major Customers and Suppliers

During the Year, the Group's sales to its five largest customers accounted for approximately 88.34% of the Group's total sales, of which sales to SWGC, the largest customer, accounted for approximately 86.50% of the Group's total sales for the Year. Purchases from the five largest suppliers for the Year accounted for approximately 81.67% of the Group's total purchases, of which purchases from the Shenyang Electricity Bureau, the largest supplier, accounted for approximately 37.00% of the Group's total purchases of the Year.

Except for Shenyang Urban Construction Company, the controlling shareholder of the Company's controlling shareholder, SPUG, which owns 100% of the equity interests in the Group's largest customer, SWGC, and director Mr. Zhang Guo Xiang who is also the General Manager of SWGC, none of the directors, their associates or any shareholder (to which the knowledge of the directors owns 5% or more of the share capital of the Company) had an interest in the above-mentioned five largest suppliers or customers.

18. Use of Proceeds of H Shares

Details of use of proceeds of H Shares during the Year are set out in Management Discussion and Analysis section on page 19.

19. Directors and Supervisors

Directors and supervisors of the Company during the Year were as follows:

Directors: Mr. Zhang Guo Xiang, Mr. Ma Ying (Resignation tendered in December 2001), Mr. Zhang Ying Jian, Mr. Chan Kam Ling, Mr. Wang Se, Ms. Li Xiao Yang (Resignation tendered in February 2001) Mr. Geng Jian Wei, Mr. Lin Wen Bin, Mr. Jacques Létondot (Resignation tendered in August 2001), Mr. Liu Gang, Mr. Liu Ting Yi, Mr. Huang Hai (Resignation tendered in February 2002), Mr. Choy Shu Kwan Wilson, Mr. Cheng Wei, Mr. Lu Tie Nan (Resignation tendered in January 2002) and Mr. Chen Jia Sheng (Resignation tendered in June 2001). Messrs Choy Shu Kwan, Cheng Wei and Lu Tie Nan were independent non-executive directors.

Supervisors: Mr. Wang Guang Zhou, Mr. Cai Hong Yuan, Mr. Li Jing Li, Mr. Zhang Yun Peng (Resignation tendered in December 2001), Mr. Hu Pei Hua (Resignation tendered in June 2001), Mr. Lin Xin Rong and Mr. Ma Hui.

The term of office of all existing directors and supervisors will expire on 12th August 2002.

20. Directors' and Supervisors' Service Contracts

<i>Directors</i>	<i>Term of Service</i>
Mr. Zhang Guo Xiang	2000.6.19-2002.8.12
Mr. Zhang Ying Jian	1999.7.2-2002.8.12
Mr. Chan Kam Ling	1999.11.24-2002.8.12
Mr. Wang Se	1999.7.2-2002.8.12
Mr. Geng Jian Wei	2001.5.11-2002.8.12
Mr. Lin Wen Bin	1999.7.2-2002.8.12
Mr. Liu Gang	1999.7.2-2002.8.12
Mr. Liu Ting Yi	2000.6.19-2002.8.12
Mr. Huang Hai	1999.7.2-2002.8.12 (Resignation tendered in February 2002)
Mr. Choy Shu Kwan, Wilson	2001.5.11-2002.8.12
Mr. Cheng Wei	2001.8.24-2002.8.12
Mr. Lu Tie Nan	1999.9.25-2002.8.12 (Resignation tendered in January 2002)
Mr. Ma Ying	1999.7.2-2002.8.12 (Resignation tendered in December 2001)
Ms. Li Xiao Yang	1999.7.2-2002.8.12 (Resignation tendered in February 2001)
Mr. Jacques Létondot	1999.11.24-2002.8.12 (Resignation tendered in August 2001)
Mr. Chen Jia Sheng	1999.7.2-2002.8.12 (Resignation tendered in June 2001)

20. Directors' and Supervisors' Service Contracts (Continued)

<i>Supervisors</i>	<i>Term of Service</i>
Mr. Wang Guang Zhou	1999.7.2-2002.8.12
Mr. Cai Hong Yuan	2001.5.11-2002.8.12
Mr. Li Jing Li	1999.7.2-2002.8.12
Mr. Ma Hui	1999.7.2-2002.8.12
Mr. Lin Xin Rong	1999.9.25-2002.8.12
Mr. Hu Pei Hua	1999.9.25-2002.8.12 (Resignation tendered in June 2001)
Mr. Zhang Yun Peng	1999.7.2-2002.8.12 (Resignation tendered in December 2001)

None of the directors who are proposed for re-election at the forthcoming annual general meeting, has a service contract with the Company which is not determinable within one year without payment of compensation, other than statutory compensation.

21. Directors', Supervisors' and Senior Management's Rights to Acquire Shares in the Company

At no time during the Year have the directors, supervisors or senior management purchased or held any shares in the Company nor acquired any benefits through the disposal of the Company's shares.

