NOTES TO FINANCIAL STATEMENTS

31 December 2003

1. CORPORATE INFORMATION

The registered office of Yanion International Holdings Limited is located at Canon's Court, 22 Victoria Street, 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, mini-audio products, car audio mechanisms, cassette deck mechanisms and related component products, and non-audio products including personal office appliances (the "Electronics Business"); and

- the manufacture, trading and contracting of Chinese medicine products in the PRC.

As further detailed in note 11 to the financial statements, the operations involved in the Electronics Business was discontinued during the year.

2. ADOPTION OF STATEMENT OF STANDARD ACCOUNTING PRACTICE

In the current year, the company has adopted, for the first time, the revised Statement of Standard Accounting Practice ("SSAP") No. 12 – Income Taxes issued by the Hong Kong Society of Accountants.

The principal effect of the implementation of SSAP 12 (Revised) is in relation to deferred tax.

In prior year, deferred taxation was accounted for at the current taxation rate in respect of timing differences between profit as computed for taxation purposes and profit as stated in the accounts to the extent that a liability or an asset was expected to be payable or recoverable in the foreseeable future.

Under the revised SSAP 12, deferred taxation is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the accounts. Taxation rates enacted or substantively enacted by the balance sheet date are used to determine deferred taxation. Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

The adoption of the revised SSAP 12 represents a change in accounting policy, which has been applied retrospectively. The adoption of revised SSAP 12 has had no material impact on the results for the current and prior accounting periods.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

3. BASIS OF PREPARATION OF FINANCIAL STATEMENTS

In preparing the financial statements, the directors have given careful consideration to the following which would likely impact on the future operation and going concern of the Group.

Due to a tightening of the regulation in the PRC, all pharmaceutical manufacturers in the PRC must apply to the State Drug Administration and obtain the Good Manufacturing Practice ("GMP") certification by 30 June 2004. GMP is a certification process laid down by the World Health Organisation to regulate the pharmaceutical industries so as to minimize production errors and drug contamination and to assure product quality. Manufacturers failing to obtain the GMP certification by the stipulated time limit shall have a risk of their Pharmaceutical Manufacturing Enterprise Permit not be renewed such that, in the absence of such permit or other arrangement, the manufacturers cannot continue their production of pharmaceutical products. The GMP standards impose strict compliance procedures.

As of the date of this report, the manufacturing facilities of a subsidiary, Huayi Pharmaceutical Co., Ltd. ("Huayi") have not been upgraded to GMP standards due to the fact that the local government has announced a compulsory reclamation plan of the land on which the manufacturing plant of Huayi is located. Huayi plant therefore has to be relocated by the second half of 2004. Consequently, the plan to upgrade its manufacturing plant to GMP standards has also been suspended pending a decision on the future of the manufacturing plant which is affected by factors as discussed below.

Huayi, through its landlord, is currently negotiating with the local government to finalise the extent of compensation which will affect the ultimate decision of the Huayi management on the relocation and the GMP upgrade plan. The Group is of the reasonable belief that the negotiation with the local government will eventually result in a reasonable compensation for Huayi. The Group is also of the reasonable belief that with the above compensation and Huayi's ability to raise additional finance, Huayi will be able to complete the relocation or arrange to lease a suitable manufacturing plant with GMP standards and resume manufacturing operation in due course. Huayi management is considering various interim alternative arrangements on sales and manufacturing during the transitional period to mitigate the effect of production suspension until a longer term solution associated with the relocation is determined.

Accordingly, the financial statements have been prepared on a going concern basis.

4. PRINCIPAL ACCOUNTING POLICIES

(a) 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.

(b) 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 2003.

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.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

4. PRINCIPAL ACCOUNTING POLICIES (continued)

(c) 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 any impairment losses.

(d) 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.

A joint venture company is treated as:

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

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

(iii) 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

(iv) 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.

(e) 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 are 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.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

4. PRINCIPAL ACCOUNTING POLICIES (continued)

(f) 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 five to ten 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.

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.

(g) 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 provided to write off the cost of fixed assets over their anticipated useful lives on a straight-line basis. The principal annual rates used for this purpose are as follows:

Leasehold land	Over the remaining term of the lease
Leasehold buildings	2%
Plant, machinery and equipment	10% – 15%
Furniture and fixtures	10%
Moulds and tools	$33^1/_3$%
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.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

4. PRINCIPAL ACCOUNTING POLICIES (continued)

(h) Chinese medicine intellectual property and knowhow

Chinese medicine intellectual property and knowhow is stated at cost less impairment losses and is amortised using the straight-line basis over the commercial lives of the underlying medicine products ranging from seven to twenty years, commencing from the date of acquisition.

(i) 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 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.

(j) 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.

(k) Investments

(i) Short term investments

Short term investments in unlisted securities are carried at fair value. At each balance sheet date, the net unrealised gain or losses arising from the changes in fair value of short term investments are recognised in the profit and loss account. Profit and loss on disposal of short term investment representing the difference between the net sales proceeds and the carrying amounts, are recognised in the profit and loss account as they arise.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

4. PRINCIPAL ACCOUNTING POLICIES (continued)

(k) Investments (continued)

(ii) 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 or an individual basis.

(l) Inventories

Inventories are valued at the lower of cost and net realisable value. Cost includes cost of purchase of materials computed using the weighted average cost method and, in the case of work in progress and finished goods, comprise direct materials, direct labour and an appropriate proportion of production overheads. Net realisable value is determined by reference to the anticipated sales proceeds of items sold in the ordinary course of business net of estimated selling expenses after the balance sheet date or to management estimates based on prevailing market conditions.

(m) Deferred taxation

Deferred taxation is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Taxation rates enacted or substantively enacted by the balance sheet date are used to determine deferred taxation.

Deferred taxation is provided for on temporary differences arising on investments in subsidiaries, associated companies and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

(n) Leases

(i) Finance leases

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 assets 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.

