1. CORPORATE INFORMATION

The registered office of Yanion International Holdings Limited is located at Cedar House, 41 Cedar Avenue, Hamilton HM12, Bermuda.

During the year, the Group was involved in the following principal activities:

- the manufacture and trading of compact disc ("CD") players, video CD ("VCD") players, CD and VCD player mechanisms, amplifiers, computer peripherals, car audio mechanisms, cassette deck mechanisms and related component products, and non-audio products including personal office appliances and medical devices;

- the sale of Internet phone sets and provision of related services by way of agency in the People's Republic of China (the "PRC"); and

- the research and development of video-on-demand systems in the PRC for the re-engineering of existing cable TV stations in the PRC.

2. IMPACT OF NEW AND REVISED STATEMENTS OF STANDARD ACCOUNTING PRACTICE ("SSAPs")

The following recently issued and revised SSAPs are effective for the first time for the current year's consolidated financial statements:

- SSAP 9 (Revised) : "Events after the balance sheet date"
- SSAP 14 (Revised) : "Leases"
- SSAP 17 (Revised) : "Property, plant and equipment"
- SSAP 26 : "Segment reporting"
- SSAP 28 : "Provisions, contingent liabilities and contingent assets"
- SSAP 29 : "Intangible assets"
- SSAP 30 : "Business combinations"
- SSAP 31 : "Impairment of assets"
- SSAP 32 : "Consolidated financial statements and accounting for investment in subsidiaries"

These SSAPs prescribe new accounting measurement and disclosure practices. The major effects on the Group's accounting policies and on the amounts disclosed in these financial statements of those SSAPs which have had a significant effect on the financial statements, are summarised as follows:

SSAP 9 (Revised) prescribes which type of events occurring after the balance sheet date require adjustment to the financial statements, and which requires disclosure, but no adjustment. SSAP 9 (Revised) has had no major impact on the financial statements.

2. IMPACT OF NEW AND REVISED STATEMENTS OF STANDARD ACCOUNTING PRACTICE ("SSAPs") (continued)

SSAP 14 (Revised) prescribes the basis for lessor and lessee accounting for finance and operating leases, and the required disclosures in respect thereof. Certain amendments have been made to the previous accounting measurement treatments, which may be accounted for retrospectively or prospectively, in accordance with the requirements of the SSAP. The revised SSAP requirements have not had a material effect on the amounts previously recorded in the financial statements. Therefore, no prior year adjustment has been required. The disclosure changes under the SSAP have resulted in changes to the detailed information disclosed for finance leases and operating leases, which are further detailed in notes 24 and 30 to the financial statements.

SSAP 17 (Revised) requires that impairment losses on fixed assets are aggregated with accumulated depreciation in note 12 to the financial statements, whereas previously they were deducted from the cost of the relevant asset. This disclosure reclassification has had no effect on the net carrying amount of fixed assets in the balance sheet.

SSAP 26 prescribes the principles to be applied for reporting financial information by segment. It requires that management assesses whether the Group's predominant risks or returns are based on business segments or geographical segments and determines one of these bases to be the primary segment information reporting format, with the other as the secondary segment information reporting format, with the other as the secondary segment information reporting format. The impact of this SSAP is the inclusion of additional segment reporting disclosures which are included in note 4 to the financial statements.

SSAP 28 prescribes the recognition criteria and measurement bases to apply to provisions, contingent liabilities and contingent assets, together with the required disclosures in respect thereof. The SSAP has had no major impact on the financial statements.

SSAP 29 prescribes the recognition and measurement criteria for intangible assets together with the disclosure requirements. The adoption of this SSAP has resulted in no change to the previously adopted accounting treatment for intangible assets and the additional disclosures that it requires have not been significant for these financial statements. The SSAP does, however, require that impairment losses on intangible assets are aggregated with accumulated amortisation (see notes 13 and 14), whereas previously they were deducted from the cost of the relevant asset. This disclosure reclassification has had no effect on the net carrying amount of intangible assets in the balance sheet.

SSAP 30 prescribes the accounting treatment for business combinations, including the determination of the date of acquisition, the method for determining the fair values of the assets and liabilities acquired, and the treatment of goodwill or negative goodwill on acquisition. The SSAP requires the disclosure of goodwill in the non-current assets section of the consolidated balance sheet. It requires that goodwill is amortised in the consolidated profit and loss account over its estimated useful life. The adoption of the SSAP has not resulted in a prior year adjustment. No goodwill/negative goodwill remains eliminated against reserves as at the balance sheet date. The required new additional disclosures are included in note 14 to the financial statements.

2. IMPACT OF NEW AND REVISED STATEMENTS OF STANDARD ACCOUNTING PRACTICE ("SSAPs") (continued)

SSAP 31 prescribes the recognition and measurement criteria for impairment of assets. The SSAP is required to be applied prospectively and therefore, has had no effect on amounts previously reported in prior year financial statements.

SSAP 32 prescribes the accounting treatment and disclosures for the preparation and presentation of consolidated financial statements, and has had no major impact on the preparation of these financial statements.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

These financial statements have been prepared in accordance with Hong Kong Statements of Standard Accounting Practice, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and all of its subsidiaries for the year ended 31 December 2001.

The results of subsidiaries acquired or disposed of during the year are consolidated from or to their effective dates of acquisition or disposal, respectively. All significant inter-company transactions and balances have been eliminated on consolidation.

Subsidiaries

A subsidiary is a company whose financial and operating policies the Company controls, directly or indirectly, so as to obtain benefits from its activities.

The Company's interests in subsidiaries are stated at cost less impairment losses.

Joint venture companies

A joint venture company is a company set up by contractual arrangement, whereby the Group and other parties undertake an economic activity. The joint venture company operates as a separate entity in which the Group and the other parties have an interest.

The joint venture agreement between the venturers stipulates the capital contributions of the joint venture parties, the duration of the joint venture and the basis on which the assets are to be realised upon its dissolution. The profits and losses from the joint venture company's operations and any distributions of surplus assets are shared by the venturers, either in proportion to their respective capital contributions, or in accordance with the terms of the joint venture agreement.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Joint venture companies (continued)
A joint venture company is treated as:

(a) a subsidiary, if the Company has unilateral control over the joint venture company;

(b) a jointly-controlled entity, if the Company does not have unilateral control, but has joint control over the joint venture company;

(c) an associate, if the Company does not have unilateral or joint control, but holds generally not less than 20% of the joint venture company's registered capital and is in a position to exercise significant influence over the joint venture company; or

(d) a long term investment, if the Company holds less than 20% of the joint venture company's registered capital and has neither joint control of, nor is in a position to exercise significant influence over, the joint venture company.

Associates
An associate is a company, not being a subsidiary or a joint venture, in which the Group has a long term interest of generally not less than 20% of the equity voting rights and, over which it is in a position to exercise significant influence.

The Group's share of the post-acquisition results and reserves of associates is included in the consolidated profit and loss account and consolidated reserves, respectively. The Group's interests in associates are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting less any impairment losses. Goodwill or negative goodwill arising from the acquisition of associates, which was not previously eliminated or recognised in reserves, is included as part of the Group's interests in associates.

Goodwill
Goodwill arising on the acquisition of subsidiaries and associates represents the excess of the cost of the acquisition over the Group's share of the fair values of the identifiable assets and liabilities acquired as at the date of acquisition.

Goodwill arising on acquisition is recognised in the consolidated balance sheet as an asset and amortised on the straight-line basis over its estimated useful life of up to twenty years. In the case of associates, any unamortised goodwill is included in the carrying amount thereof, rather than as a separately identified asset on the consolidated balance sheet.

On disposal of subsidiaries and associates, the gain or loss on disposal is calculated by reference to the net assets at the date of disposal, including the attributable amount of goodwill which remains unamortised and any relevant reserves, as appropriate.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Goodwill (continued)

The carrying amount of goodwill is reviewed annually and written down for impairment where it is considered necessary. A previously recognised impairment loss for goodwill is not reversed unless the impairment loss was caused by a specific external event of an exceptional nature that was not expected to recur, and subsequent external events have occurred which have reversed the effect of that event.

Fixed assets and depreciation

Fixed assets are stated at cost less accumulated depreciation and any impairment losses. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after the asset has been put into operation, such as repairs and maintenance, is normally charged to the profit and loss account in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of the asset, the expenditure is capitalised as an additional cost of that asset.