22. Directors' and Supervisors' Right to Purchase Shares

During the Year, the Company did not make any arrangements for directors, supervisors, chief executive officers or their spouses or their children under 18 years old, to acquire benefits by means of the acquisition of the Company's shares.

23. Total remuneration of Directors and Supervisors

Except for Messrs Chan Kam Ling and Jacques Létondot, each of the executive and non-executive directors will receive an annual salary of RMB20,000. The service contracts have not mentioned any adjustment to the annual salary of the directors. The executive directors may be entitled to certain cash bonuses according to the profitability of the Company upon the Board of Director's approval (in which case the interested directors will abstain from voting) and are entitled to the welfare benefit provided under the relevant PRC laws and regulations. Non-executive directors are only entitled to the welfare benefit provided under the relevant PRC laws and regulations. Each supervisor will receive an annual salary of RMB10,000. The supervisors are not entitled to any beneficial interests that are generally available to other employees of the Group.

During the Year, the total emoluments payable to the directors and supervisors amounted to RMB2,361,000 (2000: RMB1,277,000). Executive directors did not receive any cash bonus on the basis of the profits of the Company or other additional benefits.

24. Directors' and Supervisors' Interests in Business Contracts

Other than the director, Mr Zhang Guo Xiang, who is also the general manager of SWGC, no other contracts of significance in relation to the Company's business to which the Company, any of its subsidiaries and holding company was a party and in which any director or supervisor had a material interest, whether directly or indirectly, subsisted at any time during the year or at the end of the year.

25. Change in Share Capital and Shareholdings of Substantial Shareholders

The register of substantial shareholders maintained by the Company pursuant to Article 16(1) of the Securities (Disclosure of Interests) Ordinance as at 31st December 2001 disclosed that the following companies have an interest amounting to 10% or more of the relevant issued share capital of the Company:

- (1) SPUG holds all of the 600,000,000 domestic shares in issue, representing 58.80% of the total issued share capital of the Company;
- (2) Tai Fook Securities Company Limited holds 92,180,000 H shares, representing 21.93% of the issued H shares of the Company, of which, Sino-French Water Development (Liaoning) Company Limited ("Sino-French Liaoning") holds 88,146,000 H shares*, representing 20.97% of the issued H shares of the Company;
- (3) Citibank NA holds 49,043,000 H shares, representing 11.67% of the issued H shares of the Company.

* Sino-French Water Development Company Limited, Sino-French Holdings (Hong Kong) Limited, Beauty Ocean Limited, Lotsgain Limited, New World Infrastructure Limited, Mombasa Limited, Sea Walker Limited, New World Development Company Limited and Chow Tai Fook Enterprise Company Limited are deemed to have interests in these H shares.

Save as disclosed above, the Company has not been notified of any interest required to be disclosed pursuant to the Securities Ordinance (Disclosure of Interests) during the Year.

26. Material Contracts

- (1) During the Year, the Group continued to comply with the terms of the “Technology and Operations Services Agreement” entered into with Sino-French Water Development Company Limited, (“Sino-French Water”) on 21st November 1999. Pursuant to the agreement, Sino-French Liaoning, a wholly-owned subsidiary of Sino-French Water, shall send a management team to provide all water plants of Shenyang Water with technology and management services and continue to provide advanced technological support and the best management measures. The Group shall pay a fixed fee of RMB5,000,000 per annum to Sino-French Liaoning in respect of the services provided by that company. The agreement is valid for 10 years.
- (2) During the Year, no material contracts had been entered into between the Group and SPUG, the controlling shareholder of the Company. Apart from the Company, SPUG and its subsidiary had also not entered into any material contracts with the Group.

27. Connected Transactions

During the Year, the connected transactions of the Group were as follows:

- (1) sale of purified water to SWGC by Shenyang Water, with total sales of RMB577,362,000 (2000: RMB595,285,000);
- (2) purchase of surface raw water from SWGC by Shenyang Water, with a total purchase amount of RMB50,283,000 (2000: RMB56,452,000);
- (3) Interest charged on overdue water fee receivable due from SWGC by Shenyang Water amounted to RMB33,041,000 (2000: Nil).
- (4) lease of office from Shenyang Water Services General Company (“SWSGC”) by Shenyang Water, with total rental of RMB420,000 (2000: RMB420,000);
- (5) lease of land to SWSGC by Shenyang Water, with total rental of RMB90,000 (2000: RMB90,000);

The Stock Exchange has granted a waiver for the requirements of approval by shareholders for the connected transactions set out in (1) and (2) above, whereas connected transactions set out in (3) have been approved by the Board of Directors of Shenyang Water.

Independent non-executive directors of the Company have reviewed the above-mentioned connected transactions and expressed their opinions. Details of their opinion are set out on page 30 under the section “Work of the Audit Committee”.

28. Purchase, Sale or Redemption of Shares

During the Year, the Group did not purchase, sell or redeem any of the Company's shares.

29. Share Options

During the Year, the Group did not issue or grant any of convertible securities, futures options, warrants and other similar rights.