(ii) Operating leases

Leases where substantially all the risks and rewards of ownership of assets remain with the lessor are accounted for as operating leases. Rentals under operating leases are charged to the profit and loss account on a straight line basis over the lease term.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

4. PRINCIPAL ACCOUNTING POLICIES (continued)

(o) 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 balance sheet of subsidiaries denominated in foreign currencies are translated into Hong Kong dollars at the applicable rates of exchange ruling at the balance sheet date while the profit and loss is translated at an average rate. The resulting translation differences are included in the exchange fluctuation reserve.

(p) 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 independently administered funds. 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.

The employees of the Group's subsidiaries in the PRC are members of central pension schemes operated by the local governments in the PRC and these subsidiaries make mandatory contributions to these central pension schemes to fund the employees' retirement benefits. The retirement contributions paid by the PRC subsidiaries are based on certain percentages of the employees' salaries cost in accordance with the relevant regulations in the PRC, and are charged to the profit and loss account as incurred. The Group discharges its retirement obligations upon payment of the retirement contributions to the central pension schemes operated by the local governments in the PRC.

(q) 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;

(ii) from contracting revenues, when services have been rendered or substantially performed in accordance with the terms of the contract; and

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

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

4. PRINCIPAL ACCOUNTING POLICIES (continued)

(r) 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.

(s) 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.

5. SEGMENT INFORMATION

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:

Continuing operations

a. the manufacture, trading and contracting of Chinese medicine products;

Discontinuing operations

b. the trading of Internet phone sets and provision of related services;

c. the manufacture and trading of CD/VCD players and mechanisms, amplifiers, and mini-audio products; and

d. the manufacture and trading of car audio mechanisms, cassette deck mechanisms, personal office appliances and related products.

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.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

5. 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

	Continuing operations		Discontinuing operations							
	Manufacture, trading and contracting of Chinese medicine products		Trading of Internet phone sets and provision of related services		Manufacture and trading of CD/VCD players and mechanisms, amplifiers, and mini-audio products		Manufacture and trading of car audio mechanisms, cassette deck mechanisms, personal office appliances and related 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	**20,954**	24,250	**–**	–	**131,690**	116,946	**25,305**	43,991	**177,949**	185,187
Segment results	**(32,039)**	8,128	**(27)**	(20,990)	**(21,596)**	(31,106)	**(890)**	(6,084)	**(54,552)**	(50,052)
Interest income									**92**	570
Provision for impairment in value of investment									**–**	(250,000)
Gain on discontinuing operations									**10,566**	–
Unallocated expenses									**(15,906)**	(15,854)
Loss from operating activities									**(59,800)**	(315,336)
Finance costs									**(2,341)**	(1,279)
Loss before tax									**(62,141)**	(316,615)
Taxation									**(188)**	31
Loss before minority interests									**(62,329)**	(316,584)
Minority interests									**9,723**	(6,134)
Net loss from ordinary activities attributable to shareholders									**(52,606)**	(322,718)

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

5. SEGMENT INFORMATION (continued)

(a) Business segments (continued)

Group

	Continuing operations		Discontinuing operations							
	Manufacture, trading and contracting of Chinese medicine products		Trading of Internet phone sets and provision of related services		Manufacture and trading of CD/VCD players and mechanisms, amplifiers, and mini-audio products		Manufacture and trading of car audio mechanisms, cassette deck mechanisms, personal office appliances and related 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 assets	**208,435**	174,811	**3,181**	3,177	**–**	40,751	**–**	19,804	**211,616**	238,543
Unallocated assets									**3,929**	80,594
Total assets									**215,545**	319,137
Segment liabilities	**17,882**	9,382	**2,119**	2,088	**–**	24,544	**–**	9,800	**20,001**	45,814
Unallocated liabilities									**28,952**	42,076
Total liabilities									**48,953**	87,890
Other segment information:										
Capital expenditure	**1,732**	1,747	**–**	–	**4,504**	2,257	**886**	854	**7,122**	4,858
Unallocated capital expenditure									**200**	–
Total capital expenditure									**7,322**	4,858
Amortisation of goodwill	**10,282**	4,284	**–**	6,787	**–**	–	**–**	–	**10,282**	11,071
Provision for impairment in value of goodwill	**–**	–	**–**	14,015	**–**	–	**–**	–	**–**	14,015
Provision against inventories	**823**	–	**–**	–	**902**	2,792	**178**	1,056	**1,903**	3,848
Provision for impairment of fixed assets	**–**	–	**–**	–	**6,722**	4,771	**1,324**	1,805	**8,046**	6,576
Segment depreciation	**1,933**	709	**–**	–	**6,707**	11,485	**1,767**	4,955	**10,407**	17,149
Unallocated depreciation									**22**	19
Total depreciation									**10,429**	17,168
Amortisation and impairment loss of intangible assets	**3,187**	827	**–**	–	**–**	787	**–**	298	**3,187**	1,912

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

5. 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	
	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	**16,409**	18,822	**27,183**	36,499	**11,426**	10,086	**49,961**	55,679	**72,970**	64,101	**177,949**	185,187
Segment results	**(655)**	(2,720)	**(32,329)**	(14,608)	**(1,788)**	(2,390)	**(8,138)**	(14,792)	**(11,642)**	(15,542)	**(54,552)**	(50,052)
Other segment information:												
Segment assets	**2,185**	49,767	**213,360**	241,029	**-**	23,799	**-**	2,112	**-**	2,430	**215,545**	319,137
Capital expenditure	**788**	172	**6,544**	4,686	**-**	-	**-**	-	**-**	-	**7,322**	4,858

6. TURNOVER AND REVENUE

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

	Group	
	2003	2002
	HK$'000	*HK$'000*
Turnover		
Continuing operations	**20,954**	24,250
Discontinuing operations	**156,995**	160,937
	177,949	185,187
Investment income	**1,115**	–
Interest income	**92**	570
Other income	**243**	870
Other revenue	**1,450**	1,440
Total revenue	**179,399**	186,627

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

7. LOSS FROM OPERATING ACTIVITIES

The Group's loss from operating activities is arrived at after charging:

	Group	
	2003	2002
	HK$'000	*HK$'000*
Cost of inventories sold	**147,222**	152,773
Provision against inventories*	**1,903**	3,848
Amortisation of:		
Deferred development costs*	**–**	1,085
Chinese medicine intellectual property and knowhow	**3,187**	827
Depreciation	**10,429**	17,168
Auditors' remuneration:		
Current year	**879**	515
Under provision in prior year	**106**	449
Staff costs (excluding directors' remuneration *(note 8)*)**		
Salaries and wages (include long service payment provision)	**29,907**	31,321
Mandatory provident fund contributions	**504**	453
Less: Amount capitalised	**(1,233)**	(1,101)
	29,178	30,673
Loss on disposal of fixed assets	**1,272**	32
Exchange losses, net	**746**	781

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

** *At 31 December 2003, the Group had no forfeited contributions available to reduce its contributions to the pension scheme in future years (2002: Nil).*

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

8. 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	
	2003	2002
	HK$'000	*HK$'000*
Fees	**200**	200
Basic salaries, housing, other allowances and benefits in kind	**10,942**	10,780
Mandatory provident fund contributions	**122**	125
	11,264	11,105

Fees include HK$200,000 (2002: HK$200,000) payable to the independent non-executive directors. During the year, no options (2002: 114,000) were granted to the two independent non-executive directors under the amended share option scheme adopted details of which are set out in note 30. There were no other emoluments payable to the independent non-executive directors during the year (2002: Nil). The remuneration of the directors fell within the following bands:

	Number of directors	
	2003	2002
Nil – HK$1,000,000	**4**	4
HK$1,000,001 – HK$1,500,000	**1**	1
HK$1,500,001 – HK$2,000,000	**–**	–
HK$2,000,001 – HK$2,500,000	**3**	3
HK$2,500,001 – HK$3,000,000	**1**	–
HK$3,000,001 – HK$3,500,000	**–**	1
	9	9

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

During the year, no share options were granted to any directors and eligible participants in respect of their services rendered to the Group.

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

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

9. FINANCE COSTS

	Group	
	2003	2002
	HK$'000	*HK$'000*
Interest on bank loans, overdrafts and other borrowings wholly repayable within five years	**2,318**	1,217
Interest on finance leases	**23**	62
	2,341	1,279

10. TAXATION

(a) Hong Kong profits tax has been provided at the rate of 17.5% (2002: 16%) on the estimated assessable profits arising in Hong Kong during the year. The rate of tax has been amended with effect from the year of assessment 2003/04. 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	
	2003	2002
	HK$'000	*HK$'000*
Current year's provision:		
Hong Kong	**188**	93
Elsewhere	**–**	22
Overprovision in respect of prior years	**–**	(146)
Tax charge/(credit) for the year	**188**	(31)

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

10. TAXATION (continued)

(b) The taxation charge/(credit) for the year can be reconciled to the loss before tax as stated in the financial statements as follows:–

	2003	2002
	HK$'000	*HK$'000*
Loss before tax	**(62,141)**	(316,615)
Taxation calculated at Hong Kong profits tax of 17.5% (2002: 16%)	**(10,875)**	(50,658)
Tax effect of expenses not deductible for taxation purposes	**2,737**	43,304
Tax effect of non-taxable items	**(462)**	(447)
Tax effect of preferential tax treatment	**–**	(2,174)
Utilisation of previously unrecognized tax losses	**(83)**	–
Deferred tax assets not recognised	**9,754**	12,052
Effect of different tax rates of subsidiaries operating in other jurisdictions	**(883)**	(1,962)
Overprovision in prior years	**–**	(146)
Tax charge/(credit) for the year	**188**	(31)

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

11. DISCONTINUING OPERATIONS

Pursuant to a sale and purchase agreement dated 18 December 2003 and as announced in the Company's announcement on 30 December 2003, the Group disposed of its entire interest in Yanion (BVI) Limited and its subsidiaries, which were mainly engaged in the Electronics Business, for a nominal consideration of HK$1.00 to Mr. Leung Wah Chai and Madam Butt Wing Han, connected persons. The disposal of the above businesses was completed on 31 December 2003 and resulted in a gain on disposal of subsidiaries of approximately HK$10,566,000.

Due to drastic change in the mobile and fixed line long distance telephone charges, the Group's Internet phone business was adversely affected. Management considered the current competition and risk factors did not justify to continue this business area. Further to the full provisions made in the past year, management decided to discontinue the Internet phone business.

The turnover, other revenue, expenses and results of the discontinuing operations for the two years ended 31 December 2003 were as follows:

	Internet phone business		Electronics Business		Total	
	2003	2002	**2003**	2002	**2003**	2002
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*	***HK$'000***	*HK$'000*
Turnover	**–**	–	**156,995**	160,937	**156,995**	160,937
Cost of sales	**–**	–	**(139,444)**	(155,036)	**(139,444)**	(155,036)
Gross profit	**–**	–	**17,551**	5,901	**17,551**	5,901
Other revenue	**–**	1	**169**	826	**169**	827
Selling and distribution costs	**–**	–	**(6,736)**	(7,596)	**(6,736)**	(7,596)
Administrative expenses	**(27)**	(188)	**(25,394)**	(29,666)	**(25,421)**	(29,854)
Provision for impairment in value of fixed assets	**–**	–	**(8,046)**	(6,576)	**(8,046)**	(6,576)
Loss from operating activities	**(27)**	(187)	**(22,456)**	(37,111)	**(22,483)**	(37,298)
Finance costs	**–**	–	**(680)**	(1,280)	**(680)**	(1,280)
Loss before tax	**(27)**	(187)	**(23,136)**	(38,391)	**(23,163)**	(38,578)
Taxation	**–**	(23)	**(188)**	54	**(188)**	31
Loss before minority interests	**(27)**	(210)	**(23,324)**	(38,337)	**(23,351)**	(38,547)
Minority interests	**–**	65	**(699)**	(266)	**(699)**	(201)
Net loss from ordinary activities attributable to shareholders	**(27)**	(145)	**(24,023)**	(38,603)	**(24,050)**	(38,748)