Depreciation is calculated on the straight-line basis to write off the cost of each asset over its estimated useful life. The principal annual rates used for this purpose are as follows:

Leasehold land	Over unexpired lease terms
Leasehold buildings	2%
Plant, machinery and equipment	10% – 15%
Furniture and fixtures	10%
Moulds and tools	10%
Motor vehicles	10% – 15%

The gain or loss on disposal or retirement of a fixed asset recognised in the profit and loss account is the difference between the net sales proceeds and the carrying value of the relevant asset.

Impairment of assets

An assessment is made at each balance sheet date of whether there is any indication of impairment of any asset, or whether there is any indication that an impairment loss previously recognised for an asset in prior years may no longer exist or may have decreased. If any such indication exists, the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as the higher of the asset's value in use or its net selling price.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. An impairment loss is charged to the profit and loss account in the period in which it arises.

A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the recoverable amount of an asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation), had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is credited to the profit and loss account in the period in which it arises.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Research and development costs

All research costs are charged to the profit and loss account as incurred.

Expenditure incurred to develop new or improved materials, products or processes is capitalised to the extent that such assets will generate future economic benefits and deferred only when the projects are clearly defined; the expenditure is separately identifiable and can be measured reliably; there is reasonable certainty that the projects are technically feasible; and the products have commercial value. Product development expenditure which does not meet these criteria is expensed when incurred.

Deferred development costs are stated at cost less any impairment losses and are amortised using the straight-line basis over the commercial lives of the underlying products not exceeding two years, commencing from the date when the products are put into commercial production.

Long term investments

Long term investments in unlisted equity securities, intended to be held for a continuing strategic or long term purpose, are stated at cost less any provisions for impairments in values deemed necessary by the directors, other than those considered to be temporary in nature, on an individual basis.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on a first-in, first-out basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour and an appropriate proportion of overheads. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

Leased assets

Leases that transfer substantially all the rewards and risks of ownership of assets to the Group, other than legal title, are accounted for as finance leases. At the inception of a finance lease, the cost of the leased asset is capitalised at the present value of the minimum lease payments and recorded together with the obligation, excluding the interest element, to reflect the purchase and financing. Assets held under capitalised finance leases are included in fixed assets and are depreciated over the shorter of the lease terms and the estimated useful lives of the assets. The finance costs of such leases are charged to the profit and loss account so as to provide a constant periodic rate of charge over the lease terms.

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Group is the lessee, rentals payable under the operating leases are charged to the profit and loss account on the straight-line basis over the lease terms.

Deferred tax

Deferred tax is provided, using the liability method, on all significant timing differences to the extent it is probable that the liability will crystallise in the foreseeable future. A deferred tax asset is not recognised until its realisation is assured beyond reasonable doubt.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Foreign currencies

Foreign currency transactions are recorded at the applicable rates of exchange ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the applicable rates of exchange ruling at that date. Exchange differences are dealt with in the profit and loss account.

On consolidation, the financial statements of subsidiaries denominated in foreign currencies are translated into Hong Kong dollars at the applicable rates of exchange ruling at the balance sheet date. The resulting translation differences are included in the exchange fluctuation reserve.

Retirement benefit costs

The Group operates a defined contribution Mandatory Provident Fund retirement benefits scheme (the "MPF Scheme") under the Mandatory Provident Fund Schemes Ordinance, for those employees who are eligible to participate in the MPF Scheme. The MPF Scheme has operated since 1 December 2000. Contributions are made based on a percentage of the employees' basic salaries and are charged to the profit and loss account as they become payable in accordance with the rules of the MPF Scheme. The assets of the MPF Scheme are held separately from those of the Group in an independently administered fund. The Group's employer contributions vest fully with the employees when contributed into the MPF Scheme. Prior to the MPF Scheme being effective, the Group did not have any pension arrangements for its employees.

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

(i) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold; and

(ii) interest income, on a time proportion basis taking into account the principal outstanding and the effective interest rate applicable.

Related parties

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party, or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence. Related parties may be individuals or corporate entities.

Cash equivalents

For the purpose of the consolidated cash flow statement, cash equivalents represent short term highly liquid investments which are readily convertible into known amounts of cash and which were within three months of maturity when acquired, less advances from banks repayable within three months from the date of the advance. For the purpose of balance sheet classification, cash equivalents represent assets similar in nature to cash, which are not restricted as to use.

4. SEGMENT INFORMATION

SSAP 26 was adopted during the year, as detailed in note 2 to the financial statements. Segment information is presented by way of two segment formats: (i) on a primary segment reporting basis, by business segment; and (ii) on a secondary segment reporting basis, by geographical segment.

The Group's operating businesses are structured and managed by product segments. Each of the Group's product segments represents a strategic business unit that offers products and services which are subject to risks and returns that are different from those of other product segments. Summary details of the business segments by products are as follows:

a. the manufacture and trading of CD/VCD players and mechanisms, amplifiers, and computer peripherals;

b. the manufacture and trading of car audio mechanisms, cassette deck mechanisms and related products;

c. the manufacture and trading of personal office appliances and medical devices; and

d. the trading of Internet phone sets and provision of related services.

In determining the Group's geographical segments, revenues and results are attributed to the segments based on the location of the customers, and assets are attributed to the segments based on the location of the assets.

Intersegment sales and transfers are transacted with reference to the selling prices used for sales made to third parties at the then prevailing market prices.

4. SEGMENT INFORMATION (continued)

(a) Business segments

The following tables present revenue, results and certain assets, liabilities and expenditure information for the Group's business segments.

Group

	Manufacture and trading of CD/VCD players and mechanisms, amplifiers, and computer peripherals		Manufacture and trading of car audio mechanisms cassette deck mechanisms and related products		Manufacture and trading of personal office appliances and medical devices		Trading of Internet phone sets and provision of related services		Consolidated	
	2001	2000	**2001**	2000	**2001**	2000	**2001**	2000	**2001**	2000
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*	***HK$'000***	*HK$'000*	***HK$'000***	*HK$'000*	***HK$'000***	*HK$'000*
Segment revenue:										
Sales to external customers	**84,985**	114,746	**58,588**	111,320	**30,266**	62,847	**1,647**	–	**175,486**	288,913
Segment results	**(24,019)**	(20,959)	**(8,229)**	(10,420)	**(1,485)**	2,373	**(26,620)**	–	**(60,353)**	(29,006)
Interest income									**1,149**	939
Unallocated expenses									**(13,270)**	(9,091)
Loss from operating activities									**(72,474)**	(37,158)
Finance costs									**(3,344)**	(4,399)
Loss before tax									**(75,818)**	(41,557)
Tax									**(69)**	(1,156)
Loss before minority interests									**(75,887)**	(42,713)
Minority interests									**(310)**	(1,001)
Net loss from ordinary activities attributable to shareholders									**(76,197)**	(43,714)

4. SEGMENT INFORMATION (continued)

(a) Business segments (continued)

Group

	Manufacture and trading of CD/VCD players and mechanisms, amplifiers, and computer peripherals		Manufacture and trading of car audio mechanisms cassette deck mechanisms and related products		Manufacture and trading of personal office appliances and medical devices		Trading of Internet phone sets and provision of related services		Consolidated	
	2001	2000	**2001**	2000	**2001**	2000	**2001**	2000	**2001**	2000
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*	***HK$'000***	*HK$'000*	***HK$'000***	*HK$'000*	***HK$'000***	*HK$'000*
Segment assets	**39,406**	52,916	**32,727**	59,205	**14,193**	30,566	**8,879**	–	**95,205**	142,687
Interests in associates	**–**	–	**–**	–	**–**	–	**–**	–	**250,000**	–
Long term investments	**–**	–	**–**	–	**–**	–	**–**	–	**–**	80,000
Unallocated assets	**–**	–	**–**	–	**–**	–	**–**	–	**160,348**	68,062
Total assets									**505,553**	290,749
Segment liabilities	**9,986**	15,312	**7,696**	15,846	**3,314**	7,889	**382**	–	**21,378**	39,047
Unallocated liabilities	**–**	–	**–**	–	**–**	–	**–**	–	**50,085**	62,475
Total liabilities									**71,463**	101,522
Other segment information:										
Capital expenditure	**2,527**	3,480	**1,770**	3,485	**892**	1,890	**88**	–	**5,277**	8,855
Amortisation of goodwill	**–**	–	**–**	–	**–**	–	**5,656**	–	**5,656**	–
Provision for impairment in value of goodwill	**–**	–	**–**	–	**–**	–	**21,047**	–	**21,047**	–
Provision against inventories	**3,910**	1,733	**4,186**	2,024	**1,408**	940	**–**	–	**9,504**	4,697
Provision for impairment of fixed assets	**1,534**	591	**1,417**	690	**552**	320	**–**	–	**3,503**	1,601
Depreciation	**6,224**	6,526	**5,062**	6,672	**2,238**	3,326	**2**	–	**13,526**	16,524
Amortisation and impairment loss of deferred development costs	**2,154**	3,143	**1,538**	3,148	**776**	1,707	**–**	–	**4,468**	7,998

4. SEGMENT INFORMATION (continued)

(b) Geographical segments

The following tables present revenue, results and certain assets and expenditure information for the Group's geographical segments.

