

Directors' Report

The directors have pleasure in presenting their annual report and the audited financial statements of the Company and its subsidiaries (hereinafter collectively referred to as the "Group") for the year ended 31 December, 2003.

PRINCIPAL ACTIVITIES

The Company is an investment holding company and provides corporate management services. The principal activities of the Company's subsidiaries are set out in note 34 to the financial statements.

SEGMENTAL INFORMATION

Details of segmental information are set out in note 5 to the financial statements.

MAJOR CUSTOMERS AND SUPPLIERS

The five largest suppliers in aggregate accounted for less than 30% of the Group's total purchases for the year.

The five largest customers in aggregate accounted for 32% of the Group's turnover and the largest customer accounted for 8% of the Group's turnover for the year.

None of the directors, their associates or shareholders, who to the knowledge of the directors own more than 5% of the Company's share capital, had any interest in any of the five largest customers.

RESULTS AND APPROPRIATIONS

The results of the Group for the year are set out in the consolidated income statement on page 20.

The directors now recommend the payment of a final dividend of HK\$0.0035 per share to the shareholders on the register of members on 6 May, 2004, amounting to HK\$13,788,000 and the retention of the remaining profit for the year of HK\$15,114,000.

PROPERTY, PLANT AND EQUIPMENT

During the year, the Group acquired property, plant and equipment of HK\$2,675,000 for the expansion of production capacity. Movements during the year in the property, plant and equipment of the Group are set out in note 14 to the financial statements.

MAJOR PROPERTIES

Particulars of the Group's major properties at 31 December, 2003 are set out on page 54.

SUBSIDIARIES

Particulars of the Company's subsidiaries are set out in note 34 to the financial statements.

SHARE CAPITAL

Details of movements during the year in the Company's share capital are set out in note 24 to the financial statements.

SHARE OPTIONS

The Company has adopted a share option scheme (the "Scheme"), which was approved at a special general meeting of the Company held on 9 April, 1999, for the primary purpose of providing incentives to its employees. Pursuant to the Scheme, the board of directors of the Company may, at its discretion, grant options to eligible employees, including executive directors, of the Company or any of its subsidiaries to subscribe for shares in the Company at a price not less than 80% of the average of the closing prices of the shares on The Stock Exchange of Hong Kong Limited (the "Stock Exchange") on the five trading days immediately preceding the date of grant of the options or the nominal value of the shares, whichever is the higher. The share options are exercisable at any time for a period to be determined by its directors, which shall not be more than ten years from the adoption of the Scheme up to 8 April, 2009. Options granted must be taken up within 28 days from the date of grant, upon payment of HK\$1. Unless otherwise terminated or altered, the Scheme will remain in force for a period of ten years from the date of adoption.

The maximum number of shares in respect of which options may be granted under the Scheme together with shares previously issued pursuant to options exercised under the Scheme shall not exceed 10% of the issued share capital of the Company from time to time and the maximum number of shares in respect of which options may be granted to any one employee shall not exceed 25% of the maximum number of shares in respect of which options may be granted under the Scheme.

In accordance with The Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules"), certain terms of the Scheme need to be amended, or alternatively, a new share option scheme needs to be implemented, in order to comply with the requirements of the Listing Rules. According to the Listing Rules as amended, no more share is available for issue under the Scheme.

No options were granted by the Company during the year and no options were outstanding at 31 December, 2003.

RESERVES

Details of movements during the year in the reserves of the Group and the Company are set out in the consolidated statement of changes in equity on page 23 and note 27 to the financial statements, respectively.

DIRECTORS AND DIRECTORS' SERVICE CONTRACTS

The directors of the Company for the year and up to the date of this report were:

Executive directors:

Dr. Lam How Mun Peter

Chairman and Managing Director

Mr. Cheung Chung Kiu

Mr. Lam Hiu Lo

Mr. Leung Chun Cheong

Mr. Leung Wai Fai

Ms. Poon Ho Yee Agnes

Independent non-executive directors:

Mr. Lam Kin Fung Jeffrey

Mr. Lam Ping Cheung

In accordance with Clause 87 of the Company's Bye-laws, Ms. Poon Ho Yee Agnes retires by rotation and, being eligible, offers herself for re-election at the forthcoming annual general meeting of the Company.

Messrs. Lam Kin Fung Jeffrey and Lam Ping Cheung being re-elected as independent non-executive directors on 26 May, 2003, hold such office until the conclusion of the forthcoming annual general meeting and, being eligible, offer themselves for re-election at the forthcoming annual general meeting of the Company.

All other remaining directors continue in office.