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

11. DISCONTINUING OPERATIONS (continued)

The carrying amount of the total assets and liabilities relating to the discontinuing operations at 31 December 2003 were as follows:–

	Internet phone business		Electronics Business		Total	
	2003	2002	**2003**	2002	**2003**	2002
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*	***HK$'000***	*HK$'000*
Total assets	**3,268**	3,264	**–**	86,214	**3,268**	89,478
Total liabilities	**(3,240)**	(3,209)	**–**	(141,496)	**(3,240)**	(144,705)
Minority interests	**(176)**	(178)	**–**	(1,010)	**(176)**	(1,188)
Net assets	**(148)**	(123)	**–**	(56,292)	**(148)**	(56,415)

The net cash flows attributable to the discontinuing operations for the two years ended 31 December 2003 were as follows:

	Internet phone business		Electronics Business		Total	
	2003	2002	**2003**	2002	**2003**	2002
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*	***HK$'000***	*HK$'000*
Operating	**–**	750	**4,372**	(7,447)	**4,372**	(6,697)
Investing	**–**	(1,114)	**(3,589)**	6,663	**(3,589)**	5,549
Financing	**–**	–	**1,827**	3,020	**1,827**	3,020
Net cash (outflow)/inflow	**–**	(364)	**2,610**	2,236	**2,610**	1,872

12. NET LOSS FROM ORDINARY ACTIVITIES ATTRIBUTABLE TO SHAREHOLDERS

The net loss from ordinary activities attributable to shareholders for the year ended 31 December 2003 dealt with in the financial statements of the Company was approximately HK$5,066,000 (2002: HK$294,390,000).

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

13. 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$52,606,000 (2002: HK$322,718,000) and the weighted average of 571,650,673 (2002: 549,059,440) ordinary shares in issue during the year.

Diluted loss per share amounts for the years ended 31 December 2003 and 31 December 2002 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.

14. FIXED ASSETS

Group

	Leasehold land and buildings HK$'000	Plant, machinery and equipment HK$'000	Furniture and fixtures HK$'000	Moulds and tools HK$'000	Motor vehicles HK$'000	Total HK$'000
Cost:						
At 1 January 2003	11,113	116,954	43,036	88,364	6,812	266,279
Additions	–	2,442	890	3,990	–	7,322
Disposals	–	(9,381)	(6,078)	(15,692)	(374)	(31,525)
Disposal of subsidiaries *(note 32(c))*	(11,113)	(98,054)	(36,368)	(76,662)	(6,438)	(228,635)
At 31 December 2003	**–**	**11,961**	**1,480**	**–**	**–**	**13,441**
Accumulated depreciation and impairment:						
At 1 January 2003	4,041	95,569	35,828	71,502	5,513	212,453
Charge for the year	213	4,498	836	4,684	198	10,429
Impairment	648	1,511	365	5,522	–	8,046
Write back on disposal	–	(8,100)	(6,125)	(11,143)	(331)	(25,699)
Disposal of subsidiaries *(note 32(c))*	(4,902)	(91,053)	(30,719)	(70,565)	(5,380)	(202,619)
At 31 December 2003	**–**	**2,425**	**185**	**–**	**–**	**2,610**
Net book value:						
At 31 December 2003	**–**	**9,536**	**1,295**	**–**	**–**	**10,831**
At 31 December 2002	7,072	21,385	7,208	16,862	1,299	53,826

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

14. FIXED ASSETS (continued)

Company

	Furniture and fixtures *HK$'000*
Cost:	
At 1 January 2003	53
Additions	200
At 31 December 2003	**253**
Accumulated depreciation:	
At 1 January 2003	10
Charge for the year	15
At 31 December 2003	**25**
Net book value:	
At 31 December 2003	**228**
At 31 December 2002	43

The net book value of assets held under finance leases as at 31 December 2002 included a motor vehicle of approximately HK$927,000. The finance lease has been fully settled during the year.

The Group's leasehold land and buildings as at 31 December 2002 were held under medium term leases, situated in Hong Kong and were pledged to secure the Group's bank loans in prior years (note 27).

A provision for impairment in value of approximately HK$8,046,000 (2002: HK$6,576,000) was made during the year as the recoverable amount of leasehold land and buildings, plant, machinery and equipment, furniture and fixtures, and certain moulds and tools declined below their carrying amount.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

15. INTANGIBLE ASSETS

Group

	Chinese medicine intellectual property and knowhow HK$'000	Deferred development costs HK$'000	Total HK$'000
Cost:			
At 1 January 2003	23,532	26,259	49,791
Additions	14,019	–	14,019
Disposal of subsidiaries *(note 32(c))*	–	(26,259)	(26,259)
At 31 December 2003	**37,551**	**–**	**37,551**
Accumulated amortisation:			
At 1 January 2003	827	26,259	27,086
Charge for the year	3,187	–	3,187
Disposal of subsidiaries *(note 32(c))*	–	(26,259)	(26,259)
At 31 December 2003	**4,014**	**–**	**4,014**
Net book value:			
At 31 December 2003	**33,537**	**–**	**33,537**
At 31 December 2002	22,705	–	22,705

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

16. GOODWILL

The amount of goodwill capitalised as an asset, arising from the acquisition of subsidiaries, is as follows:

	Group
	HK$'000
Cost:	
At 1 January 2003 and at 31 December 2003	**150,328**
Accumulated amortisation and impairment:	
At 1 January 2003	51,789
Amortisation for the year	10,282
At 31 December 2003	**62,071**
Net book value:	
At 31 December 2003	**88,257**
At 31 December 2002	98,539

17. INTERESTS IN SUBSIDIARIES

	Company	
	2003	2002
	HK$'000	*HK$'000*
Unlisted shares/capital contributions, at cost	**1**	94,687
Due from subsidiaries	**493,731**	506,701
	493,732	601,388
Provision for impairment	**(313,907)**	(479,024)
	179,825	122,364