Group

	Hong Kong		PRC		Other Asian countries		Europe		America		Consolidated	
	2001	2000	**2001**	2000	**2001**	2000	**2001**	2000	**2001**	2000	**2001**	2000
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*	***HK$'000***	*HK$'000*	***HK$'000***	*HK$'000*	***HK$'000***	*HK$'000*	***HK$'000***	*HK$'000*
Segment revenue:												
Sales to external customers	**36,744**	83,614	**23,851**	43,641	**13,321**	34,936	**71,404**	59,657	**30,166**	67,065	**175,486**	288,913
Segment results	**(6,311)**	(10,309)	**(29,666)**	(3,358)	**(3,066)**	(4,340)	**(16,721)**	(8,782)	**(4,589)**	(2,217)	**(60,353)**	(29,006)
Other segment information:												
Segment assets	**66,229**	87,675	**434,092**	187,552	**604**	2,967	**3,239**	5,067	**1,389**	7,488	**505,553**	290,749
Capital expenditure	**1,501**	2,011	**3,776**	6,844	**–**	–	**–**	–	**–**	–	**5,277**	8,855

5. TURNOVER AND REVENUE

Turnover represents the net invoiced value of goods sold, after allowances for goods returned and trade discounts. An analysis of turnover and revenue is as follows:

	Group	
	2001	2000
	HK$'000	*HK$'000*
Turnover	**175,486**	288,913
Interest income	**1,149**	939
Other income	**1,502**	1,101
Other revenue	**2,651**	2,040
Total revenue	**178,137**	290,953

6. LOSS FROM OPERATING ACTIVITIES

The Group's loss from operating activities is arrived at after charging/(crediting):

	Group	
	2001	2000
	HK$'000	*HK$'000*
Cost of inventories sold	**148,880**	248,305
Provision against inventories*	**9,504**	4,697
Deferred development costs:*		
Amortisation for the year	**4,468**	6,694
Impairment arising during the year	**–**	1,304
Depreciation	**13,526**	16,524
Operating lease rentals for land and buildings	**8,995**	8,607
Less: Amount capitalised	**(229)**	(759)
	8,766	7,848
Auditors' remuneration	**780**	780
Staff costs (excluding directors' remuneration – *note 7*)**		
Salaries and wages	**30,471**	32,588
MPF Scheme Contributions	**555**	45
Less: Amount capitalised	**(524)**	(2,704)
	30,502	29,929
Provision for doubtful debts	**2,687**	3,051
Loss on disposal of fixed assets	**–**	927
Loss on disposal of a subsidiary	**–**	541
Exchange losses, net	**115**	1,030

* *Provision against inventories and the amortisation and impairment of deferred development costs for the year are included in "Cost of sales" on the face of the consolidated profit and loss account.*

** *At 31 December 2001, the Group had no forfeited contributions available to reduce its contributions to the pension scheme in future years.*

7. REMUNERATION OF DIRECTORS AND THE FIVE HIGHEST PAID INDIVIDUALS

Directors' remuneration disclosed pursuant to the Listing Rules and Section 161 of the Hong Kong Companies Ordinance is as follows:

	Group	
	2001	2000
	HK$'000	*HK$'000*
Fees	**243**	263
Basic salaries, housing, other allowances and benefits in kind	**11,141**	9,682
Bonus paid and payable	**–**	769
Mandatory provident fund contributions	**107**	7
	11,491	10,721

Fees include HK$243,000 (2000: HK$162,500) payable to the independent non-executive directors. There were no other emoluments payable to the independent non-executive directors during the year (2000: Nil). The remuneration of the directors fell within the following bands:

	Number of directors	
	2001	2000
Nil – HK$1,000,000	**7**	11
HK$1,000,001 – HK$1,500,000	**2**	2
HK$2,000,001 – HK$2,500,000	**1**	–
HK$2,500,001 – HK$3,000,000	**1**	1
HK$3,000,001 – HK$3,500,000	**–**	–
HK$3,500,001 – HK$4,000,000	**1**	1
	12	15

There were no arrangements under which a director waived or agreed to waive any remuneration during the year.

During the year, 22,800,000 share options were granted to certain directors and employees in respect of their services rendered to the Group, further details of which are set out under the heading "Share option scheme" in the Report of the Directors on pages 20 to 22. No value in respect of the share options granted during the year has been charged to the profit and loss account.

The five highest paid individuals during the year were all directors, whose remuneration is disclosed above.

8. FINANCE COSTS

	Group	
	2001	2000
	HK$'000	*HK$'000*
Interest on bank loans, overdrafts and other borrowings wholly repayable within five years	**3,181**	4,184
Interest on finance leases	**163**	215
	3,344	4,399

9. TAX

Hong Kong profits tax has been provided at the rate of 16% (2000: 16%) on the estimated assessable profits arising in Hong Kong during the year. Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the countries in which the Group operates, based on existing legislation, interpretations and practices in respect thereof.

	Group	
	2001	2000
	HK$'000	*HK$'000*
Current year's provision:		
Hong Kong	**139**	409
Elsewhere	**135**	747
Deferred – *note 25*	**(205)**	–
Tax charge for the year	**69**	1,156

10. NET LOSS FROM ORDINARY ACTIVITIES ATTRIBUTABLE TO SHAREHOLDERS

The net loss from ordinary activities attributable to shareholders for the year ended 31 December 2001 dealt with in the financial statements of the Company is HK$119,218,000 (2000: HK$43,723,000).

11. LOSS PER SHARE

The calculation of basic loss per share is based on the net loss from ordinary activities attributable to shareholders for the year of HK$76,197,000 (2000: HK$43,714,000) and the weighted average of 397,849,029 (2000: 137,237,941) ordinary shares in issue during the year.

Diluted loss per share amounts for the years ended 31 December 2001 and 31 December 2000 have not been shown as the share options outstanding during both years had an anti-dilutive effect on the basic loss per share for both years.

12. FIXED ASSETS

Group

	Leasehold land and buildings	Plant, machinery and equipment	Furniture and fixtures	Moulds and tools	Motor vehicles	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Cost:						
At beginning of year:						
As previously reported	11,113	105,171	41,129	80,696	6,812	244,921
Reclassified to accumulated depreciation and impairment *(note)*	–	–	–	1,601	–	1,601
As restated	11,113	105,171	41,129	82,297	6,812	246,522
Additions	–	920	1,149	3,208	–	5,277
At 31 December 2001	**11,113**	**106,091**	**42,278**	**85,505**	**6,812**	**251,799**
Accumulated depreciation and impairment:						
At beginning of year:						
As previously reported	2,815	84,984	33,478	44,019	4,861	170,157
Reclassified from cost	–	–	–	1,601	–	1,601
As restated	2,815	84,984	33,478	45,620	4,861	171,758
Provided during the year	213	5,775	1,415	5,697	426	13,526
Impairment during the year recognised in the profit and loss account	–	–	–	3,503	–	3,503
At 31 December 2001	**3,028**	**90,759**	**34,893**	**54,820**	**5,287**	**188,787**
Net book value:						
At 31 December 2001	**8,085**	**15,332**	**7,385**	**30,685**	**1,525**	**63,012**
At 31 December 2000	8,298	20,187	7,651	36,677	1,951	74,764

Note: Accumulated impairment losses are aggregated with accumulated depreciation under the revised disclosure requirements of SSAP 17, as detailed in note 2 to the financial statements, whereas previously they were disclosed as an adjustment to the cost of the assets. This change has been disclosed as a retrospective reclassification.