None of the directors being proposed for re-election at the forthcoming annual general meeting has a service contract with the Company or any of its subsidiaries which is not determinable by the Group within one year without payment of compensation, other than statutory compensation.

DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS IN SHARES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS

As at 31 December, 2003, the interests and short positions of the directors and chief executives of the Company and their associates in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) as recorded in the register required to be kept by the Company pursuant to section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies of the Listing Rules, were as follows:

(a) Interests in shares of the Company (long positions)

| Name of director | Nature of interest | Number of shares held | Percentage of issued share capital |
|-------------------------|----------------------------|------------------------------|---|
| Dr. Lam How Mun Peter | Personal | 110,000 | 0.00% |
| Mr. Cheung Chung Kiu | Corporate (notes 1 & 3) | 2,752,396,360 | 69.87% |
| Mr. Leung Chun Cheong | Personal | 7,410,000 | 0.19% |
| Ms. Poon Ho Yee Agnes | Personal | 1,040,000 | 0.03% |

(b) Interests in shares of Yugang International Limited ("Yugang"), the Company's ultimate holding company (long positions)

| Name of director | Nature of interest | Number of shares held | Percentage of issued share capital |
|-------------------------|----------------------------|------------------------------|---|
| Mr. Cheung Chung Kiu | Corporate (notes 2 & 3) | 3,194,434,684 | 37.79% |
| | Personal | 53,320,000 | 0.63% |
| Mr. Lam Hiu Lo | Total | 3,247,754,684 | 38.42% |
| | Personal | 41,800,000 | 0.49% |

DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS IN SHARES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS (continued)

(c) Interests in underlying shares of Yugang (long positions)

| Name of director | Nature of interest | Number of underlying shares held | Percentage of issued share capital |
|-------------------------|-----------------------------|---|---|
| Mr. Cheung Chung Kiu | Corporate (<i>note 4</i>) | 833,333,333 | 9.86% |

Notes:

- The 2,752,396,360 shares are held by (i) Bookman Properties Limited ("Bookman") as to 126,288,000 shares, and (ii) Regulator Holdings Limited ("Regulator") as to 2,626,108,360 shares. Mr. Cheung Chung Kiu is deemed to be interested in these shares by virtue of his indirect shareholding interests in Bookman and Regulator. Bookman and Regulator are both indirect wholly-owned subsidiaries of Yugang, which is, in turn, owned as to 37.79% by Chongqing Industrial Limited ("Chongqing").
- The 3,194,434,684 shares are held by Chongqing. Mr. Cheung Chung Kiu is deemed to be interested in these shares by virtue of his shareholding interests in Chongqing.
- Mr. Cheung Chung Kiu, Peking Palace Limited, Miraculous Services Limited and Prize Winner Limited have a 35%, 30%, 5% and 30% equity interest in Chongqing respectively. Peking Palace Limited and Miraculous Services Limited are beneficially wholly-owned by Palin Discretionary Trust, a family discretionary trust, the objects of which included Mr. Cheung Chung Kiu and his family. Prize Winner Limited is beneficially wholly-owned by Mr. Cheung Chung Kiu and his associates.
- The 833,333,333 shares represent the interest in the underlying shares in respect of a convertible note of principal amount of HK\$100,000,000 issued by Yugang with maturity date on 31 July, 2004 to Timmex Investment Limited in which Mr. Cheung Chung Kiu has 100% beneficial interest. The convertible note can be converted into Yugang's shares at a conversion price of HK\$0.10 per share during the period from 31 July, 2001 to 31 July, 2002, HK\$0.11 per share for the period from 1 August, 2002 to 31 July, 2003 and HK\$0.12 per share for the period from 1 August, 2003 to 31 July, 2004, subject to adjustment. The total number of underlying shares of the convertible note will change with the change of conversion price of the convertible note from year to year.

Save as disclosed above, as at 31 December, 2003, the Company had not been notified of any interests or short positions in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be kept by the Company pursuant to section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies of the Listing Rules.

DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBENTURES

Under a share option scheme of the Company's ultimate holding company, Yugang, options may be granted to directors and employees of Yugang or its subsidiaries to subscribe for shares in Yugang. On 24 March, 2000, the following directors of the Company were granted share options to subscribe for shares in Yugang at an exercise price of HK\$0.144 per share and exercisable from 24 September, 2000 to 18 October, 2003 as follows:

| Name of director | Number of share options | | |
|----------------------|---------------------------|------------------------------|-----------------------------|
| | Balance at 1.1.2003 | Lapsed during the year | Balance at 31.12.2003 |
| Mr. Cheung Chung Kiu | 10,000,000 | (10,000,000) | – |
| Mr. Lam Hiu Lo | 10,000,000 | (10,000,000) | – |
| Mr. Leung Wai Fai | 10,000,000 | (10,000,000) | – |

Other than as disclosed above and under the heading "Directors' and Chief Executives' Interests in Shares of the Company and its Associated Corporations" above, at no time during the year was the Company, any of its subsidiaries or its holding company, a party to any arrangement to enable the directors of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate, and none of the directors, or any of their associates, had any right to subscribe for shares of the Company, or had exercised any such right during the year.

CONNECTED TRANSACTIONS AND DIRECTORS' INTERESTS IN CONTRACTS

On 22 June, 2000, the Company issued a convertible note (the "Note") to Faircom Limited ("Faircom"), a wholly-owned subsidiary of Yugang with a principal amount of HK\$150 million. Details of the terms of the Note are set out in the circular to shareholders dated 26 May, 2000.

During the year, an interest for the Note of approximately HK\$3,517,000 was paid to Faircom. Faircom transferred the Note to Regulator, a wholly-owned subsidiary of Yugang, on 17 June, 2003. Regulator exercised its conversion rights attaching to the Note and converted the Note into 1,562,500,000 shares of the Company at the conversion price of HK\$0.096 per share on 18 June, 2003.

Both Faircom and Regulator are wholly-owned subsidiaries under the group of companies headed by Yugang which is a substantial shareholder of the Company. By virtue of his interests in Yugang, Mr. Cheung Chung Kiu is deemed to be interested in the Note.

CONNECTED TRANSACTIONS AND DIRECTORS' INTERESTS IN CONTRACTS (continued)

Saved as disclosed above and in note 32 to the financial statements:

- (i) there were no transactions which need to be disclosed as connected transactions in accordance with the requirements of the Listing Rules; and
- (ii) no contracts of significance subsisted at the end of the year or at any time during the year to which the Company or any of its subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly.

SUBSTANTIAL SHAREHOLDERS

As at 31 December, 2003, the following persons (other than directors or chief executives of the Company) had interests or short positions in the shares or underlying shares of the Company which were recorded in the register required to be kept by the Company pursuant to Section 336 of the SFO:

| Name of substantial shareholder (long positions) | Number of shares held | Percentage of issued share capital of the Company |
|--|-----------------------------|---|
| Regulator | 2,626,108,360 | 66.66% |
| Yugang International (B.V.I.) Limited ("Yugang-BVI") | 2,752,396,360 (notes 1 & 2) | 69.87% |
| Yugang | 2,752,396,360 (note 2) | 69.87% |
| Chongqing | 2,752,396,360 (note 2) | 69.87% |
| Palin Holdings Limited ("Palin") | 2,752,396,360 (note 2) | 69.87% |

Notes:

1. Yugang-BVI's interest disclosed above includes 2,626,108,360 shares representing 66.66% held by Regulator and 126,288,000 shares representing 3.21% held by Bookman. Regulator and Bookman are respectively a direct and an indirect wholly-owned subsidiary of Yugang-BVI, therefore Yugang-BVI has a deemed interest in a total of 2,752,396,360 shares by virtue of its shareholding interests in Regulator and Bookman.
2. The interests in 2,752,396,360 shares held by Yugang-BVI, Yugang, Chongqing and Palin as shown above refer to interests in the same block of shares. Yugang-BVI is a direct wholly-owned subsidiary of Yugang, and Yugang is owned by Chongqing as to 37.79%, which is controlled by Mr. Cheung Chung Kiu. The said interests are also duplicated with the interest in shares of the Company of Mr. Cheung Chung Kiu as disclosed on page 14.

Save as disclosed above, as at 31 December, 2003, the Company has not been notified of any other relevant interests or short positions in the issued share capital of the Company to be recorded in the register required to be kept by the Company pursuant to Section 336 of the SFO.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's Bye-laws, or the laws of Bermuda, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

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

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities during the year.

SUBSEQUENT EVENTS

Details of significant events which took place subsequent to the balance sheet date are set out in note 33 to the financial statements.

CORPORATE GOVERNANCE

The Company has complied throughout the year ended 31 December, 2003 with the Code of Best Practice as set out in Appendix 14 to the Listing Rules.

AUDITORS

A resolution will be submitted to the annual general meeting to re-appoint Messrs. Deloitte Touche Tohmatsu as auditors of the Company.

On behalf of the Board

Lam How Mun Peter

Chairman and Managing Director

Hong Kong, 26 March, 2004