YANION INTERNATIONAL HOLDINGS LIMITED

(Incorporated in Bermuda with limited liability)

Interim Report 2003

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CORPORATE INFORMATION

HONORARY CHAIRMAN

Zuo Tai Hang

HONORARY DIRECTOR

Xia Zhi Wu

DIRECTORS

Executive Directors
Butt Wing Han
Cheng Kowk Choi, Godwin
Cheng Shu Wing
Guo Duen How, Tom
Kao Ying Lun
Leung Wah Chai
Wu Fred Fong

Independent non-executive Directors
Choy Tak Ho
Tsui Chun Chung, Arthur

COMPANY SECRETARY

Chiu Lai Chun, Rhoda

PRINCIPAL BANKERS

Bank of China
DBS Bank (Hong Kong) Limited
Fortis Bank Asia HK
The Hongkong and Shanghai Banking Corporation Limited

AUDITORS

Horwath Hong Kong CPA Limited

REGISTRARS

Butterfield Fund Services (Bermuda) Limited
Rosebank Centre
11 Bermudiana Road
Pembroke, Bermuda

REGISTRARS IN HONG KONG

Tengis Limited
Ground floor, BEA Harbour View Centre
56 Gloucester Road
Wanchai, Hong Kong

REGISTERED OFFICE

Canon's Court, 22 Victoria Street
Hamilton, HM12, Bermuda

PRINCIPAL PLACE OF BUSINESS

6th Floor, Wah Lik Industrial Centre
459-469 Castle Peak Road, Tsuen Wan
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The board of directors of Yanion International Holdings Limited (the "Company") is pleased to announce that the unaudited condensed consolidated interim results of the Company and its subsidiaries (the "Group") for the six months ended 30 June 2003 as follows:

CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT

For the six months ended 30 June 2003

		Six months ended 30 June	
		2003	2002
		(Unaudited)	(Unaudited)
	Notes	***HK$'000***	*HK$'000*
TURNOVER	*2*	**84,316**	62,494
Cost of sales		**(69,316)**	(60,203)
Gross profit		**15,000**	2,291
Other revenue		**1,372**	644
Selling and distribution costs		**(7,094)**	(2,454)
Administrative expenses		**(26,580)**	(22,872)
Amortisation of goodwill		**(5,141)**	(3,393)
Provision for impairment in value of fixed assets		**(8,188)**	–
LOSS FROM OPERATING ACTIVITIES		**(30,631)**	(25,784)
Finance costs		**(380)**	(771)
LOSS BEFORE TAX	*3*	**(31,011)**	(26,555)
Taxation	*4*	**(46)**	(29)
LOSS BEFORE MINORITY INTERESTS		**(31,057)**	(26,584)
Minority interests		**(802)**	(61)
NET LOSS FROM ORDINARY ACTIVITIES ATTRIBUTABLE TO SHAREHOLDERS		**(31,859)**	(26,645)
LOSS PER SHARE	*5*		
Basic		**(5.6 cents)**	(5.1 cents)
Diluted		**N/A**	N/A

CONDENSED CONSOLIDATED BALANCE SHEET

As at 30 June 2003

	Notes	As at 30 June 2003 (Unaudited) HK$'000	As at 31 December 2002 (Audited) HK$'000
NON-CURRENT ASSETS			
Fixed assets	7	**42,116**	53,826
Intangible assets	8	**34,730**	22,705
Goodwill	9	**93,398**	98,539
Interests in associates	10	**–**	–
Long term investment		**1,000**	1,000
		171,244	176,070
CURRENT ASSETS			
Inventories		**25,539**	31,406
Accounts receivable	11	**40,342**	32,571
Prepayments and other receivables		**16,403**	19,381
Short term investment		**24,470**	23,415
Pledged deposits		**3,858**	4,636
Cash and cash equivalents		**13,147**	31,658
		123,759	143,067
CURRENT LIABILITIES			
Accounts payable	12	**31,985**	36,811
Other payables and accruals	13	**47,839**	31,897
Due to related companies		**1,416**	1,295
Tax payable		**2,718**	2,672
Interest-bearing bank loans and other borrowings		**8,557**	12,615
Finance lease payables		**171**	332
		92,686	85,622
NET CURRENT ASSETS		**31,073**	57,445
TOTAL ASSETS LESS CURRENT LIABILITIES		**202,317**	233,515
NON-CURRENT LIABILITIES			
Interest-bearing bank loans and other borrowings		**1,991**	2,132
Deferred taxation		**136**	136
		2,127	2,268
MINORITY INTERESTS		**53,039**	52,237
		147,151	179,010
CAPITAL AND RESERVES			
Share capital	14	**5,717**	285,825
Reserves		**141,434**	(106,815)
		147,151	179,010