12. FIXED ASSETS (continued)

Company

	Furniture and fixtures *HK$'000*
Cost:	
Additions during the year and at 31 December 2001	53
Accumulated depreciation:	
Charged for the year and at 31 December 2001	(5)
Net book value:	
At 31 December 2001	**48**
At 31 December 2000	–

The net book value of assets held under finance leases as at 31 December 2001 included motor vehicles of HK$1,070,000 (2000: HK$2,822,000).

The Group's leasehold land and buildings are held under medium term leases and are situated in Hong Kong.

The Group's leasehold land and buildings are pledged to secure the Group's bank loans (note 23).

A provision for impairment in value of HK$3,503,000 (2000: HK$1,601,000) was made during the year as the recoverable amount of certain moulds and tools declined below their carrying amount.

13. INTANGIBLE ASSETS

	Group Deferred development costs HK$'000
Cost:	
At beginning of year and at 31 December 2001	26,259
Accumulated amortisation and impairment:	
At beginning of year	20,706
Provided during the year – *note 6*	4,468
At 31 December 2001	25,174
Net book value:	
At 31 December 2001	**1,085**
At 31 December 2000	5,553

14. GOODWILL

SSAP 30 was adopted during the year, as detailed in note 2 to the financial statements. The amount of the goodwill capitalised as an asset, arising from the acquisition of subsidiaries, is as follows:

	Group
Cost:	
Acquisition of subsidiaries during the year and at 31 December 2001	33,935
Accumulated amortisation and impairment:	
Amortisation provided during the year	5,656
Impairment provided during the year *(note)*	21,047
At 31 December 2001	26,703
Net book value:	
At 31 December 2001	**7,232**
At 31 December 2000	–

14. GOODWILL (continued)

Note: The impairment losses have been provided for the goodwill arising from the acquisition of subsidiaries namely, Kongnet Group Limited ("Kongnet") and Tianjin Weikang Communication Company Limited ("Tianjin Weikang"), during the year (notes 15 and 28(b)). The impairment losses are estimated by the directors based on the recoverable amount of the goodwill, which is the value in use determined by discounting the future net cash inflows estimated to arise from the relevant cash-generating units. In the opinion of the directors, such impairment losses have arisen from the prevailing unfavourable economic environment in the Internet phone business. Further details of the acquisition of these subsidiaries are set out in notes 26(a) and 28(b) to the financial statements.

15. INTERESTS IN SUBSIDIARIES

	Company	
	2001	2000
	HK$'000	*HK$'000*
Unlisted shares/capital contributions, at cost	**94,687**	94,687
Due from subsidiaries	**462,025**	148,944
	556,712	243,631
Provisions for impairment	**(190,248)**	(74,974)
	366,464	168,657

The amounts due are unsecured, interest-free and are not repayable within the twelve months following the balance sheet date.

Particulars of the Company's principal subsidiaries are as follows:

Name	**Place of incorporation/ registration and operations**	**Nominal value of issued ordinary/ registered and paid-up capital**	**Percentage of equity attributable to the Company**		**Principal activities**
			Direct	**Indirect**	
Yanion (BVI) Limited	British Virgin Islands	HK$370,000	100	–	Investment holding
Yacata Limited	British Virgin Islands	US$1	100	–	Investment holding
Kongnet Group Limited *(note)*	British Virgin Islands	US$1	100	–	Investment holding

15. INTERESTS IN SUBSIDIARIES (continued)

Name	Place of incorporation/ registration and operations	Nominal value of issued ordinary/ registered and paid-up capital	Percentage of equity attributable to the Company Direct	Indirect	Principal activities
Tianjian Weikang Communication Company Limited *(note)*	People's Republic of China	US$160,000	–	90	Sales of Internet phone sets and provision of related services
Yanion Company Limited	Hong Kong	HK$31,202,370	–	100	Trading of cassette deck mechanisms, CD/VCD mechanisms and players, amplifiers and related products, personal office appliances and medical devices
Chia Neng Spring (HK) Limited	Hong Kong	HK$1,350,000	–	77.78	Manufacture and trading of precision springs
Dongguan Yanion Electronics Manufacturing Limited	People's Republic of China	HK$155,000,000	–	100	Manufacture and trading of cassette deck mechanisms, CD/VCD mechanisms and players, amplifiers and related products, personal office appliances and medical devices
Dongguan Yanion Mould & Die Manufacturing Limited	People's Republic of China	HK$21,499,997	–	100	Manufacture and trading of precision moulds and dies

The above table lists the subsidiaries of the Company as at 31 December 2001 which, in the opinion of the directors, principally affected the results for the year or formed a substantial portion of the net assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

15. INTERESTS IN SUBSIDIARIES (continued)

Note:

On 21 February 2001, the Group acquired a 100% equity interest in Kongnet from an independent third party at a consideration of HK$35 million. The principal asset of Kongnet is its 90% equity interest in a sino-foreign enterprise, Tianjian Weikang, which is engaged in the Internet phone business in the PRC.

Kongnet and Tianjin Weikang had no material transactions since the date of their acquisitions to 31 December 2001. The Group's interest in Kongnet was principally reflected as goodwill arising on the acquisition of approximately HK$34 million, and the details of which are set out in notes 14 and 28(b) to the financial statements.

16. INTERESTS IN ASSOCIATES

	Group	
	2001	2000
	HK$'000	*HK$'000*
Unlisted shares, at cost	**250,000**	–

Particulars of the associate at 31 December 2001 are as follows:

Company	Business structure	Place of incorporation and operations	Percentage of equity attributable to the Group 2001	2000	Principal activities
Global Cyber Limited*# ("Global Cyber")	Corporation	British Virgin Islands	**27**	10	Investment holding

The underlying investment of Global Cyber is:

Company	Business structure	Place of incorporation and operations	2001	2000	Principal activities
Shanghai Dazheng Worldvest Technology Company Limited* ("Shanghai Dazheng")	Corporation	People's Republic of China	**21.6**	–	Provision of research & development of video-on-demand systems

* Not audited by Ernst & Young Hong Kong or other Ernst & Young International member firms.

\# The associate has been accounted for at cost in the Group consolidated financial statements.

Note:

Included in the consolidated balance sheet as at 31 December 2001 is a 27% equity interest in an associate, Global Cyber, with a carrying amount of HK$250 million. As set out in note 17 to the financial statements, in 2000 the Group originally acquired an initial 10% equity interest in Global Cyber from Majestic Star Holdings Limited ("Majestic Star"), for HK$80 million. The acquisition was recorded as a long term investment in the prior year's consolidated balance sheet.

16. INTERESTS IN ASSOCIATES (continued)

During the year, pursuant to a sale and purchase agreement dated 29 March 2001, the Group acquired an additional 4% equity interest in Global Cyber from Majestic Star for a cash consideration of HK$40 million (the "4% Global Cyber Interest"). At the date of entering into the agreement, one of the executive directors of the Company was also a director of Majestic Star, as a result of which the acquisition of the 4% Global Cyber Interest constituted a related party transaction. The consideration for the 4% Global Cyber Interest was arrived at having regard to another transaction which occurred at around the same time with an independent third party. On 31 March 2001, the executive director of the Company ceased to be a director of Majestic Star, but remained a signing officer thereof.

On 18 July 2001, the Group acquired further 10% and 3% equity interests in Global Cyber from Majestic Star and Great Web Holdings Limited, respectively, for cash considerations of HK$100 million and HK$30 million, respectively, pursuant to a sale and purchase agreement entered into between the Group and each of the parties on that date.

As a result, the Group's interest in Global Cyber increased from 10% to 27% and Global Cyber became an associated company of the Group. The Group's interest in Global Cyber has been accounted for at its total cost of acquisition of HK$250 million in the consolidated balance sheet as at 31 December 2001.

