

V. MANAGEMENT DISCUSSION AND ANALYSIS

1. ANALYSIS OF THE PRINCIPAL FINANCIAL INDEXES

Indicator Items	<i>(Unit: RMB)</i>		
	Jan-June 2002	Jan-June 2001	Analysis of changes
Revenues from principal activities	585,374,156	611,252,829	A
Profits from principal activities	185,096,265	112,209,911	B
Net profits	37,938,962	-105,669,418	C
Net increase (decrease) in cash and cash equivalents	-213,460,842	15,985,602.48	D

Analysis of changes:

- A: due to a decrease in profits generated by Shenyang Transformers which was disposed of in the currently period.
- B: due to an increase in price of products, new products launched in the market and a decrease in production costs.
- C: due to an increase in profits from principal operations and revenues from transfer of equity interest in Shenyang Transformers.
- D: due to transfer of equity interest in Shenyang Transformers and repayment of loans from cash and bank balance.



(unit:RMB)

Indicator Items	30 June 2002	31 Dec 2001		Analysis of changes
		Before adjustment	After adjustment	
Total assets	1,943,316,553	3,884,189,577	3,869,352,033	A
Shareholders' funds (excluding minority's interest)	504,354,477	333,137,780	318,300,235	B
Net assets per share	0.58	0.38	0.36	
Adjusted net assets per share	0.53	0.34	0.32	

Analysis of changes:

A: due to the disposal of relevant assets from Shenyang Transformers.

B: due to an increase in net profits in the current period and exemption from repayment of part of debts.

2. OPERATIONS OF THE COMPANY

During the reporting period, after the disposal of Shenyang Transformers recognized, revenues from principal activities amounted to RMB585,374,000, up 18.6% compared to the corresponding period over last year. Profits from principal activities amounted to RMB185,096,000, up 65% compared to the corresponding period over last year.

During the reporting period, financial activities and manufacturing activities contributed the core of business to the Company, effectively resolving hurdles on the operation and development of the Company. Currently, operations were orderly run and operational efficiency was significantly improved over last year. As for making a turnaround from recording loss to profits, progress was made on schedule. Following recording loss for the three past consecutive years, policies implemented by the Company to make a turnaround from recording loss to profits were:

1. to effectively control costs, thereby significantly enhancing profitability: firstly, to audit costs more rigorously, determine effective ways to increase profits and lower expense; secondly, to increase the cap on bidding prices and increase the percentage of supplies, purchased through comparison in terms of qualities and prices, over the total supplies, lower costs of various materials and parts purchased; thirdly, subject to the maintenance of functions and quality of products manufactured, to proceed replacement of targeted materials and parts, improve design of products and manufacturing technologies and implement cost-cutting policies, such as lowering consumption of materials; fourthly, since prices of certain products bounced, sales revenues increased, enhancing profitability.
2. to continue to grow at a rapid pace, further consummate the structure of products. During the reporting period, production of sealed sets of electric appliances and capacitors increased 74.4% and 18.8% compared to the corresponding period over last year respectively.
3. to achieve a significant success in developing new products, leading to market development and enhancement of efficiency. During the reporting period, the Company succeeded in manufacturing 18 new products, representing an increase of 12 compared to the corresponding period over last year; to record production value of RMB300.12 million, up 43.6% compared to the corresponding period over last year.

4. to expand market and stimulate sales, resulting in an improvement in the overall trend for receiving orders compared to the corresponding period over last year; During the reporting period, the Company received orders for its principal products for a consideration of RMB900 million, forming a solid basis on which business can grow for the second half of this year and next year.
5. to improve recovery of loans, and recover, settle and solve various lingering non-performing loans; to lay off 2,000 redundant staff members, dispose of loss-making assets and non-operating assets in an effort to further reduce operating expense.