CONDENSED STATEMENT OF CHANGES IN EQUITY

For the six months ended 30 June 2003

	Share capital HK$'000 (note 14)	Share premium account HK$'000	Contributed surplus HK$'000	Statutory surplus reserve HK$'000	Enterprise development fund HK$'000	Exchange fluctuation reserve HK$'000	Retained profits/ (Accumulated losses) HK$'000	Total HK$'000
At 1 January 2003	285,825	315,215	33,474	957	478	11	(456,950)	179,010
Capital reduction	(280,108)	–	–	–	–	–	280,108	–
Share premium reduction *(note i)*	–	(232,515)	–	–	–	–	232,515	–
Net loss for the period	–	–	–	–	–	–	(31,859)	(31,859)
At 30 June 2003	**5,717**	**82,700**	**33,474**	**957**	**478**	**11**	**23,814**	**147,151**

	Share capital HK$'000	Share premium account HK$'000	Contributed surplus HK$'000	Exchange fluctuation reserve HK$'000	Accumulated losses HK$'000	Total HK$'000
At 1 January 2002						
– as originally stated	260,375	271,195	33,474	198	(132,023)	433,219
– prior year adjustment *(note ii)*	–	–	–	–	(774)	(774)
– as restated	260,375	271,195	33,474	198	(132,797)	432,445
Issue of new shares	25,450	45,810	–	–	–	71,260
Share issue expenses	–	(1,790)	–	–	–	(1,790)
Net loss for the period	–	–	–	–	(26,645)	(26,645)
At 30 June 2002	285,825	315,215	33,474	198	(159,442)	475,270

Notes:

i. Pursuant to the special resolutions passed on the annual general meeting of the Company held on 30 May 2003, the share premium account of the Company would be reduced by an amount of not more than HK$315,215,000. Upon the passing of the special resolutions, the Directors have applied $232,515,000 from the share premium account to set off an equivalent amount of accumulated losses of the Company as at 31 December 2002.

ii. In the year ended 31 December 2002, the Group has adopted for the first time the Hong Kong Statement of Standard Accounting Practice ("SSAP") 34 "Employee benefits". In accordance with SSAP 34, employee entitlement to long service payment payable on cessation of employment are recognized in accordance with certain circumstances under the Hong Kong Employment Ordinance. The accumulated losses at 1 January 2002 have been increased by HK$774,000, which is the cumulative effect of the adoption of the policy on the results for the period prior to 1 January 2002.

CONDENSED CONSOLIDATED CASH FLOW STATEMENT

For the six months ended 30 June 2003

	Six months ended 30 June	
	2003	2002
	(Unaudited)	(Unaudited)
	HK$'000	*HK$'000*
NET CASH OUTFLOW FROM OPERATING ACTIVITIES	**(15,134)**	(15,086)
NET CASH OUTFLOW FROM INVESTING ACTIVITIES	**(3,000)**	(3,799)
NET CASH INFLOW FROM FINANCING ACTIVITIES	**2,152**	77,307
INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	**(15,982)**	58,422
Cash and cash equivalents at beginning of the period	**27,020**	20,504
CASH AND CASH EQUIVALENTS AT END OF THE PERIOD	**11,038**	78,926
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS		
Cash and bank balances	**13,147**	84,719
Bank overdrafts	**(949)**	(793)
Trust receipts and export loans with maturity within three months	**(1,160)**	(5,000)
	11,038	78,926

NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION AND ACCOUNTING POLICIES

The unaudited condensed consolidated interim financial statements have been prepared in accordance with Hong Kong Statement of Standard Accounting Practice ("SSAP") 25, "Interim financial reporting" issued by the Hong Kong Society of Accountants ("HKSA"), and requirements of Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (the "Listing Rules"). The condensed interim financial statements should be read in conjunction with the Company's 2002 annual report.

The accounting policies and methods of computation used in the preparation of the condensed interim financial statements are consistent with those used in the annual financial statements for the year ended 31 December 2002 except that the Group has changed certain of its accounting policies following its adoption of the SSAP 12 (Revised) "Income taxes" issued by the HKSA which is effective for accounting periods commencing on or after 1 January 2003.

SSAP 12 (Revised) principally prescribes the accounting treatment and disclosures for deferred tax. In prior years, deferred tax is provided using the income statement 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 recognized until its realization is assured beyond reasonable doubt. SSAP 12 (Revised) requires the adoption of the balance sheet liability method, whereby deferred tax is recognised in respect of all temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, with limited exceptions. In the opinion of the Directors, the adoption of the revised SSAP did not have a material impact on the results of the Group for the current and prior accounting periods, accordingly, no prior period adjustment has been required.