Global Cyber is an investment holding company. The principal asset of Global Cyber is its 80% equity interest in Shanghai Dazheng, a sino-foreign joint venture established in the PRC. Pursuant to the terms of the joint venture agreement dated 16 December 1999, the PRC party to the Shanghai Dazheng joint venture (the "PRC Party") is required to contribute its video-on-demand ("VOD") technology as part of its capital contribution in exchange for its 20% equity interest in Shanghai Dazheng. The principal activities of Shanghai Dazheng are the research and development of VOD systems in the PRC which involves the re-engineering of existing cable TV stations in the PRC by employing related operating software, servers and set-top boxes.

In October 2001, the directors of Global Cyber and the Company became aware that the PRC Party had applied to the State Intellectual Property Office of the PRC for the registration of a VOD chip in its own name, which the directors believe to have been developed based on Shanghai Dazheng's VOD technology. The directors of Global Cyber consider that such registration may infringe the intellectual property rights of the Shanghai Dazheng VOD technology, and they communicated to the PRC Party their concern and disapproval of the situation. Attempts were made to clarify the ownership rights and legal title to the VOD technology and whether the PRC Party's application to the patent office infringed the intellectual property rights and commercial interests of Shanghai Dazheng. The matter was and remains disputed by the PRC Party. As the relationship with the PRC Party deteriorated, the books and records in respect of Shanghai Dazheng have not been made available for examination by the directors of Global Cyber. The directors of Global Cyber and the Company are now seeking advice from PRC legal counsel as to the appropriate course of action, including arbitration and/or the legal action that should be taken. However, at the date of approval of these financial statements, the directors of the Company are not in a position either (i) to equity account for this investment; or (ii) to quantify the outcome and the effect of such dispute including any resultant impairment provision that may be required against the carrying amount of the associate of the Group as at 31 December 2001.

17. LONG TERM INVESTMENTS

	Group	
	2001	2000
	HK$'000	*HK$'000*
Unlisted equity investments, at cost	**1,000**	81,000

A long term investment with a carrying amount of HK$1,000,000 was pledged to secure an other borrowing of HK$800,000 granted to the Group as at 31 December 2000 (note 23). The other borrowing was fully repaid during the year.

Included in the prior year's balance was an investment in Global Cyber of HK$80,000,000. As at 31 December 2000, the Group held 100,000 ordinary shares in Global Cyber, which represented a 10% equity interest. During the year, the Group increased its equity interest in Global Cyber from 10% to 27% through two additional purchases. Global Cyber then ceased to be a long term investment and became an associate of the Group. Further details of the acquisitions during the year and this investment are set out in note 16 to the financial statements.

In the opinion of the directors, there has been no impairment loss on the carrying value of the long term investment as at 31 December 2001.

18. DEPOSITS

The deposits comprise sums paid to two separate independent third parties during the year, amounting to HK$101.5 million (2000: Nil). These amounts represent in substance advance payments in respect of acquisition agreements subsequently entered into by the Group with the independent parties as described below.

(a) Pursuant to the terms of a loan agreement dated 18 September 2001 entered into between the Group and Korning Investments Limited ("Korning"), a HK$90 million payment (the "Korning Deposit") was made to an independent third party via Majestic Star, under the instruction of the vendor of Korning (the "Korning Vendor"), which payment was intended to secure the investment in a pharmaceutical joint venture in the PRC. The Korning Deposit was interest-free, unsecured and repayable within six months from the date of the agreement if the Korning Vendor proved to be unable to secure the pharmaceutical joint venture investment for the Group on satisfactory terms. The repayment date for the Korning Deposit was subsequently extended to 15 August 2002 by mutual agreement.

Subsequent to the balance sheet date on 2 January 2002 and 11 April 2002, the Group entered into a conditional sale and purchase agreement with the Korning Vendor for acquisition of an 87% equity interest in Korning (the "Korning Acquisition") at a total consideration of HK$99.84 million, using the Korning Deposit to offset part of the consideration. Further details of the Korning Acquisition are set out in note 33(a) to the financial statements.

18. DEPOSITS (continued)

(b) Pursuant to the terms of a loan agreement dated 29 October 2001 entered into between the Group and Modern Capital Overseas Limited, an independent third party, an aggregate amount of HK$11.5 million was advanced to the vendor of Modern Vocal Limited (the "Modern Vocal Vendor"). The advance was unsecured, bore interest at the rate of 5% per annum and was repayable within six months from the date of the advancement.

On 19 December 2001, the Group entered into a conditional sale and purchase agreement with the Modern Vocal Vendor to acquire a 60% equity interest in Modern Vocal Limited ("Modern Vocal") at a total consideration of HK$13.5 million (the "Modern Vocal Acquisition"). On the same day, it was further agreed with the Modern Vocal Vendor to set off the 29 October 2001 advance against the purchase consideration payable by the Group pursuant to the Modern Vocal Acquisition. As at 31 December 2001, the remaining balance of HK$2 million payable for the Modern Vocal Acquisition is disclosed as a capital commitment in note 31 to the financial statements and the amount was subsequently paid by the Group in February and March 2002, following which the Modern Vocal Acquisition was completed on 22 March 2002.

19. INVENTORIES

	Group	
	2001	2000
	HK$'000	*HK$'000*
Raw materials	**17,044**	36,027
Work in progress	**3,681**	4,850
Finished goods	**7,351**	8,956
	28,076	49,833

The amount of inventories carried at net realisable value included in the above balance was HK$4,475,000 (2000: HK$661,000) at the balance sheet date.

20. ACCOUNTS RECEIVABLE

The Group maintains a defined credit policy and allows credit periods ranged from 15 to 90 days to its trade customers. The Group seeks to maintain strict control over its outstanding receivables. Overdue balances are reviewed and monitored by senior management.

An aged analysis of the accounts receivable as at the balance sheet date, based on payment due date, and net of provisions is as follows:

	Group	
	2001	2000
	HK$'000	*HK$'000*
Within 1 month	**5,551**	12,410
2 to 3 months	**3,565**	10,227
4 to 6 months	**459**	2,586
7 to 12 months	**–**	1,190
Over 1 year	**–**	2,073
	9,575	28,486

21. CASH AND CASH EQUIVALENTS AND PLEDGED DEPOSITS

	Group		**Company**	
	2001	2000	**2001**	2000
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*
Cash and bank balances	**26,421**	27,654	**24,663**	21,210
Time deposits	**13,839**	13,370	**–**	–
	40,260	41,024	**24,663**	21,210
Less: Pledged time deposits for trust receipt and export loans and bank overdraft facilities – note 23	**(13,839)**	(13,370)	**–**	–
Cash and cash equivalents	**26,421**	27,654	**24,663**	21,210

22. ACCOUNTS PAYABLE

An aged analysis of the accounts payable as at the balance sheet date, based on payment due date, is as follows:

	Group	
	2001	2000
	HK$'000	*HK$'000*
Within 1 month	**5,777**	12,695
2 to 3 months	**9,545**	20,010
4 to 6 months	**3,604**	4,554
7 to 12 months	**504**	350
Over 1 year	**1,848**	1,438
	21,278	39,047

23. INTEREST-BEARING BANK LOANS AND OTHER BORROWINGS

	Group		Company	
	2001	2000	**2001**	2000
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*
Bank overdrafts, secured	**917**	442	**–**	–
Bank loans, secured	**25,904**	30,583	**–**	–
	26,821	31,025	**–**	–
Other borrowings:				
Secured	**–**	800	**–**	800
Unsecured	**1,250**	2,000	**–**	–
	1,250	2,800	**–**	800
	28,071	33,825	**–**	800
Bank overdrafts repayable within one year or on demand	**917**	442	**–**	–
Bank loans repayable:				
Within one year	**24,104**	30,583	**–**	–
In the second year	**1,658**	–	**–**	–
In the third to fifth years, inclusive	**142**	–	**–**	–
	25,904	30,583	**–**	–
Other borrowings repayable within one year	**1,250**	2,800	**–**	800
	28,071	33,825	**–**	800
Portion classified as current liabilities	**(26,271)**	(33,825)	**–**	(800)
Long term portion	**1,800**	–	**–**	–

The above bank loans are secured by the following:

(i) a fixed charge on the Group's leasehold land and buildings in Hong Kong with a net book value of HK$8,085,000 (2000: HK$8,298,000); and

(ii) a fixed charge on the Group's pledged time deposits of HK$13,839,000 (2000: HK$13,370,000) (note 21).