Statistical table for sales of goods by location of customers in the first half of 2002 is as follows:

Geographical segments	<i>(Unit: RMB)</i>	
	Revenue from principal operations	Costs from principal operations
Northeast China	55,177,920	40,062,487
Northern China (including Shandong)	162,393,984	112,648,604
Central China (including the Three Gorges)	87,052,608	49,641,626
Eastern China	82,733,760	58,718,007
Southern China	136,030,464	84,800,294
Southwest of China	31,662,720	26,850,193
North South of China	23,236,992	18,438,228
Export	7,085,708	5,112,471
Total (including tax)	<u>585,374,156</u>	<u>396,271,910</u>

Statistical table for sales of goods by industries in the first half of 2002 is as follows:

(1) Revenue from principal operations

	Six months ended 30.6.2002 (Accumulated) RMB	Six months ended 30.6.2001 (Accumulated) RMB
Ancillary products of transformer	208,075,141.18	292,016,735.00
High voltage switch	236,621,573.00	203,629,125.00
Voltage and current transformer	-	16,875,228.00
Power capacitor	73,457,179.64	62,997,171.00
Close bus bar	45,131,471.00	8,810,017.00
Food, beverage and accomodation	17,229,023.55	21,660,687.00
Others	4,859,767.96	5,263,865.76
	<u>585,374,156.33</u>	<u>611,252,828.76</u>



(2) Costs from principal operations

	Six months ended 30.6.2002 (Accumulated) <i>RMB</i>	Six months ended 30.6.2001 (Accumulated) <i>RMB</i>
Ancillary products of transformer	146,140,563.83	230,808,573.00
High voltage switch	173,716,565.00	183,988,228.00
Voltage and current transformer	–	17,333,474.00
Power capacitor	38,922,479.33	49,244,681.00
Close bus bar	23,556,412.00	6,867,244.00
Food, beverage and accomodation	11,652,939.74	3,724,440.00
Others	2,282,950.17	4,473,380.39
	<u>396,271,910.07</u>	<u>496,440,020.39</u>

(3) Investment in the reporting period

There were no proceeds raised in the reporting period.

In the reporting period, the total of RMB6.584 million of non-raised proceeds was utilized to finance investment, details of which are as follows (RMB'0000):

Item	The total volume of intended investment	Actual investment	Intended investment for the current year	Actual investment for the current year
500kV GIS Project	19,210	14,336.4	4,873.6	658.4

4. OPERATIONAL PLANS IN THE SECOND HALF OF THE YEAR

In the second half of the year and next year, it is estimated that the government polices which expand market demand in the PRC and stimulate continuous and steady growth in the economy, especially infrastructure adjustments, such as the on-going investment for constructing the Three Gorges Project, improvement of electric network, the implementation of the “State western region development strategy”, “Electricity transmission from eastern China to western China” Project, consolidation of electric network and improvement of electric systems, catalyzing demand for electrical transmission and transformation equipment on continuous basis, providing lucrative opportunities for the Company to maintain continuous operations and development.

Major measures for further consolidation of profitability and continuous operational ability in the second half of the year:

1. The Company will step up adjustment of operations and focus on consolidating advanced control and monitoring the relevant procedures. The Company will consolidate internal management and audit, effectively lowering expense.

2. The Company will implement sales and marketing strategies so as to expand market share and effectively utilize all kinds of resources to develop and dominate markets through synergy. First of all, the Company will fully eliminate faulty designs regarding its products, lower and remove the possibility of launching low-quality products in the market; secondly, adjust product mix to provide promptly products and services following any changes in the market; thirdly, place more efforts to develop international markets; fourthly, expand market share and product range, increasing sales revenues.
3. The Company will improve technologies developing system to enhance products developing capability. In the second half of the year, the Company will commence installation and research on high-tech development for the State. The Company will develop the minimized version of GIS and 800KV high voltage switch equipment for the State. The Company will determine and coordinate product development plans for the next three years, implement product development plan for next year as soon as possible, immaculate testing procedures for news products and modify the existing products suited for changes in the market.
4. The Company will determine and implement development strategies for the Company and its subsidiaries, actively carry out joint ventures. In the second half of the year, the Company will implement various ways organizational methods and ept management for joint ventures with breakthrough in progress. The Company will further dispose of assets, which do not generate profits and speed up reorganization of the internal human resources, cut redundant staff members, train and review them in an effort to raise their skills.

Following the improvements of production of the Company and market, it is estimated that net profits in the third quarter will record a significant increase compared to the same time over last year.

5. EXPLANATION ON MATTERS CONTAINED IN THE 2002 AUDITED FINANCIAL REPORT BY THE BOARD OF THE COMPANY

1. Explanation on matters related to qualified opinions

With regard to the disposal of Shenyang Transformers Ltd. (“Shenyang Transformers”) on 4 June 2002, the Board of the Directors was of opinion that the disposal was in principle completed and the selling price of Shenyang Transformers was determined with reference to the values of audited net assets of Shenyang Transformers as at 31 December 2001. Hence, whether profits from operations of Shenyang Transformers between January and May were correctly calculated could only affect determination of profits from operations and transfer of interest of Shenyang Transformers contained in consolidated results, however, posing no impact on the total profits for the first half of the year and operational results of the Company for the future.