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

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

17. INTERESTS IN SUBSIDIARIES (continued)

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 Direct	Indirect	Principal activities
China Medicine International Limited	Hong Kong	HK$2	100	–	Provision of administrative services
Yacata Limited	British Virgin Islands	US$1	100	–	Investment holding
Korning Investments Limited	British Virgin Islands	US$1	–	87	Investment holding
Star Wisdom Investments Limited	British Virgin Islands	US$1	–	87	Investment holding
Huayi Pharmaceutical Co., Ltd	People's Republic of China	RMB126,000,000	–	52	Manufacture, trading and contracting of Chinese medicine products
Kongnet Group Limited	British Virgin Islands	US$1	–	100	Investment holding
Tianjin Weikang Communication Company Limited*	People's Republic of China	US$160,000	–	90	Sales of Internet phone sets and provision of related services
Modern Vocal Limited	British Virgin Islands	US$1,000	–	60	Investment holding
Tianjin Jitong Network Technology Company Limited*	People's Republic of China	US$160,000	–	54	Promotion, sales, distribution, service support and development of a digital data/voice transmission device over the Internet

* Not audited by Horwath Hong Kong CPA Limited or other Horwath International member firms.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

18. INTERESTS IN ASSOCIATES

	Group 2003 HK$'000	2002 HK$'000
Unlisted shares, at cost	–	250,000
Provision for impairment	–	(250,000)
	–	–

Particulars of the associates at 31 December 2003 are as follows:

Company	Business structure	Place of incorporation and operations	Percentage of equity attributable to the Group 2003	2002	Principal activities
Global Cyber Limited* ("Global Cyber")	Corporation	British Virgin Islands	**27**	27	Investment holding

The underlying investment of Global Cyber is:

Company	Business structure	Place of incorporation and operations	2003	2002	Principal activities
Shanghai Dazheng WorldVest Technology Company Limited* ("Shanghai Dazheng")	Corporation	People's Republic of China	**21.6**	21.6	Provision of research & development of video-on-demand systems

* Not audited by Horwath Hong Kong CPA Limited or other Horwath International member firms.

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 were the research and development of VOD systems in the PRC which involved the re-engineering of existing cable TV stations in the PRC by employing related operating software, servers and set-top boxes. For reasons discussed below, operation of Shanghai Dazheng has ceased during the year.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

18. INTERESTS IN ASSOCIATES (continued)

As discussed in the notes to 2002 financial statements of the Group, the dispute relating to the possible infringement of intellectural property right affecting the commercial interest of the Group could not be settled and the relationship with the PRC Party continued to have deteriorated. The directors of Global Cyber and the Company had sought advice from PRC legal counsel as to the appropriate course of action, including arbitration and/or the legal action that should be taken. 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 as at 31 December 2002 and for conservative reason, full provision has been made against the investment cost of HK$250 million in 2002. After reviewing the current status of the dispute and based on the legal advice from PRC legal counsel, during the year, the directors considered that it was not cost effective and not practicable to pursue the dispute any further. As a result, the investment cost in Global Cyber was fully written off against the provision for impairment.

19. LONG TERM INVESTMENT

	Group	
	2003	2002
	HK$'000	*HK$'000*
Unlisted equity investments, at cost	**–**	1,000

The long term investment was disposed of at the consideration of HK$1,000,000 during the year.

20. INVENTORIES

	Group	
	2003	2002
	HK$'000	*HK$'000*
Raw materials	**1,318**	15,686
Work in progress	**3,235**	6,880
Finished goods	**5,606**	8,840
	10,159	31,406

The amount of inventories carried at net realisable value included in the above balance was approximately HK$6,889,000 (2002: HK$8,906,000) at the balance sheet date.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

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

	Group	
	2003	2002
	HK$'000	*HK$'000*
Within 1 month	**1,301**	21,820
2 to 3 months	**858**	6,665
4 to 6 months	**736**	1,327
7 to 12 months	**467**	643
Over 1 year	**10,505**	2,116
	13,867	32,571

22. DEPOSIT FOR INVESTMENT

On 21 March 2003, Huayi has entered into an agreement to acquire from an independent third party (i) 40% equity interest in two Sino-foreign joint venture companies and (ii) the right of exploitation of wild herbs (collectively referred to as the "Investment") at a total consideration of approximately HK$67,888,000. The purpose of the investment is to develop a Chinese medicinal centre and wild herbs harvesting area. Partial payments for the consideration in the total of approximately HK$48,879,000 were made in July 2003. The vendor has agreed with Huayi on 31 December 2003 that the balance of consideration in the amount of approximately HK$19,009,000 be payable by 31 May 2004. The current status of the Investment is detailed in note 33.

23. SHORT TERM INVESTMENT

	Group and Company	
	2003	2002
	HK$'000	*HK$'000*
Participating redeemable preference shares in a fund	**–**	23,415

The short term investment has been redeemed on 8 August 2003 and earned a total investment income of approximately HK$1,115,000 (yielded approximately 4.8%). The proceeds were used to partially repaid other borrowings as disclosed in note 27.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

24. CASH AND CASH EQUIVALENTS AND PLEDGED DEPOSITS

	Group		Company	
	2003	2002	**2003**	2002
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*
Cash and bank balances	**2,980**	31,658	**1,157**	19,394
Time deposits	**–**	4,636	**–**	–
	2,980	36,294	**1,157**	19,394
Less: Pledged time deposits for trust receipt, export loans and bank overdraft facilities *(note 27)*	**–**	(4,636)	**–**	–
Cash and cash equivalents	**2,980**	31,658	**1,157**	19,394

25. ACCOUNTS PAYABLE

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

	Group	
	2003	2002
	HK$'000	*HK$'000*
Within 1 month	**611**	10,521
2 to 3 months	**115**	17,826
4 to 6 months	**163**	6,071
7 to 12 months	**31**	136
Over 1 year	**1,466**	2,257
	2,386	36,811

26. DUE TO A DIRECTOR

The balance due to a director as at 31 December 2002 was unsecured, interest free and had no fixed terms of repayment.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