23. INTEREST-BEARING BANK LOANS AND OTHER BORROWINGS (continued)

In the prior year, the other borrowings were secured by the Group's long term investment of HK$1,000,000 (note 17). The other borrowings bore interest at the prevailing prime rate and were repaid in full during the year.

Included in bank loans above, is a total of HK$17,530,000 (2000: HK$29,535,000) trust receipt and export loans and a term loan of HK$3,374,000 (2000: Nil) with maturity dates of over three months. The remaining balance of HK$5,000,000 (2000: HK$1,048,000) is repayable within three months from the date of advance.

24. FINANCE LEASE PAYABLES

The Group leases certain of its motor vehicles for its general business purposes. These leases are classified as finance leases and have remaining lease terms of two years.

At 31 December 2001, the total future minimum lease payments under finance leases and their present values, were as follows:

Group

	Minimum lease payments 2001 *HK$'000*	Minimum lease payments 2000 *HK$'000*	**Present value of minimum lease payments 2001 *HK$'000***	Present value of minimum lease payments 2000 *HK$'000*
Amounts payable:				
Within one year	**356**	822	**332**	659
In the second year	**355**	356	**293**	332
In the third to fifth years, inclusive	**–**	355	**–**	293
Total minimum finance lease payments	**711**	1,533	**625**	1,284
Future finance charges	**(86)**	(249)		
Total net finance lease payables	**625**	1,284		
Portion classified as current liabilities	**(332)**	(659)		
Long term portion	**293**	625		

SSAP 14 was revised and implemented during the year, as detailed in note 2 to the financial statements. Certain new disclosures are required and have been included above. The prior year comparative amounts for the new disclosures have also been included where appropriate.

25. DEFERRED TAX

	Group	
	2001	2000
	HK$'000	*HK$'000*
At beginning of year	**341**	341
Credit for the year – note 9	**(205)**	–
At 31 December 2001	**136**	341

The principal components of the Group's provision for deferred tax, and net deferred tax asset position not recognised in the financial statements are as follows:

	Provided		Not Provided	
	2001	2000	**2001**	2000
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*
Accelerated capital allowances	**136**	341	**3,499**	4,640
Tax losses	**–**	–	**(30,045)**	(25,146)
	136	341	**(26,546)**	(20,506)

The Company had no unprovided deferred tax at the balance sheet date (2000: Nil).

26. SHARE CAPITAL

Shares

	2001	2000
	HK$000	*HK$'000*
Authorised:		
1,000,000,000 (2000: 500,000,000) ordinary shares of HK$0.50 each	**500,000**	250,000
Issued and fully paid:		
520,750,673 (2000: 228,750,673) ordinary shares of HK$0.50 each	**260,375**	114,375

26. SHARE CAPITAL (continued)

During the year, the following changes in the Company's authorised and issued share capital took place:

Pursuant to an ordinary resolution passed at a special general meeting on 30 January 2001, the authorised share capital of the Company was increased from HK$250,000,000 to HK$500,000,000 by the creation of 500,000,000 new ordinary shares of HK$0.50 each, ranking pari passu in all respects with the then existing ordinary shares of the Company.

The movements in the issued share capital of the Company during the year were as follows:

	Notes	Number of ordinary shares	Share capital HK$'000
At beginning of year		228,750,673	114,375
Issue of new ordinary shares	*(a)*	269,200,000	134,600
Exercise of share options	*(b)*	22,800,000	11,400
At 31 December 2001		520,750,673	260,375

Notes:

(a) On 7 February 2001, the Company placed through Dao Heng Securities Limited ("Dao Heng") a total of 45,600,000 new ordinary shares with a par value of HK$0.50 each in the Company to independent investors at a consideration of HK$0.68 per placing share. At the date of entering into the placing agreement, the Company's share price was HK$0.70 per share. The corresponding issue and allotment of new shares was completed on 21 February 2001. The excess of the share consideration over the nominal value of the issued shares of HK$8,208,000 was credited to the share premium account (note 27). The net proceeds from the placing of HK$30.6 million, were used to finance the acquisition of a 100% equity interest in Kongnet, a company incorporated in the British Virgin Islands, the details of which are set out in notes 15 and 28(b) to the financial statements.

On 12 March 2001, the Company, through Dao Heng, proposed to place a total of 200,000,000 new ordinary shares with a par value of HK$0.50 each in the Company to independent investors at a consideration of HK$1.25 per placing share. At the date of entering into the placing agreement, the Company's share price was HK$1.20 per share. On 25 May 2001, the Company announced that only 137,600,000 new ordinary shares were actually issued to independent investors and the net proceeds from the placing amounted to HK$170.1 million. The excess of the share consideration over the nominal value of the issued shares of HK$103,200,000 was credited to the share premium account (note 27). All net proceeds were used for acquisition of additional equity interest in Global Cyber during the year, the details of which are set out in note 16 to the financial statements.

On 23 August 2001, the Company placed through Dao Heng a total of 86,000,000 new ordinary shares with a par value of HK$0.50 each in the Company to independent investors at a consideration of HK$1.26 per placing share. At the date of entering into the placing agreement, the Company's share price was HK$1.41 per share. The corresponding issue and allotment of new shares was completed on 10 September 2001. The excess of the share consideration over the nominal value of the issued shares of HK$65,360,000 was credited to the share premium account (note 27). The net proceeds from the placing of HK$107.3 million were used as general working capital and future investment projects for the Group.

26. SHARE CAPITAL (continued)

(b) On 6 February 2001, a total of 22,800,000 share options were granted to certain directors and employees at an exercise price of HK$0.61 per share, which entitled the option holders to subscribe for shares in the Company at any time during the period from 26 February 2001 to 25 February 2002. As at 31 December 2001, all of these share options were exercised and the corresponding 22,800,000 new ordinary shares were allotted and issued, and the details of which are set out below. The excess of the share consideration over the nominal value of the issued shares of HK$2,508,000 was credited to the share premium account (note 27).

There were no changes to the carrying amount or number of ordinary shares in issue during the prior year.

Share options

The Company operates a share option scheme (the "Scheme"), further details of which are set out under the heading "Share option scheme" in the Report of the Directors on pages 20 to 22.

Owing to the amendments to Chapter 17 of the Listing Rules, which came into effective on 1 September 2001, subsequent to the balance sheet date an amended share option scheme was adopted and approved by the shareholders of the Company at a special general meeting held on 7 June 2002 (the "New Scheme"). The terms of the New Scheme comply with the amended Chapter 17 of the Listing Rules.

Movements in share options during the year were as follows:

	Notes	**Number of share options**
Share options outstanding at beginning of year		3,970,000
Share options granted and accepted during the year	*(i)*	22,800,000
Share options exercised	*(i)*	(22,800,000)
Share options lapsed and expired	*(ii)*	(3,970,000)
Share options outstanding at end of year		–

Notes:

(i) On 6 February 2001, the Company granted a total of 22,800,000 share options for a consideration of HK$1.00 per grantee which entitled the holders to subscribe for shares of the Company at any time during the period from 26 February 2001 to 25 February 2002. The subscription price payable upon the exercise of each option was HK$0.61, subject to adjustment. These share options granted were exercised in full in three tranches of 19,100,000, 1,000,000 and 2,700,000 share options on 26 February 2001, 2 March 2001, and 7 March 2001, respectively, and resulted in the issue and allotment of 22,800,000 new ordinary shares in the Company of HK$0.50 each for a total cash consideration of HK$13,908,000.

(ii) 3,970,000 options granted in the prior year lapsed and expired on 25 October 2001.

27. RESERVES

	Share premium account HK$'000	Contributed surplus HK$'000	Exchange fluctuation reserve HK$'000	Accumulated losses HK$'000	Total HK$'000
Group					
At 1 January 2000	55,796	33,474	198	(12,112)	77,356
Issue of new shares	41,940	–	–	–	41,940
Share issue expenses	(2,516)	–	–	–	(2,516)
Net loss for the year	–	–	–	(43,714)	(43,714)
At 31 December 2000 and 1 January 2001	95,220	33,474	198	(55,826)	73,066
Issue of new shares	179,276	–	–	–	179,276
Share issue expenses	(3,301)	–	–	–	(3,301)
Net loss for the year	–	–	–	(76,197)	(76,197)
At 31 December 2001	**271,195**	**33,474**	**198**	**(132,023)**	**172,844**
Retained by:					
Company and subsidiaries					
At 31 December 2001	**271,195**	**33,474**	**198**	**(132,023)**	**172,844**
Company and subsidiaries					
At 31 December 2000	95,220	33,474	198	(55,826)	73,066

Note: No goodwill/negative goodwill remains eliminated against reserves at the balance sheet date.