2. SEGMENT INFORMATION

(a) Business segments

The following table presents revenue and results for the Group's business segments for the six months ended:

	Manufacture and trading of CD/VCD players and mechanisms, amplifiers, mini-audio products		Manufacture and trading of car audio mechanisms, cassette deck mechanisms, personal office appliance and related products		Trading of Internet phone sets and provision of related services		Manufacture, trading and contracting of Chinese medicine products		Consolidated	
	2003	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**	2002
	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	**52,950**	39,093	**14,582**	23,401	**–**	–	**16,784**	–	**84,316**	62,494
Segment results	**(17,077)**	(10,972)	**(2,578)**	(4,670)	**(27)**	(3,457)	**(4,183)**	–	**(23,865)**	(19,099)
Interest income									**96**	217
Unallocated expenses									**(6,862)**	(6,902)
Loss from operating activities									**(30,631)**	(25,784)
Finance costs									**(380)**	(771)
Loss before tax									**(31,011)**	(26,555)
Taxation									**(46)**	(29)
Loss before minority interests									**(31,057)**	(26,584)
Minority interests									**(802)**	(61)
Net loss from ordinary activities attributable to shareholders									**(31,859)**	(26,645)

(b) Geographical segments

The following table presents revenue and results for the Group's geographical segments for the six months ended:

	Hong Kong		PRC		Other Asian countries		Europe		America		Consolidated	
	2003	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**	2002	**2003**	2002
	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	**7,580**	9,956	**20,570**	6,766	**1,413**	4,791	**22,604**	26,184	**32,149**	14,797	**84,316**	62,494
Segment results	**(1,353)**	(2,042)	**(4,905)**	(4,843)	**(378)**	(1,205)	**(7,228)**	(7,332)	**(10,001)**	(3,677)	**(23,865)**	(19,099)

3. LOSS BEFORE TAX

Loss before tax is arrived at after charging/(crediting) the followings:

	Six months ended 30 June	
	2003	2002
	HK$'000	*HK$'000*
Other revenue:		
Interest income	**(96)**	(217)
Investment income	**(1,055)**	–
Other income	**(221)**	(427)
	(1,372)	(644)
Finance costs:		
Interest on bank loans, overdrafts and other borrowings wholly repayable within five years	**363**	735
Interest on finance leases	**17**	36
	380	771
Cost of inventories sold	**66,441**	60,203
Amortisation of deferred development costs	**–**	583
Amortisation of Chinese medicine intellectual property and knowhow	**1,994**	–
Provision against inventories	**2,876**	–
Loss on disposal of fixed assets	**1,275**	–
Staff costs (excluding directors' remuneration)	**12,946**	12,880
Depreciation	**6,121**	9,237

4. TAXATION

Hong Kong profits tax has been provided at the rate of 17.5% (Six months ended 30 June 2002: 16%) on the estimated assessable profits arising in Hong Kong during the period. 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.

	Six months ended 30 June	
	2003	2002
	HK$'000	*HK$'000*
Hong Kong profits tax	**46**	29

5. LOSS PER SHARE

The calculation of basic loss per share is based on the net loss from ordinary activities attributable to shareholders for the period of HK$31,859,000 (Six months ended 30 June 2002: HK$26,645,000) and the weighted average of 571,650,673 (30 June 2002: 524,386,387) ordinary shares in issue during the period.

Diluted loss per share for the six months ended 30 June 2002 and 30 June 2003 have not been shown as the share options outstanding during both periods had an anti-dilutive effect on the basic loss per share for both periods.

6. DIVIDENDS

The directors of the Company do not recommend the payment of any interim dividend for the six months ended 30 June 2003 (Six months ended 30 June 2002: Nil).

7. FIXED ASSETS

	30 June 2003	31 December 2002
	HK$'000	*HK$'000*
Net book value at beginning of period/year	**53,826**	63,012
Additions	**3,874**	4,858
Arising from acquisition of subsidiaries	**–**	9,732
Disposals	**(1,275)**	(32)
Depreciation	**(6,121)**	(17,168)
Provision for impairment in value	**(8,188)**	(6,576)
Net book value at end of period/year	**42,116**	53,826

8. INTANGIBLE ASSETS

	30 June 2003	31 December 2002
	HK$'000	*HK$'000*
Balance at beginning of period/year	**22,705**	1,085
Arising from acquisition of subsidiaries	**–**	23,532
Additions of Chinese medicine intellectual property and knowhow	**14,019**	–
Amortisation for the period/year	**(1,994)**	(1,912)
Balance at end of period/year	**34,730**	22,705

9. GOODWILL

	30 June 2003	31 December 2002
	HK$'000	*HK$'000*
Balance at beginning of period/year	**98,539**	7,232
Arising from acquisition of subsidiaries	**–**	116,393
Amortisation for the period/year	**(5,141)**	(11,071)
Provision for impairment in value	**–**	(14,015)
Balance at end of period/year	**93,398**	98,539

10. INTERESTS IN ASSOCIATES

As explained in the annual report 2002 of the Company, the directors of Global Cyber Limited ("Global Cyber") and the Company have sought advice from PRC legal counsel as to the appropriate course of action, including arbitration and/or the legal action that should be taken. At the date of approval of these financial statements, the directors of the Company are not in a position to quantify the outcome and effect of the dispute. In the opinion of the directors of the Company, there had been an impairment loss on the carrying value of the investment in Global Cyber and for conservative reason, full provision had been made against the investment cost of HK$250 million on 31 December 2002.