Cash from disposal of subsidiaries as set out in consolidated cash flow was arrived at according to provisions of the transfer agreement and calculated after deducting from opening cash balance of Shenyang Transformers. Therefore, changes in the cash position of Shenyang Transformers would not lead to changes in relevant current items as set out in cash flow statement; however, posing no impact on net cash flow in this period and cash balance at the end of the period.



2. With regard to the explanatory notes and relevant matters

Payment of transfer borne for the purchaser and the transfer of interest in Shenyang Transformers to Shenyang National Industrial Assets Management Company (“SNIAMC”) (瀋陽工業國有資產經營公司) were based on the following:

On 24 April, the Company and Northeast Construction & Installation Corporation (東北建築安裝工程總公司) (“Northeast Construction”) entered into an agreement to dispose of Shenyang Transformers. On 27 May 2002, Northeast Construction and SNIAMC signed an Agreement for Transfer of Interest in Shenyang Transformers (關於沈變股權交易的協議書), according to which, Northeast Construction agreed to sell Shenyang Transformers to SNIAMC. In order to enhance efficiency and speed up the process to dispose of Shenyang Transformers, the Company, Northeast Construction and SNIAMC signed Payment Agreement on 27 May 2002, clearing specifying that SNIAMC was required to pay for the acquisition of Northeast Construction to the Company. After payment was made, SNIAMC directly owned interest in Shenyang Transformers. As for this matters, Commerce & Finance Law Office (北京通商律師事務所) provided legal opinions and believed that after the Company received RMB150 million from SNIAMC in accordance with Payment Agreement for Northeast Construction, transfer of interest under Payment Agreement was effectively completed in accordance with the relevant laws.

6. IMPROVEMENT BY THE BOARD OF THE COMPANY WITH REGARD TO MATTERS CONTAINED IN THE 2001 AUDITORS’ REPORT

1. With regard to the syndicated loan: on 29 May 2002, the Company entered into a repayment agreement (“the Agreement”) with the syndicate in Hong Kong, pursuant to which both parties agreed that the Company should make repayment (i.e. US\$ 26million) of 65% of the principal amount (US\$40 million) of the loan by 3 installments. According to the Agreement, the outstanding debt decreased by US\$14 million and the Company was exempt from repaying any outstanding interest thereto. After the Agreement was in force, the Company repaid the first installment of US\$18 million on 30 May 2002. By the end of 29 November 2002, the Company will further repay US\$ 8 million, principally settling the litigation with respect to the loans dominated in US dollar and fully eliminating the risk of H shares being subject to winding-up. In the winding-up hearing of High Court of Hong Kong, the judge approved the application by the syndicate banks to revoke the winding-up petition against the Company on 10 June 2002. (Please refer to announcements published on selected newspapers on 31 May 2002 and 19 June 2002).
2. With regard to the deposit placed with Liaoning Trust and Investment Company (“Liaoning Trust”) (遼寧信託投資公司): in 1998, Liaoning Trust guaranteed the Hong Kong syndicated loan amounting to US\$ 40 million for the Company. As a prior condition in return for such guarantee, US\$ 20 million of US\$ 40 million were placed with Liaoning Trust. In October of 2001, Liaoning Trust was revoked with executive order. The Company utilized various channels to recover such deposit. Liaoning Trust Liquidation Team (遼寧信託投資公司清算組) classified the deposit as foreign debts to deal with and agreed that US\$8 million was first repaid to the Company and the remaining balance of US\$12 million would be handled through negotiation, providing sufficient support to the Company to settle the syndicated loan in accordance with the Agreement.

3. With regard to accounts due from Northeast Electrical Transmission & Transformation Equipment Group Corporation Limited (“NET”) (東北輸變電設備集團公司): as at 31 December 2001, there was an outstanding amount of RMB237 million due from NET for connected transactions. As of 4 June 2001, following the deposal of Shenyang Transformers, the Company has outstanding loan amounting to RMB162 million from NET. In 2001, the Company provided RMB 101.134 million for bad loans. Unprovided other long term assets only amounted to RMB74 million. The Provincial High Court ruled in the Judgement ((2002) Liao Fa Zhi Zi No. 9) dated 25th June 2002 that NET should use 33% equity interest held by it in Shenyang Furukawa Cable Company Limited (“Furukawa Cable”) to set off RMB52,015,000 of the debt owing to the Company. After negotiations, the Company and NET signed an agreement for assignment of equity interest, pursuant to which NET agreed to use the remaining 9.5% equity interest of Furukawa Cable to set off RMB14,900,000 of the debt of the Company on 29 July 2002. In total, NET will use 42.5% equity interest of Furukawa Cable to set off the debt amounting to RMB66.915 million.