27. RESERVES (continued)

	Share premium account HK$'000	Contributed surplus HK$'000	Accumulated losses HK$'000	Total HK$'000
Company				
At 1 January 2000	55,796	76,838	(55,293)	77,341
Issue of new shares	41,940	–	–	41,940
Share issue expenses	(2,516)	–	–	(2,516)
Net loss for the year	–	–	(43,723)	(43,723)
At 31 December 2000 and 1 January 2001	95,220	76,838	(99,016)	73,042
Issue of new shares	179,276	–	–	179,276
Share issue expenses	(3,301)	–	–	(3,301)
Net loss for the year	–	–	(119,218)	(119,218)
At 31 December 2001	**271,195**	**76,838**	**(218,234)**	**129,799**

The Company's contributed surplus is derived from the difference between the fair value of the shares of the subsidiaries acquired and the nominal value of the Company's shares issued in exchange therefor pursuant to the Group reorganisation in 1991. Under the Companies Act 1981 of Bermuda, a company may make distributions to its members out of its contributed surplus under certain circumstances.

The Group's contributed surplus is derived from the difference between the nominal value of the Company's shares issued pursuant to the same reorganisation and the nominal value of the shares acquired.

28. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

(a) Reconciliation of loss from operating activities to net cash inflow/(outflow) from operating activities:

	Group	
	2001	2000
	HK$000	*HK$'000*
Loss from operating activities	**(72,474)**	(37,158)
Provision against inventories	**9,504**	4,697
Provision for doubtful debts	**2,687**	3,051
Provision for impairment in value of fixed assets	**3,503**	1,601
Provision for impairment in value of goodwill	**21,047**	–
Interest income	**(1,149)**	(939)
Depreciation	**13,526**	16,524
Amortisation of deferred development costs	**4,468**	7,998
Amortisation of goodwill	**5,656**	–
Loss on disposal of a subsidiary	**–**	541
Loss on disposal of fixed assets	**–**	927
Decrease in inventories	**12,492**	15,152
Decrease in accounts receivable	**17,344**	2,309
Decrease/(increase) in prepayments and other receivables	**8,613**	(4,278)
Decrease in accounts payable	**(17,769)**	(10,317)
Decrease in other payables and accruals	**(8,230)**	(330)
Increase in amounts due to related companies	**91**	531
Increase/(decrease) in trust receipt and export loans with maturity over three months	**(12,005)**	3,364
Net cash inflow/(outflow) from operating activities	**(12,696)**	3,673

28. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (continued)

(b) Acquisition of subsidiaries:

	Group	
	2001	2000
	HK$000	*HK$'000*
Net asset acquired of:		
Cash and bank balances	**10**	–
Accounts receivable	**1,120**	–
Inventories	**2,576**	–
Other payables and accruals	**(2,523)**	–
Minority interests	**(118)**	–
	1,065	–
Goodwill on acquisition	**33,935**	–
	35,000	–
Satisfied by:		
Cash consideration	**35,000**	–

An analysis of the net outflow of cash and cash equivalents in respect of the acquisition of subsidiaries is as follows:

	Group	
	2001	2000
	HK$000	*HK$'000*
Cash consideration	**(35,000)**	–
Cash and bank balances acquired	**10**	–
Net outflow of cash and cash equivalents in respect of the acquisition of subsidiaries	**(34,990)**	–

On 21 February 2001, the Group acquired a 100% equity interest in Kongnet from an independent third party for a consideration of HK$35 million. The principal asset of Kongnet is its 90% equity interest in a Sino-foreign enterprise, Tianjin Weikang. The details of the acquisition are set out in note 15 to the financial statements.

Since the acquisition of Kongnet and Tianjin Weikang, their cash flows from operating activities contributed to the Group during the year were not significant and the effect of the results of these acquired subsidiaries on the Group's result was not material.

28. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (continued)

(c) Disposal of a subsidiary:

	Group	
	2001	2000
	HK$000	*HK$'000*
Net asset disposed of:		
Fixed assets, at net book value	–	12,188
Loss on disposal of a subsidiary	–	(541)
	–	11,647
Satisfied by:		
Cash proceeds	–	11,647

The cash flows contributed and utilised by the subsidiary disposed of in the prior year were not significant and the effect of the subsidiary disposed of on the results in the prior year was not material.

28. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (continued)

(d) Analysis of changes in financing during the year:

	Issued capital, (including share premium account) HK$'000	Finance lease payables HK$'000	Bank and other borrowings HK$'000	Minority interests HK$'000
At 1 January 2000	104,971	2,046	4,000	1,565
Net cash inflow/(outflow) from financing	104,624	(762)	(1,200)	–
Share of net profit for the year	–	–	–	1,001
Dividends paid to minority shareholders	–	–	–	(780)
At 31 December 2000 and 1 January 2001	209,595	1,284	2,800	1,786
Net cash inflow/(outflow) from financing	321,975	(659)	1,824	7
Share of net profit for the year	–	–	–	310
Arising from acquisition of subsidiaries	–	–	–	118
Dividends paid to minority shareholders	–	–	–	(1,350)
At 31 December 2001	**531,570**	**625**	**4,624**	**871**

29. CONTINGENT LIABILITIES

	Group		Company	
	2001	2000	**2001**	2000
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*
Guarantees given to banks in connection with facilities granted to subsidiaries	**–**	–	**50,000**	50,000
Bills discounted with recourse	**2,421**	13,724	**–**	–
	2,421	13,724	**50,000**	50,000

As at 31 December 2001, credit facilities utilised by the subsidiaries under the Company's guarantee amounted to HK$30,493,000 (2000: HK$47,755,000).

30. OPERATING LEASE ARRANGEMENTS

At 31 December 2001, the Group had total future minimum lease payments under non-cancellable operating leases in respect of its land and buildings falling due as follows:

	Group	
	2001	2000
	HK$'000	*HK$'000*
		(Restated)
Within one year	**10,116**	9,999
In the second to fifth years, inclusive	**17,894**	30,103
	28,010	40,102

SSAP 14 (Revised) requires lessees under operating leases to disclose the total future minimum operating lease payments, rather than only the payments to be made during the next year as was previously required. Accordingly, the prior year comparative amounts for operating leases as lessee, have been restated to accord with the current year's presentation.

The Company did not have any operating lease commitments at the balance sheet date (2000: Nil).

31. CAPITAL COMMITMENTS

	Group	
	2001	2000
	HK$000	*HK$'000*
Contracted, but not provided for:		
Acquisition of a subsidiary *(note 18)*	**2,000**	–

The Company did not have any capital commitments at the balance sheet date (2000: Nil).

32. CONNECTED AND RELATED PARTY TRANSACTIONS

In addition to the related party transaction disclosed in note 16 to the financial statements, set out below are the other related party transactions disclosed in accordance with SSAP 20 issued by the Hong Kong Society of Accountants. The transactions disclosed below also constituted connected transactions under the Listing Rules.

		Group	
		2001	2000
	Notes	***HK$000***	*HK$'000*
Purchases of raw materials from a related company:			
Simple Link Company Limited ("Simple Link")	*(a)*	**920**	1,426
Rental expenses paid to related companies:			
Bestbond Company Limited	*(b)*	**1,650**	1,913
Well Hero Industrial Limited	*(b)*	**216**	216
Kamga Investment Limited	*(b)*	**216**	216
WorldVest Capital Limited	*(b)*	**871**	–
Rental expenses paid to a director:			
Leung Wah Chai	*(b)*	**720**	732
Consultancy fees paid/payable to a related company:			
WorldVest Capital Limited	*(c)*	**900**	900

(a) The directors consider that the purchases of raw materials were made at prices and on conditions similar to those offered by other independent suppliers of the Group. The balance due to Simple Link at 31 December 2001 amounted to HK$245,000 (2000: HK$210,000). The balance due is unsecured, interest-free and has no fixed terms of repayment.