11. ACCOUNTS RECEIVABLE

The Group maintains a defined credit policy and allows credit periods ranged from 15 to 90 days to its trade customers. Under exceptional cases, the Group may extend credits to specific customer for periods beyond 90 days upon special approval. The Group seeks to maintain strict control over its outstanding receivables. Overdue balances are reviewed and monitored by senior management.

An aged analysis of accounts receivable based on payment due date and net of provisions is as follows:

	30 June 2003	31 December 2002
	HK$'000	*HK$'000*
Within 1 month	**10,459**	21,820
2 to 3 months	**2,874**	6,665
4 to 6 months	**6,679**	1,327
7 to 12 months	**18,392**	643
Over 1 year	**1,938**	2,116
	40,342	32,571

12. ACCOUNTS PAYABLE

An aged analysis of accounts payable based on payment due date is as follows:

	30 June 2003	31 December 2002
	HK$'000	*HK$'000*
Within 1 month	**9,627**	10,521
2 to 3 months	**12,898**	17,826
4 to 6 months	**4,957**	6,071
7 to 12 months	**1,691**	136
Over 1 year	**2,812**	2,257
	31,985	36,811

13. OTHER PAYABLES AND ACCRUALS

Other payables and accruals included the amount due to a director of HK$9,990,000 (31 December 2002: HK$5,990,000) which is unsecured, interest-free and has no fixed terms of repayment.

14. SHARE CAPITAL

	30 June 2003	31 December 2002
	HK$'000	*HK$'000*
Authorised:		
50,000,000,000 ordinary shares of HK$0.01 each (2002: 1,000,000,000 ordinary shares of HK$0.50 each)	**500,000**	500,000
Issued and fully paid:		
571,650,673 ordinary shares of HK$0.01 each (2002: 571,650,673 ordinary shares of HK$0.50 each)	**5,717**	285,825

Pursuant to the special resolutions passed on the annual general meeting of the Company held on 30 May 2003, the nominal value of all the shares of HK$0.50 each in the capital of the Company in issue has been reduced from HK$0.50 each to HK$0.01 each by cancelling HK$0.49 paid up on each of such shares in issue so that the issued share capital of HK$285,825,000 is reduced to HK$5,717,000 and the capital reduction of HK$280,108,000 has been applied to set off against the accumulated losses. The authorised share capital of the Company remains at HK$500,000,000 and each of the unissued shares of HK$0.50 in the capital of the Company be subdivided into 50 unissued shares of HK$0.01 each, and the issued and unissued share capital of the Company is comprise 50,000,000,000 new shares of HK$0.01 each.

15. RELATED PARTY TRANSACTIONS

Set out below are the related party transactions disclosed in accordance with SSAP 20 issued by the HKSA.

	Six months ended 30 June	
	2003	2002
	HK$'000	*HK$'000*
Purchases of raw materials from a related company	**272**	426
Rental expenses paid/payable to related companies	**2,765**	1,983
Rental expenses paid/payable to a director	**360**	360
Consultancy fees paid/payable to a related company	**450**	450

16. CONNECTED TRANSACTIONS

In addition to the related party transactions disclosed in note 15 which also constituted connected transactions under the Listing Rules, the following transactions constituted connected transactions under the Listing Rules.

	Six months ended 30 June	
	2003	2002
	HK$'000	*HK$'000*
Accrual of balance of purchase consideration relating to intellectual and operating rights of twelve Chinese medicines from a minority interest	**9,346**	–
Purchase of raw materials/herbs from a minority interest	**2,780**	–
Sales of medicinal products to China National Group Corp. of Traditional and Herbal Medicine	**1,608**	–

17. CONTINGENT LIABILITIES

		31 December
	30 June 2003	2002
	HK$'000	*HK$'000*
Bills discounted with recourse	**6,837**	3,685

18. OPERATING LEASE ARRANGEMENTS

	Six months ended 30 June	
	2003	2002
	HK$'000	*HK$'000*
Minimum lease payments paid under operating leases	**6,572**	4,849
Less: Amount capitalised	**(199)**	(156)
	6,373	4,693

		31 December
	30 June 2003	2002
	HK$'000	*HK$'000*
Total future minimum lease payments under non-cancellable operating leases in respect of its land and buildings falling due:		
Within one year	**7,583**	11,805
In the second to fifth years, inclusive	**6,223**	10,847
	13,806	22,652

19. CAPITAL COMMITMENTS

		31 December
	30 June 2003	2002
	HK$'000	*HK$'000*
Contracted, but not provided for:		
Acquisition of a subsidiary	**43,028**	43,028
Acquisition of Chinese medicine intellectual property and knowhow	**–**	9,346
Acquisition of associated companies	**68,000**	–

20. POST BALANCE SHEET EVENTS

(a) In July 2003, the Company has been granted short term credit facilities to the extent of HK$50,000,000 from an independent financial institution to finance general working capital and to partially finance the capital contributions to Huayi Pharmaceutical Company Limited ("Huayi") by the Group.