27. INTEREST-BEARING BANK LOANS AND OTHER BORROWINGS

	Group		Company	
	2003	2002	**2003**	2002
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*
Bank overdrafts, secured	**–**	888	**–**	–
Bank loans, secured	**–**	10,454	**–**	–
	–	11,342	**–**	–
Other borrowings – unsecured	**22,597**	3,405	**19,192**	–
	22,597	14,747	**19,192**	–
Bank overdrafts repayable within one year or on demand	**–**	888	**–**	–
Bank loans repayable:				
Within one year	**–**	10,313	**–**	–
In the second year	**–**	141	**–**	–
	–	10,454	**–**	–
Other borrowings repayable:				
Within one year	**20,606**	1,414	**19,192**	–
In the second year	**1,991**	1,991	**–**	–
	22,597	3,405	**19,192**	–
	22,597	14,747	**19,192**	–
Portion classified as current liabilities	**(20,606)**	(12,615)	**(19,192)**	–
Long term portion	**1,991**	2,132	**–**	–

The above bank loans as at 31 December 2002 were 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$7,072,000 as at 31 December 2002; and

(ii) a fixed charge on the Group's time deposits of HK$4,636,000 as at 31 December 2002 (note 24).

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

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

Included in bank loans as at 31 December 2002 was a total of HK$4,905,000 of trust receipt and export loans and a term loan of HK$1,799,000 with maturity dates of over three months. The remaining balance of HK$3,750,000 was repayable within three months from the date of advance.

In July 2003, the Company was 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 by the Group. The borrowings were partially repaid during the year out of the proceeds from redemption of the short term investment as referred to in note 23. The borrowings are unsecured and interest bearing at Hong Kong dollar prime rate plus 2% per annum, payable upon repayment of principals. The borrowings are repayable by 31 December 2004.

As at 31 December 2003, save for the unsecured other borrowings, the Group and the Company did not have any other bank debts, corporate guarantee or pledge of assets remained outstanding from the prior year.

28. FINANCE LEASES PAYABLES

At 31 December 2003, the total future minimum lease payments under the finance lease and their present values, were as follows:

Group

	Minimum lease payments 2003 *HK$'000*	Minimum lease payments 2002 *HK$'000*	**Present value of minimum lease payments 2003 *HK$'000***	Present value of minimum lease payments 2002 *HK$'000*
Amounts payable:				
Within one year	–	355	–	332
Total minimum finance lease payments	–	355	–	332
Future finance charges	–	(23)		
Total net finance lease payables – current	–	332		

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

29. DEFERRED TAXATION

	Group	
	2003	2002
	HK$'000	*HK$'000*
At beginning of year	**136**	136
Disposal of subsidiaries *(note 32(c))*	**(136)**	–
At end of year	**–**	136

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	
	2003	2002	**2003**	2002
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*
Accelerated capital allowances	**–**	136	**–**	2,773
Tax losses	**–**	–	**(11,860)**	(35,502)
	–	136	**(11,860)**	(32,729)

The Company had unprovided deferred tax assets in respect of tax losses in the amount of approximately HK$6,661,000 at the balance sheet date (2002: HK$5,286,000).

30. SHARE CAPITAL

Shares

	2003	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

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

30. SHARE CAPITAL (continued)

Pursuant to the special resolutions passed at 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. The issued share capital of HK$285,825,000 was reduced to HK$5,717,000 and the capital reduction of HK$280,108,000 has been applied to set off against 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 had been subdivided into 50 unissued shares of HK$0.01 each, and the issued and unissued share capital of the Company comprise 50,000,000,000 new shares of HK$0.01 each.

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

	Number of ordinary shares	Share capital *HK$'000*
At 1 January 2003	571,650,673	285,825
Reduction in nominal value of shares	–	(280,108)
At 31 December 2003	**571,650,673**	**5,717**

Share options

The Company adopted a new share option scheme on 7 June 2002, details of which are set out under the heading "Share Option Scheme" in the Report of the Directors.

Movements in share options during the year were as follows:

	Number of share options
Share options outstanding at beginning of year	44,390,000
Share options lapsed during the year	(44,390,000)
Share options outstanding at end of year	–

On 21 October 2002, the Company granted a total of 44,390,000 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 5 November 2002 to 4 November 2003. The subscription price payable upon the exercise of each option was HK$0.79, subject to adjustment. All share options granted have lapsed on 4 November 2003.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

31. RESERVES

Company

	Share premium HK$'000	Contributed surplus HK$'000 (note i)	Accumulated losses HK$'000	Total HK$'000
At 1 January 2002	271,195	76,838	(218,234)	129,799
Issue of new shares *(note ii)*	45,810	–	–	45,810
Share issue expenses	(1,790)	–	–	(1,790)
Net loss for the year	–	–	(294,390)	(294,390)
At 31 December 2002	315,215	76,838	(512,624)	(120,571)
Capital reduction	–	–	280,108	280,108
Share premium reduction	(232,515)	–	232,515	–
Net loss for the year	–	–	(5,065)	(5,065)
At 31 December 2003	**82,700**	**76,838**	**(5,066)**	**154,472**

Note:

(i) 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 therefore 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.

(ii) On 12 June 2002, 50,900,000 new ordinary shares with a par value of HK$0.50 each was issued on placement at a consideration of HK$1.40 per share. The excess of the share consideration over the nominal value of the issued shares of HK$45,810,000 was credited to the share premium account. The net proceeds from the placing of HK$69.5 million were used to finance the capital contribution to the equity interest in Huayi and for general working capital of the Group.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

32. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

(a) Reconciliation of loss before tax to net cash outflow generated from operating activities