In a special general meeting of the Company held on 30 November 1995, two ordinary resolutions were passed whereby the Group's purchases of lathe parts (the "Purchases") from Simple Link, a company of which Leung Wah Chai was a director and controlling shareholder for the period from 1 January 1992 up to 30 November 1995, were approved, ratified and confirmed. In addition, it was stipulated that the aggregate amount of the Purchases for the year ended 31 December 1995 and for each subsequent financial year should not exceed 3% of the annual purchases of the Group.

The independent non-executive directors of the Company have reviewed the Purchases for the year ended 31 December 2001 and confirmed to the board that, in their opinion, the Purchases have been conducted in the ordinary and usual course of the Group's business and were fair and reasonable so far as the shareholders of the Company were concerned, and that the aggregate value of the Purchases did not exceed 3% of the total purchases of the Group for the year then ended.

32. CONNECTED AND RELATED PARTY TRANSACTIONS (continued)

(b) The rental expenses related to properties rented for the purpose of providing quarters to the directors and for office purposes, and were charged in accordance with the terms of the related rental agreements. The balance due to WorldVest Capital Limited at 31 December 2001 was HK$308,000 (2000: Nil). The balance is unsecured, interest-free and has no fixed terms of repayment.

(c) The consultancy fees were charged in accordance with the terms of the service agreement. The balance due to WorldVest Capital Limited at 31 December 2001 was HK$450,000 (2000: HK$702,000). The balance due is unsecured, interest-free and has no fixed terms of repayment.

Leung Wah Chai is a director and controlling shareholder of Simple Link and Bestbond Company Limited. Leung Wah Chai and Butt Wing Han are directors and controlling shareholders of Well Hero Industrial Limited and Kamga Investment Limited. Cheng Shu Wing, Guo Duen How, Tom and Wu Fred Fong are the directors of WorldVest Capital Limited.

33. POST BALANCE SHEET EVENTS

(a) On 2 January 2002, the Group entered into a conditional sale and purchase agreement (the "Korning Acquisition Agreement") with an independent third party ("the Korning Vendor") for the acquisition of the entire issued share capital in Korning Investments Limited ("Korning"), a company incorporated in the British Virgin Islands, for a cash consideration of US$12.8 million (equivalent to HK$99.84 million) (the "Korning Purchase Consideration"). The only asset of Korning is its 100% equity interest in Star Wisdom Limited ("Star Wisdom"), a company incorporated in the British Virgin Islands. Star Wisdom intended to establish a sino-foreign pharmaceutical joint venture (the "Pharmaceutical JV") with an original registered share capital of RMB40 million with Huahe Pharmaceutical Company Limited ("Huahe"), an independent pharmaceutical enterprise in the PRC and a subsidiary of China National Group Corporation of Traditional Herbal and Medicine (the "China National Medicine"). Through the acquisition of such a joint venture, the Group intends to secure certain operating assets and rights for the development of the pharmaceutical business in the PRC. The completion of the Korning Acquisition was conditional upon, inter-alia, Star Wisdom entering into the Pharmaceutical JV with terms satisfactory to the Group.

33. POST BALANCE SHEET EVENTS (continued)

(a) (continued)

On 10 April 2002, Star Wisdom entered into a joint venture agreement and the respective articles of association with Huahe for the establishment of the Pharmaceutical JV. Pursuant to the terms of the joint venture agreement, the total investment and registered capital of the Pharmaceutical JV were revised from RMB40 million to RMB126 million. Huahe would contribute to the Pharmaceutical JV RMB50.4 million worth of tangible and intangible assets, including all approvals, licences and other intellectual properties, machinery and equipment relating to four Chinese herbal medicines. Star Wisdom would contribute RMB75.6 million in two cash instalments. The first instalment of RMB11.34 million was to be payable within one month after the issue date of the business licence of the Pharmaceutical JV and the second instalment of RMB64.26 million was to be payable within six months after the issue date of the business licence. On the same date, Star Wisdom and Huahe entered into a shareholders' agreement whereby Huahe agreed to transfer all the intellectual properties of an additional twelve medicines to the Pharmaceutical JV upon its establishment at a further consideration of RMB15 million. The consideration is payable by the Pharmaceutical JV to Huahe in two instalments. The first instalment of RMB5 million is payable within three days after the first capital contribution made by Star Wisdom and the balance of RMB10 million is payable within three days after the final capital contribution made by Star Wisdom. The ultimate holding companies of both parties, China National Medicine and the Company have also signed letters of undertaking to provide full support to the establishment and business development of the Pharmaceutical JV.

As a result of the enhancements to the terms and the increase in total investment and registered capital from RMB40 million to RMB126 million of the Pharmaceutical JV, on 11 April 2002, the Group and the Korning Vendor entered into a Supplemental Agreement. Pursuant to the Supplemental Agreement, certain terms of the Korning Acquisition Agreement and conditions on the completion of the Acquisition were amended. The Group agreed to purchase an 87% equity interest in Korning for the Korning Purchase Consideration of US$12.8 million (equivalent to HK$99.84 million). The remaining 13% interest was sold by the Korning Vendor to another independent third party.

Further details of the original Korning Acquisition Agreement and the Supplemental Agreement were disclosed in the Company's announcements dated 3 January 2002 and 12 April 2002, and in the circulars to shareholders dated 21 January 2002 and 3 May 2002, respectively.

As a consequence of the Korning Acquisition subsequent to the balance sheet date: (i) The Group and the Korning Vendor agreed to set off the Korning Deposit (note 18) against the purchase consideration payable by the Group; and (ii) The Group incurred an additional capital commitment of approximately HK$73 million in relation to the Korning Acquisition and the Group's contracted capital contribution to the Pharmaceutical JV through Star Wisdom.

In the opinion of the directors, the entire Korning Purchase Consideration of HK$99.84 million became part of the cost of the Group's interest in the Pharmaceutical JV. In accounting for the Group's new investment in the pharmaceutical joint venture the entire amount of this payment will be accounted for as goodwill.

33. POST BALANCE SHEET EVENTS (continued)

(a) (continued)

The entire Pharmaceutical JV investment of approximately HK$163 million contributed by the Group, including the Korning Acquisition, is valued at an indicative prospective price earnings ratio of approximately 6.5 times. This price earnings ratio takes into account the amounts paid or to be paid in respect of the Korning Purchase Consideration and the capital contribution to the Pharmaceutical JV, against the target net earnings for the first twelve months after the establishment of the Pharmaceutical JV. The directors of the Company are also of the view that commercially, the Korning Deposit and the Korning Acquisition are in the best interests of the Group and its shareholders.

(b) Pursuant to ordinary resolutions passed on 7 June 2002, the Company approved the adoption of a new share option scheme (the "New Scheme") and the termination of the then existing share options scheme adopted on 30 January 2001. Under the New Scheme, the Directors may, at their discretion, invite any eligible participants to take up options to subscribe for shares in the capital of the Company. The New Scheme is effective for the period from 7 June 2002 to 6 June 2012. The total number of shares which may be allotted and issued upon exercise of all options to be granted under the New Scheme shall not in aggregate exceed 10% of the number of shares in issue as at the date of approval of the New Scheme (the "General Scheme Limit") provided that, inter-alia, the Company may seek approval of the shareholders at a general meeting to refresh the General Scheme Limit. The maximum number of shares in respect of which options may be allotted and issued upon exercise of all outstanding options granted and yet to be exercised under the New Scheme may not, subject to shareholders approval, exceed 30% of the share capital of the Company in issue from time to time.

(c) Pursuant to a placing agreement entered into between the Company and Dao Heng dated 24 May 2002, a total of 50,900,000 ordinary shares of HK$0.50 each were issued and allotted to independent institutional investors for cash at a price of HK$1.40 per placing shares on 18 June 2002. The net proceeds of approximately HK$69.4 million are intended to be used primarily to finance the capital contribution of approximately HK$62.6 million for the Pharmaceutical JV and the balance is intended to be available as general working capital of the Group.

34. COMPARATIVE AMOUNTS

As further explained in note 2 to the financial statements, due to the adoption of certain new and revised SSAPs during the current year, the accounting treatment and presentation of certain items and balances in the financial statements have been revised to comply with the new requirements. Accordingly, certain comparative amounts have been reclassified to conform with the current year's presentation.

35. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 12 August 2002.