(b) As of 26 July 2003, the Group has fulfilled all its capital contribution commitment to Huayi of approximately HK$63 million. The Group has also made additional contributions of Rmb8,328,000 (equivalent to HK$7,852,000) which pertained to capital contribution defaulted by the minority shareholder of Korning Investments Limited ("Korning"). Pursuant to the shareholders' agreement of Korning, the Group is entitled to subscribe for additional shares in Korning with the additional contributions as the consideration for such subscription. The Group is currently under negotiation with the defaulted minority shareholder for other acceptable alternatives.

(c) During the period, for the purpose of developing the Chinese medicine business, Huayi has committed to acquire from an independent third party 40% interest in two Chinese private companies and the right of exploitation of wild herbs (the "Investment") at a total consideration of approximately HK$68,000,000. The purpose of the Investment is to develop a Chinese medicinal center and wild herbs harvesting area. Partial payment for the consideration of approximately HK$49,000,000 was made in July 2003.

(d) The short term investment in participating redeemable preference shares in a fund of HK$23,415,000 has been redeemed on 8 August 2003 and earned a total investment income of HK$1,115,000 (yielded about 4.8%). The proceeds were used to partially repaid the short term loan as disclosed in note (a) above.

(e) The long term investment has been disposed of at the consideration equivalent to its carrying value of HK$1,000,000 in August 2003.

21. APPROVAL OF THE INTERIM FINANCIAL STATEMENTS

The condensed interim financial statements were approved by the board of directors on 24 September 2003.

MANAGEMENT DISCUSSION AND ANALYSIS

Business Review

Turnover of the Group for the six months period ended 30 June 2003 was HK$84,316,000 (HK$62,494,000 for the corresponding period last year) and the loss attributable to shareholders for the period was HK$31,859,000 (HK$26,645,000 for the corresponding period last year).

The Group's turnover for the first six months of 2003 represents an increase of 35%, which was mainly due to contribution from the Chinese traditional and herbal medicine business. Nevertheless, the 2003 first half year results were hampered by the effects of the Iraqi war and the outbreak of severe acute respiratory syndrome (SARS).

Pharmaceutical Business

Sales of Chinese medicine for the first half year was HK$16,784,000, representing 20% of the Group's turnover (2002: Nil). As a strategic move, the Group in the second half of last year formed a sino-foreign joint venture, Huayi Pharmaceutical Company Limited ("Huayi") with a subsidiary of China National Group Corporation of Traditional and Herbal Medicine ("China National Medicine"). This enables the Group to transform its main business focus to the enormous Chinese medicine market. Since the establishment of Huayi joint venture, the Chinese medicine business has quickly developed into a substantial core business of the Group.

Business development had been satisfactory since Huayi's early establishment. For the first five months upto 2002 year end, earnings before amortization of goodwill, intangible assets and depreciation was HK$13,948,000. After amortization and depreciation, the Chinese medicine business contributed a net profit of HK$8,128,000 to the Group then. Due to the outbreak of SARS in Asia, and China being one of the most affected countries, sale and promotion had been hampered during the first half of the current year in various provinces and cities. Except for a couple of Huayi's medicines for treatment of fever, headaches, sore throats and influenza symptoms which, in the wake of SARS, received a stronger demand, the remainders being prescription drugs experienced sluggish sales during the first half of 2003. This was because Huayi's activities of sales teams during that period were prohibited, like most people, from entering the hospitals without special permission. As a result, Huayi's sales fell far short of its original targets. The launch of other new medicines originally planned also had to be delayed. Therefore, the SARS fiasco had a temporary negative effect on Huayi's business development plan throughout China during this period. Earnings before amortization of goodwill, intangible assets and depreciation for the first six months of 2003 was HK$3,900,000. After deducting amortization and depreciation, a net loss of HK$4,183,000 was recorded from the Chinese medicine business during the period. In spite of this temporary deterant, Huayi will use its best effort to achieve its plans.

In the first half of 2003, Huayi was notified by the relevant government authority that under the new Beijing city development plan, Huayi's factory located at Zhong Guan Cun, Haidian District (中關村海淀區) has to be relocated to make way for new infrastructure and main roads to be built under the plan. The Government will appoint the District Land Bureau (區土地局) to evaluate and make compensations to affected business enterprises. Due to this indeterminant, Huayi had to temporarily shelf its plan of upgrading its production facilities which were intended to increase its production capability for a wider range of pharmaceutical products. In order to obtain the best compensation, Huayi has commenced liaising with relevant bodies and data gathering. However up-to-date a number of compensation criteria remain unclear and there is no definite time schedule on the part of Huayi for relocation. Huayi is keeping close liaison with the relevant authority, with the view of achieving the best relocation scheme so as to amalgamate with the company's long term development.