	Group	
	2003	2002
	HK$'000	*HK$'000*
Loss before tax	**(62,141)**	(316,615)
Provision for impairment in value of investment	**–**	250,000
Provision for impairment in value of fixed assets	**8,046**	6,576
Provision for impairment in value of goodwill	**–**	14,015
Provision against inventories	**1,903**	3,848
Provision for doubtful debts	**9,832**	1,600
Depreciation	**10,429**	17,168
Amortisation of intangible assets	**3,187**	1,912
Amortisation of goodwill	**10,282**	11,071
Loss on disposal of fixed assets	**1,272**	32
Interest income	**(92)**	(570)
Interest expense	**2,341**	1,279
Gain on disposal of short term investment	**(1,115)**	–
Gain on disposal of subsidiaries	**(10,566)**	–
Operating loss before working capital changes	**(26,622)**	(9,684)
Increase in inventories	**(4,437)**	(340)
Increase in accounts receivable	**(3,752)**	(19,128)
Decrease/(increase) in prepayments and other receivables	**3,633**	(8,521)
Increase in accounts payable	**8,393**	13,464
Increase in other payables and accruals	**14,524**	1,960
Increase in amounts due to related companies	**719**	292
Decrease in trust receipt and export loans with maturity over three months	**(439)**	(12,625)
Net cash used in operations	**(7,981)**	(34,582)

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

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

(b) Acquisition of subsidiaries

	Group	
	2003	2002
	HK$'000	*HK$'000*
Net asset acquired:		
Fixed assets	–	9,732
Intangible assets	–	23,532
Inventories	–	6,838
Accounts receivable	–	5,468
Prepayments and other receivables	–	2,372
Cash and bank balances	–	1,713
Accounts payable	–	(2,069)
Other payables and accruals	–	(5,407)
Minority interests *(note 32(d))*	–	(45,232)
	–	(3,053)
Goodwill on acquisition	–	116,393
	–	113,340
Satisfied by:		
Cash consideration	–	113,340

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

	Group	
	2003	2002
	HK$'000	*HK$'000*
Cash consideration	–	113,340
Deposits paid on acquisition	–	(101,500)
Cash and bank balances acquired	–	(1,713)
Net outflow of cash and cash equivalents in respect of the acquisition of subsidiaries	–	10,127

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

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

(c) Disposal of subsidiaries

	Group	
	2003	2002
	HK$'000	*HK$'000*
Net assets disposed:		
Fixed assets	**26,016**	–
Inventories	**28,330**	–
Accounts receivable	**12,624**	–
Prepayments and other receivables	**4,040**	–
Cash and bank balances	**2,866**	–
Pledged deposits	**3,866**	–
Accounts payable	**(42,818)**	–
Other payables and accruals	**(22,964)**	–
Due to a related company	**(1,118)**	–
Minority interests *(note 32(d))*	**(1,709)**	–
Due to a director	**(9,550)**	–
Bank loans and overdraft	**(7,168)**	–
Tax payable	**(2,645)**	–
Deferred taxation	**(136)**	–
Reverse of exchange fluctuation	**(200)**	–
Negative net assets sold	**(10,566)**	–
Gain on disposal of subsidiaries	**10,566**	–
Satisfied by cash consideration *(note)*	**–**	–

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

	Group	
	2003	2002
	HK$'000	*HK$'000*
Cash consideration *(note)*	**–**	–
Cash and bank balances disposed	**(2,866)**	–
Bank overdrafts	**1,913**	–
Trust receipt and export loans with maturity within three months	**649**	–
Net outflow of cash and cash equivalents in respect of the disposal of subsidiaries	**(304)**	–

Note: Consideration for the disposal of subsidiaries was satisfied by cash of HK$1.00.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

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

(d) Analysis of changes in financing during the year

	Issued capital, (including share premium) *HK$'000*	Finance lease payables *HK$'000*	Due to a director, bank and other borrowings *HK$'000*	Minority interests *HK$'000*
At 1 January 2002	531,570	625	4,624	871
Net cash inflow/(outflow) from financing	69,470	(355)	6,570	–
Interest element of finance lease payment	–	62	–	–
Share of net profit for the year	–	–	–	6,134
Arising from acquisition of subsidiaries *(note 32(b))*	–	–	–	45,232
At 31 December 2002	601,040	332	11,194	52,237
Net cash inflow/(outflow) from financing	–	(355)	20,373	–
Capital reduction	(280,108)	–	–	–
Share premium reduction	(232,515)	–	–	–
Accrued interest	–	–	721	–
Interest element of finance lease payment	–	23	–	–
Share of net loss for the year	–	–	–	(9,723)
Arising from disposal of subsidiaries *(note 32(c))*	–	–	(9,691)	(1,709)
At 31 December 2003	**88,417**	**–**	**22,597**	**40,805**

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

33. CONTINGENT LIABILITIES

	Group		Company	
	2003	2002	**2003**	2002
	HK$'000	*HK$'000*	***HK$'000***	*HK$'000*
Guarantees given to banks in connection with facilities granted to subsidiaries	**–**	–	**–**	34,000
Bills discounted with recourse	**–**	3,685	**–**	–
	–	3,685	**–**	34,000

(a) As at 31 December 2003, all corporate guarantee commitment previously undertaken by the Group associated with the discontinuing operations have been cancelled. As at 31 December 2002 credit facilities utilised by the subsidiaries under the Company's guarantee amounted to HK$15,027,000.

(b) As detailed in note 22 to the financial statements, Huayi has contracted for the acquisition of (i) 40% equity interest in two Sino-foreign joint venture companies and (ii) the right of exploitation of wild herbs for the purpose of development of a Chinese medicinal centre and wild herbs harvesting area. As of 31 December 2003, partial payments of approximately HK$48,879,000 have been made and the remaining consideration of approximately HK$19,009,000 has been disclosed under capital commitments (note 35).

Owing to a change in senior management of Huayi resulting from a change of representatives nominated by the minority shareholder, the board of Huayi which includes members nominated by the minority shareholder has not yet come to a decision of whether to complete the above mentioned acquisition. The situation is further exasperated due to competing financial resources. There is now the uncertainty in the ability of Huayi to obtain adequate funding to settle the remaining consideration by the extended deadline of 31 May 2004 in view of possible substantial capital required for the possible building of a new plant and relocation and upgrade of manufacturing plants to GMP standards. In accordance with the sale and purchase agreement, the vendor has the right to cancel the acquisition and claim for losses to the extent the vendor has suffered, which is not quantifiable at this stage. Notwithstanding the above, the Group consider that they would negotiate with the vendor such that a satisfactory resolution would be found which would limit any losses to the Group to an acceptable level.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

34. OPERATING LEASE ARRANGEMENTS

	Group	
	2003	2002
	HK$'000	*HK$'000*
Minimum lease payments paid under operating leases	**13,264**	10,505
Less: Amount capitalised	**(414)**	(308)
	12,850	10,197

At 31 December 2003, 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	
	2003	2002
	HK$'000	*HK$'000*
Within one year	**3,084**	11,805
In the second to fifth years, inclusive	**375**	10,847
	3,459	22,652

Operating lease payments represent rentals payable by the Group on certain of its leased properties. Leases are negotiated for terms of one to two years at fixed rental.