30. Significant Events

(1) The 1st Extraordinary General Meeting for 2001

The 1st Extraordinary General Meeting of the Company for 2001 was held on 24th August 2001. As SPUG, the controlling shareholder of the Company, considered that the use of proceeds from A Share Issue required further review, all special resolutions in relation to the proposed A Share Issue were not approved. Accordingly, it was resolved to postpone the A Share Issue. In addition, the appointment of Mr. Cheng Wei as an independent non-executive director of the Company was duly approved at the 1st Extraordinary General Meeting.

(2) Resignation of the president

Due to another appointment of Mr. Ma Ying by Shenyang Municipal Government, Mr. Ma Ying resigned from his positions of president, vice-chairman and executive director of the Company on 5th December 2001, with immediate effect. Mr. Zhang Guo Xiang, the chairman of the Company, assigned Mr. Zhang Ying Jian, the deputy president of the Company, to be temporarily in charge of the daily work of the Company.

31. Bank Borrowings

As at 31st December 2001, the repayment terms of the Group's bank borrowings of RMB80,000,000 are either repayable on demand or repayable within one year. The bank borrowings were used as the working capital of the Group. During the Year, the Group had no delay in repayment of bank borrowings.

32. Trust Deposits

During the Year, the Group placed a trust deposit of RMB80,000,000 with Citic Bank (Beishi Branch, Shenyang) for a short period of time. The Company earned an interest income of RMB1,889,000 from the deposit. The deposit had been recovered by 31st December 2001.

33. Retirement Scheme

Details of the retirement scheme and the amount of contributions to the retirement scheme are set out in note 5 on page 54.

34. Pre-emptive Rights

There are no provisions for pre-emptive rights under the Company's Articles of Association and the laws of the PRC which would require the Company to offer new shares to existing shareholders on a pro rata basis.

35. Loans to Senior Management

During the Year, the Group did not give any loan or other kinds of financial assistance to the senior management of the Group.

36. Work of the Audit Committee

Pursuant to the Code of Best Practice as set out in Appendix 14 to the Listing Rules, the Company established an Audit Committee at the fifth meeting of the Board of Directors. The main function of the Committee, which is a special committee under the Board of Directors, is to review and supervise the financial reporting procedures and methods of the Group. The Audit Committee comprises two independent non-executive directors of the Company, namely Messrs Choy Shu Kwan, Wilson and Cheng Wei.

At the meeting held on 15th April 2002, the Audit Committee reviewed the accounts of the Company and expressed its opinion in respect of the connected transactions of the Company as follows:

- (1) The information disclosed in the accounts of the Company is complete, accurate and fair and the accounting policies adopted are correct, without any material problems being discovered.

36. Work of the Audit Committee (Continued)

- (2) The connected transactions of the Company have been carried out:
- A in the ordinary and usual course of business of the Company;
 - B on normal commercial terms (by reference to transactions of a similar nature and as made by similar entities in the PRC) or (where there is no available comparison) on terms no less favourable than those available to third parties;
 - C in accordance with the terms of the respective agreements governing such transactions;
 - D are fair and reasonable so far as the shareholders of the Company are concerned; and
 - E the value of the connected transactions as a percentage of the Group's turnover does not exceed the respective cap in respect of the waiver for the connected transactions granted by the Stock Exchange, that is, the sales of purified water accounted for 86.50% but less than 100% of the Group's turnover and the purchase of raw water from SWGC accounted for 7.53% but less than 15% of the Group's turnover.

37. Code of Best Practice

The directors of the Company are pleased to confirm that the Company has complied with the Code of Best Practice as set out in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") during the Year.

38. Material Litigation

During the Year, the Group was not involved in any material litigation or arbitration.

39. Auditors

The accounts of the Group prepared in accordance with the accounting principles generally accepted in Hong Kong and the accounting standards issued by the Hong Kong Society of Accountants have been audited by PricewaterhouseCoopers, Certified Public Accountants. A resolution will be submitted at the forthcoming Annual General Meeting to re-appoint PricewaterhouseCoopers, Certified Public Accountants, as international auditors of the Group. The Group did not change its international auditors during the past three years.

Since our previous domestic auditors Hualun Certified Public Accountants has not obtained the relevant approval of qualification of securities practice by the China Securities Regulatory Commission for the 2002 year. The Company, as such, proposed to newly appoint Yuehua Certified Public Accountants as auditors of the 2001 results of the Group. The Company will submit the proposal of the newly appointment of Yuehua Certified Public Accountants as domestic auditors to the annual general meeting.

40. Publication of Information on the Web-site of the Stock Exchange

Financial and other relevant information of the Company in accordance with the paragraphs from 45(1) to 45(3) of Appendix 16 to the Listing Rules will be available for publication on the web-site of the Stock Exchange in due course.

By order of the Board
Zhang Guo Xiang
Chairman

19th April 2002, Shenyang, the PRC