Completion of Huayi Capital Contribution Obligation

In 2002, the Group acquired an 87% stake in Korning Investments Limited ("Korning") and through Star Wisdom Investments Limited ("Star Wisdom") indirectly holds a 60% interest in the sino-foreign joint venture-Huayi. Huayi's registered capital is RMB126,000,000 of which 60% represents Star Wisdom's contribution, equivalent to RMB75,600,000. The Group paid in such sum prior to 26 July 2003, ascertaining our strategic partnership with China's pharmaceutical leader, China National Medicine. This will undoubtedly assist our developing the enormous Chinese pharmaceutical and healthcare products market.

Subscription of Further Interests in Korning

On 5 August 2003 the Company announced paying an additional RMB8,328,000 (equivalent to HK$7,852,000) advance to its non-wholly-owned subsidiary, Korning, on 24 July 2003 for fulfilling its capital contribution obligation to Huayi. The said amount represented the unfulfilled commitment of Korning's 13% independent minority shareholder ("Investor"). The additional amount was paid in order to avoid non-compliance of the joint venture Agreement by Star Wisdom which would have an adverse impact on the interests of the Group. In accordance with the 1 August 2002 shareholders' agreement between the Group, the Investor and Korning, should the Investor determine not to make additional capital contribution, the Group is entitled to, according to the agreement, exercise the subscription right to subscribe additional Korning shares. The subscription price still has to be determined by independent accountants. Other acceptable alternatives are being discussed and, depending on the actual circumstances, will be announced later.

Electronics Manufacturing Business

Sale of the existing high-end audio/visual products, including CD/VCD players and mechanisms, amplifiers and other high-end mini-audio products amounted to HK$52,950,000, representing 63% of total turnover (2002: HK$39,093,000 and 63% respectively). This is followed by sale of non-audio products and knock-down components including cassette deck mechanisms, car audio mechanisms, high precision springs and different types of metal and plastic parts amounted to HK$14,582,000, representing 17% of total turnover (2002: HK$23,401,000 and 37% respectively).

Geographically, the Group's sales in the first half of 2003 to the America, Europe, China, Hong Kong and other Asian countries were respectively 38%, 27%, 24%, 9% and 2% of the total turnover (2002: 24%, 42%, 11%, 16% and 7% respectively).

In terms of electronics manufacturing business, the Group continues to actively solicit orders from reputable brand names for Original Design Manufacture (ODM) and Original Equipment Manufacture (OEM). Nevertheless, due to cut throat competition and a weak consumer confidence, the electronics business still has not been able to return to profitability. It was contemplated that the traditional manufacturing business be retained for purpose of complementing the Group's investment in the VOD project and the set-top box manufacture. Unfortunately the VOD project did not materialize as originally planned. The Board in the first half year had been reviewing whether maintaining this business would be for the Group's long term interest. Other alternatives were also weighted including the teaming up with strategic partners and the disposal of the traditional manufacturing business to interested parties based on acceptable considerations.

Other Businesses

The Group, in its planned business transformation, invested respectively in 2000 and 2001 in an VOD cable television station re-engineering project and an Internet phone project. As a result of the Group's long term focusing in Chinese pharmaceuticals and the changes in project investment environments, the management in 2002 year end adopted a conservative policy in making full provision for these two business areas as stated below:

a) Internet phone

This mainly involves the distribution of Internet phones and stored-value calling cards in major cities in China. Due to a drastic change in mobile and fixed line long distance telephone and the Internet phone market, calling charges experienced substantial decline and competition becomes keener than ever. The management continues to watch the market closely and re-evaluate the long distance telephone business prospects in China. In order to adopt a conservative accounting policy, the Group made full provision for this investment last year. In view of future uncertainties, the management will not make further investment for purpose of enhancing competitive edge. However, the possibility of disposing off this investment when the right opportunity arises should not be ruled out.

b) *Video-on-demand System*

Video-on-demand ("VOD") system is an investment in the re-engineering of cable television stations in the PRC. As of to-date, the Group has a 27% shareholding in its associated company, Global Cyber Limited, which only asset being an 80% equity interest in Shanghai Dazheng, a sino-foreign joint venture. The PRC party is a Shanghai company with many years' experience in research, development and implementation of digital VOD system in PRC, involving the provision of relevant softwares, servers and set-top boxes for the reconfiguration of cable television stations in China. However, such products have not, up-till now, received the recognition and confirmation from the relevant authority as the standard for the country's cabled television stations. In addition, the joint venture partners are in dispute in respect of ownership of the underlying intellectual property rights of the VOD softwares resulting in the project coming to a standstill. The Group in 2002 year end made a full provision on the total investments in this project.