The Company did not have any operating lease commitments at the balance sheet date (2002: HK$Nil).

35. CAPITAL COMMITMENTS

	Group	
	2003	2002
	HK$'000	*HK$'000*
Contracted, but not provided for:		
Acquisition of investment *(note 22)*	**19,009**	–
Acquisition of a subsidiary	**–**	43,028
Acquisition of Chinese medicine intellectual property and knowhow	**–**	9,346

The Company did not have any capital commitments at the balance sheet date (2002: HK$Nil).

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

36. RELATED PARTY TRANSACTIONS

(a) Set out below are the related party transactions disclosed in accordance with SSAP 20 issued by the Hong Kong Society of Accountants:–

		Group	
		2003	2002
	Notes	***HK$'000***	*HK$'000*
Purchases of raw materials from a related company:			
Simple Link Company Limited ("Simple Link")	*(i)*	**658**	885
Rental expenses paid to related companies:	*(ii)*		
Bestbond Company Limited ("Bestbond")		**1,650**	1,650
Well Hero Industries Limited ("Well Hero")		**216**	216
Kamga Investment Limited ("Kamga")		**216**	216
WorldVest Capital Limited ("WorldVest")		**603**	804
Sun View Company Limited ("Sun View")		**1,080**	1,080
Rental expenses paid to a director:			
Leung Wah Chai	*(ii)*	**720**	720
Consultancy fees paid/payable to a related company:			
WorldVest	*(iii)*	**900**	900
Purchases of fixed assets from a related company:			
WorldVest	*(iv)*	**200**	–

i) 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 2002 amounted to HK$778,000. The balance due was unsecured, interest-free and has no fixed terms of repayment. As at 31 December 2003, the balance due to Simple Link was disposed of (note 32(c)).

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 2003 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.

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

36. RELATED PARTY TRANSACTIONS (continued)

(a) (continued)

ii) 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. In October 2003, the lease of the office premise and the related rental deposit of approximately HK$246,000 was assigned by an agreement from WorldVest to the Group. The related balance due to WorldVest at 31 December 2003 was approximately HK$246,000 (2002: HK$67,000). The balance is unsecured, interest free and has no fixed terms of repayment.

iii) The consultancy fees were charged in accordance with the terms of the service and management fee agreements. The balance due to WorldVest at 31 December 2003 in respect of consultancy fees outstanding was HK$450,000 (2002: HK$450,000). The balance due is unsecured, interest-free and has no fixed terms of repayment.

iv) The Directors have reviewed lists of the used fixed assets and physically inspected the condition of the assets and considered that the terms and offer price of these used fixed assets were in accordance with general commercial practice and were fair and reasonable to the Company. The amount due to WorldVest in respect of purchase of fixed assets at 31 December 2003 was HK$200,000 (2002: HK$Nil). The balance 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. Leung Wah Chai and Butt Wing Han are directors and controlling shareholders of Well Hero and Kamga. Cheng Shu Wing, Guo Duen How, Tom and Wu Fred Fong are directors of WorldVest. Sun View is owned by an associated person of Kao Ying Lun.

37. CONNECTED TRANSACTIONS

In addition to the related party transactions disclosed in note 36 which also constituted connected transactions under the Listing Rules, the following transactions constitute connected transactions under the Listing Rules.

		Group	
		2003	2002
	Notes	***HK$'000***	*HK$'000*
Payment and accrual/deposit paid in respect of purchase of intellectual and operating rights of twelve Chinese medicines from a minority interest, Huahe Pharmaceutical Co., Limited ("Huahe")	*(i)*	**9,346**	4,673
Purchase of raw materials/herbs from Huahe	*(i)*	**1,622**	1,533
Sales of medicine products to China National Group Corporation of Traditional and Herbal Medicine ("China National Medicine")	*(ii)*	**4,104**	1,751

NOTES TO FINANCIAL STATEMENTS (continued)

31 December 2003

37. CONNECTED TRANSACTIONS (continued)

Note:

(i) The directors consider that the acquisition of the twelve Chinese medicines and purchase of raw materials/herbs were based on arm's length negotiation with Huahe. These transactions were made in the ordinary and usual course of business with terms made on normal commercial terms.

(ii) China National Medicine is the controlling shareholder of Huahe. The Directors consider that these sales were made in the ordinary and usual course of business with terms made on normal commercial terms.

38. POST BALANCE SHEET EVENTS

(a) On 24 July 2003, the Group has fulfilled all its capital contribution commitment to Huayi of approximately HK$63 million. The Group has also made additional contribution of RMB8,328,000 (equivalent to HK$7,852,000) which pertained to capital contribution defaulted by the 13% minority shareholder of 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 additional subscription, details of which was published in the Company's announcement of 3 February 2004, increased the Company's shareholding in Korning from 87% to 94% with effect from 2 January 2004.

(b) On 20 April 2004, the Company has entered into a subscription agreement with DBS Bank Ltd ("DBS"), whereby DBS has agreed to conditionally subscribe in tranches for an aggregate principal amount of up to HK$24,940,000 of unsecured convertible notes for the period ending on 15 June 2004. The convertible notes shall mature on 30 April 2006, unless redeemed earlier by the Company or converted into shares by the noteholders prior to the maturity date. The notes have with a coupon interest rate of 2% per annum and may be convertible into new conversion shares at a conversion price of HK$0.43 per share. The proceeds from the convertible notes will be used for general working capital of the Group.

39. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 22 April 2004.