The above transaction constitutes a connected transaction which is subject to shareholders in an Extraordinary General Meeting held at the office of the Company on 13 September 2002.

The Company is taking new measures to recover such loans. The Board is confident that any outstanding unprovided loans will be fully recovered by 31 December 2002. The Company will take any action at its disposal to recover loans and protect the interest of the Company and shareholders (Please refer announcements published on 1 August 2002 on selected newspapers).

4. With regard to borrowing from the third parties: As at 31 December 2001, the Company had accounts receivable RMB 92.88 million due from Guangzhou Laureland Group Corporation (廣州羅蘭德集團). As for such loan, the Company provided RMB62.88 million for bad loans in 2001. In 2001, the Company initiated litigation in the court and received civil settlement ((2001) Chen Jing Chu Zi No. 393) from the People’s Intermediate Court of Shenyang City, Liaoning Province on 29 November 2001, according to which, Hong Kong Deao Investment Ltd. (香港德奧投資有限公司), a guarantor of such loan, is willing to satisfy a liability amounting to RMB50 million. The joint task team, comprising of enforcement of the Shenyang Intermediate Court and municipal government, actively supported the Company to retrieve loans. In April of 2002, the authority impounded land use right held by Guangzhou Laureland Property Co., Ltd. (廣州羅蘭德房地產有限公司). Through the mediation by the Shenyang Intermediate Court, the defaulting party agreed to put a charge on all of its equity interest in Hong Kong Deao Investment Ltd. to Northeast Electrical Investment Ltd. (東北電投資有限公司), a proxy of the Company. The defaulting party also agreed to repay RMB46 million of loans within one year to release the charge. However, if the defaulting party failed to repay RMB46 million in accordance with the Agreement, such equity interest in Hong Kong Deao Investment Ltd. and other assets would be deposited of by the Court to settle the loans due to the Company.
5. With regard to reserves against value depreciation of fixed assets and reserves against decline in prices of inventories: according to the principles of provision for impairment confirmed by the Board and valuation report prepared by the valuer, the above impairment was calculated based on sufficient reasons and confirmed by the auditor.



6. With regard to cancellation of accounts payable: the Company reviewed and cancelled out accounts payable and prepayments. In addition, after the disposal of Shenyang Transformers, the relevant accounts posed no impact on the results in the current period. The auditor did not have any disagreement on this issue.
7. With regard to guarantee or contingent liabilities: NET, original controlling shareholder of the Company, and China Everbright Bank signed a borrowing contract with a line of credit amounting to RMB30 million. The Company acted as guarantor and undertook guarantee joint liability. In December of 2001, China Everbright Bank sued NET and the Company for repayment of the principal of the loan (RMB26.40 million) and interest thereto. The Company appointed a lawyer to review the guarantee contract and concluded that such contract was invalid since there was no approval from the Board. The company is in a position to question the validity of the contract and is trying to seek exemption from compliance with guarantee joint liability. However, there is no concrete progress so far.

In April and September of 1999, the Company guaranteed two loans of RMB20 million in total on behalf of Shenyang Cable Company Ltd. (瀋陽電纜有限責任公司) from Bank of China (Shenyang Branch). Bank of China (Shenyang Branch) petitioned a lawsuit in the People's Intermediate Court of Shenyang City which delivered a verdict ((2001) Chen Jing Chu Zi No. 321) dated 2 July 2001 that refuted the lawsuit initiated by Bank of China (Shenyang Branch), the plaintiff, on the grounds that Shenyang Cable Company Ltd., the defendant, announced winding-up in accordance with ((2000) Chen Jing Chu Zi No. 422) dated 29 August 2000. As of 30 June 2002, the Company did not received any affidavit. The Board is of the opinions that the winding-up of Shenyang Cable Company Ltd. is still proceeding. In the short run, the Company is subject to any other guarantee joint liabilities.