Liquidity and Financial Resources

As at 30 June 2003, the Group's current assets amounted to HK$123,759,000 representing a decrease of approximately HK$19,308,000 as compared to the end of last year. Amongst them, accounts receivable increased by HK$7,771,000 to HK$40,342,000; cash and cash equivalents decreased HK$18,511,000 to HK$13,147,000; pledged deposits decreased HK$778,000 to HK$3,858,000; inventories decreased HK$5,867,000 to HK$25,539,000; prepayments and other receivables decreased HK$2,978,000 to HK$16,403,000. Short term investment increased HK$1,055,000 to HK$24,470,000.

Current liabilities amounted to HK$92,686,000 representing an increase of HK$7,064,000 compared to the end of last year. Amongst them, accounts payable decreased HK$4,826,000 to HK$31,985,000; other payables and accruals increased HK$15,942,000 to HK$47,839,000; interest-bearing bank loans and other borrowings dropped HK$4,058,000 to HK$8,557,000. Most liabilities were short term in nature and the settlement currencies of which were mainly in Hong Kong dollars. Bank loans were to be calculated based on Hong Kong prime rate. As at 30 June 2003, the current ratio (the ratio of current assets to current liabilities) was 1.34.

As for non-current assets, the amount was HK$171,244,000, representing a decrease of HK$4,826,000 as compared to the end of last year. Amongst them, goodwill decreased HK$5,141,000 to HK$93,398,000; fixed assets reduced HK$11,710,000 to HK$42,116,000; intangible assets increased HK$12,025,000 to HK$34,730,000. The Group's total liabilities were HK$94,813,000. The overall gearing ratio (the ratio of total liabilities to shareholders' equity) was approximately 64%.

Besides, in relation to contingent liabilities as at 30 June 2003, bill discounted with recourse was HK$6,837,000, increased by HK$3,152,000 from the end of last year. The Company has given the guarantees to three banks for a total sum of HK$34,000,000 in connection with facilities granted to subsidiaries, of which only one bank guarantee for the sum of HK$7,144,000 was utilized as at 30 June 2003.

As an overview, the Group's negative results caused a weakened cash flow. On the other hand, the capital market is highly liquid and investment funds have shown significant interest in the Chinese pharmaceutical business. The Board feels that the Group will, when the opportunity arises, raise additional equity in the capital market, therefore enabling more investments to direct towards the China investment projects.

Capital Structure

As of 30 June 2003, the Group's issued shares numbered 571,650,673 and the shareholders' equity amounted to approximately HK$147,151,000.

Capital Reorganization

The shareholders on the 30 May 2003 annual general meeting approved the capital reorganization to reduce the nominal value of the shares in issue from HK$0.50 each to HK$0.01 each. After the implementation of the capital reduction, the authorized share capital of the Company is HK$500,000,000 divided into 50,000,000,000 new shares of HK$0.01 each. Upon completion of the capital reduction, the issued share capital of HK$285,825,000 was reduced to HK$5,717,000 and the credit of HK$280,108,000 arising therefrom has been applied to set off against an equivalent amount in the accumulated losses. Upon the passing of a special resolution, share premium of HK$232,515,000 was reduced by applying the credit to set off against the accumulated losses.

The implementation of this capital reorganization will facilitate the Company any capital fund-raising exercise when appropriate in future and also enable the Company to make distribution for payment of dividends from retained earnings account of the Company for the best interest of the Company and the shareholders as a whole.

Pledged Assets

As of 30 June 2003, the Group has pledged assets with total book value of HK$10,338,000 (31 December 2002: HK$11,708,000), including the industrial property located in Hong Kong with carrying amount of HK$6,480,000 (31 December 2002: HK$7,072,000) and bank deposits of approximately HK$3,858,000 (31 December 2002: HK$4,636,000) to banks to secure general banking facilities.

Prospects

After the SARS outbreak that shocked the world was tamed by the middle of the year, Huayi has been able to regather its pace in planning its market development and new pharmaceutical medicine distribution with the view of enhancing future profitability. The Board believes that due to the Group's unique position of having established a firm cooperative foundation with China National Medicine and maintaining close liaison therewith, this enhances the Group's competitive edge and development capability in the pharmaceutical and health care products market, enabling the Group to achieve stable and long term profit growth in the future.

In June 2003, two leading pharmaceutical enterprises China National Pharmaceutical Group Corporation ("China National Pharmaceutical") – (中國醫葯集團總公司) and China National Medicine merged under the approval of the Large Enterprise Supervisory Committee of the State Council (國務院國有資產管理委員會). Through this exercise, China National Medicine became a division of China National Pharmaceutical. China National Pharmaceutical is the largest state-run pharmaceutical manufacturer, distributor and import/export in China primarily involving western medicines and medical equipment with annual sales turnover exceeding RMB10 billion, and China National Medicine is primarily engaged in the manufacture and distribution of Chinese traditional and herbal medicine. Both enterprises were under the direct supervision of the Central Government prior to the merger. The merger and reorganization will enable the two groups to maintain their leading positions in the international market. We believe that China National Medicine's continued efforts in modernizing its Chinese pharmaceutical products and China National Pharmaceutical's provision of an extensive international distribution network will greatly enhance China National Medicine's export potentials. The merger will no doubt provide the Group with many business opportunities and development possibilities in the long run. The continued Chinese economic expansion has created many high return business investment opportunities. In this regard, the Group will consider, at suitable times, to raise additional capital to strengthen its capital base and increase its working capital for future business development. We believe that based on investors' interest in daunting industries like pharmaceuticals and health care products and anticipated profit possibilities, it will generate the best return for the shareholders.

Employees

As at 30 June 2003, there were approximately 1,500 management, administrative, production and selling staff located in Hong Kong and the PRC. The Company has adopted an employee share option scheme and housing benefits were provided for certain Hong Kong and PRC employees. Salaries of employees were determined taking into account job performance and professional experience of the employees concerned and the general practice within the industry. Since December 2000, all employees and directors in Hong Kong Special Administrative Region have joined the mandatory provident fund scheme implemented by the Hong Kong Special Administrative Region.

AUDIT COMMITTEE

The audit committee of the Company is comprised of two independent non-executive directors, Messrs. Choy Tak Ho and Tsui Chun Chung, Arthur. The audit committee, together with the management has examined the accounting policies and practice adopted by the Group and discussed and reviewed the financial statements of the unaudited consolidated interim results announced by the Group for the six months ended 30 June 2003.

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS IN THE SECURITIES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS

(a) Shares Capital

	Number of ordinary shares in the Company	
Name of director	**Personal interest**	**Corporate interest***
Butt Wing Han	8,915,250	2,983,500
Cheng Shu Wing	100,000	–
Guo Duen How, Tom	2,800,000	–
Kao Ying Lun	5,000,000	–
Leung Wah Chai	33,915,600	9,783,500
Wu Fred Fong	5,000,000	–

* *Kamga Investment Limited held 2,983,500 shares in the Company. Leung Wah Chai and Butt Wing Han are controlling shareholders and directors of Kamga Investment Limited. Bestbond Company Limited held 6,800,000 shares in the Company. Leung Wah Chai is a controlling shareholder and a director of Bestbond Company Limited.*

(b) Share Option Scheme

Pursuant to ordinary resolutions passed on 7 June 2002, the Company approved the adoption of a new share option scheme (the "New Scheme"). 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 following share options were outstanding under the New Scheme during the period from 1 January 2003 to 30 June 2003.

	Number of outstanding share options from 1 January 2003 to 30 June 2003
Name of director:	
Butt Wing Han	5,000,000
Cheng Kwok Choi, Godwin	500,000
Cheng Shu Wing	600,000
Choy Tak Ho	570,000
Guo Duen How, Tom	1,150,000
Kao Ying Lun	5,000,000
Leung Wah Chai	5,000,000
Tsui Chun Chung, Arthur	570,000
Wu Fred Fong	5,000,000
Directors and executives of Huayi, and eligible employees	21,000,000
	44,390,000

Save as disclosed above, as at 30 June 2003, none of the directors or the chief executive of the Company and their associates had any interests or short positions in the shares, underlying shares and debentures of the Company or any of its associated corporation (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")), as recorded in the register required to be kept under section 352 of the SFO; or notified to the Company and the Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to the Model Code for Securities Transactions by Directors of the Listed Companies.

DIRECTORS' RIGHTS TO ACQUIRE SHARES

Save as disclosed above, at no time during the period was the Company or any of its subsidiaries a party to any arrangement to enable the directors of the Company, their respective spouses, or children under 18 years of age to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate.

SUBSTANTIAL SHAREHOLDERS

As at 30 June 2003, save as disclosed below and other than the directors and chief executive of the Company and the companies controlled by them whose interests are disclosed above, the Company did not aware of any shareholder, had any interests or short positions in the shares and underlying shares as recorded in the register required to be kept by the Company under section 336 of the SFO.

Long position in the shares of the Company

Name of shareholder	Number of issued shares held	% of the issued share capital
Grimwood Enterprises Limited	47,450,000	8.3%

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

There was no purchase, sale or redemption by the Company or any of its subsidiaries of the Company's listed securities during the six months ended 30 June 2003.

CODE OF BEST PRACTICE

None of the directors of the Company is aware of information that would reasonably indicate that the Company is not, or was not for any part of the period for the six months ended 30 June 2003, in compliance with the Code of Best Practice as set out in Appendix 14 of the Listing Rules. The Independent non-executive directors of the Company are subject to retirement by rotation and re-election at the Company's annual general meeting in accordance with the Bye-Laws of the Company.

On behalf of the Board
Cheng Kwok Choi, Godwin
Executive Director

Hong Kong,
24 September 2003