Chairman's Statement and Management Discussion and Analysis

I am pleased to report the activities of South China Industries Limited (the "Company") and its subsidiaries (together the "Group") for the year ended 31 December 2003.

BUSINESS REVIEW

The Group recorded a turnover of HK$3.1 billion for the year ended 31 December 2003, an impressive increase of HK$1.4 billion or 82.6%, compared with that of 2002. The increase in the Group's turnover was mainly attributable to the impressive turnover growth of Wah Shing International Holdings Limited ("Wah Shing") and the full consolidation of the results of the travel business in which the Group acquired the remaining interest in December 2002. As a result, gross profit increased by HK$53 million. The decrease in the Group's gross profit margin from 14.9% to 9.9% was mainly due to the increase in the direct manufacturing costs and the relatively low gross profit margin of the travel business. Distribution and operating expenses, though significant due to increasing turnover, were under strict cost control. The Group had a write back of HK$15.4 million of allowance for doubtful debts mainly on two major former customers of Wah Shing following the receipt of their settlement, compared to a HK$24.3 million allowance for doubtful debts charged in 2002. There was a gain on disposal of non-trading securities of HK$8.9 million. The impairment loss of non-trading securities was also greatly reduced to HK$2 million as compared to HK$16.4 million last year. Overall, the Group achieved a better profit from operations of HK$79.8 million in the current year, when compared to HK$10.2 million in the last year.

In 2003, there was a write back of allowance for advances to an associate of HK$40.0 million due to the significant appreciation in property value of our 30% owned Grade-A commercial building, "The Centrium" in Central, as compared to the provision of HK$75.0 million made in 2002. Profit attributable to shareholders in 2003 was HK$67.1 million which showed a marked increase of 3.4 times as compared to the previous year.

Trading and Manufacturing

Wah Shing reported an impressive growth of 48% in turnover to HK$1.83 billion, principally due to increased orders from certain customers. Wah Shing faced a number of challenges during the year. The continuing consolidation of toy companies and concentration of retailers both in the United States and Europe and the over supply of production capacity in China continued to exert price reduction pressure. As the US military conflicts in Iraq along with the Severe Acute Respiratory Syndrome ("SARS") fallout had delayed the merchandising cycle of overseas buyers to later months, Wah Shing had to incur extra costs to fulfil customer orders with shorter delivery times. The weak US dollar, the rising material prices and labour costs in Mainland China also added to the manufacturing costs. Against these adverse factors, Wah Shing continued to improve its cost control and efficiency and, with some bad debts recovered, reported a net profit of HK$43.3 million.

Wah Shing Electronics Company Limited ("WSE"), a subsidiary of Wah Shing, faced a decrease in revenue and, despite imposition of strict cost control schemes, reported a loss of approximately HK$5.5 million for the year.

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First half figures for our footwear and garment businesses fell substantially due to cancellation of orders by major overseas customers as a result of the outbreak of SARS. However, major sales efforts in the second half made up for most of the revenue gap, contributing to a net profit of approximately HK$5.7 million for the year.

The Group's associate Nority International Group Limited ("Nority") which engages in the manufacture and export of athletic-style leisure footwear, was also adversely affected by the war in Iraq and the SARS epidemic and reported a loss of HK$22.6 million in 2003.

Travel and Related Services

2003 was a particularly difficult period for all travel related industries due to the effects of SARS. However, for our Hong Kong Four Seas Tours Limited ("Fourseas"), 2003 was an exceptionally successful year. Fourseas was able to capitalise on a weak competitive market during the SARS period to cement its position as one of Hong Kong's leading airline consolidators. This was reflected in the posting of a very strong second half performance.

Fourseas began to develop the Mainland market in the year by opening an office in Guangzhou, and so far its performance has been satisfactory.

Property Investment and Development

The property market picked up steadily after the SARS period with a rise in general property prices and transaction volume. Our property arm enjoyed a 5.7% increase to report a contribution of HK$6.6 million, as a result of increased rental revenue from higher property occupancy rates and a reviving commercial sector. A more significant appreciation in property value was recorded in respect of the 30% owned Grade-A commercial building, "The Centrium" in Central. Over 85% of the gross floor area was leased out at the end of 2003, generating satisfactory revenue.

In Shanghai, a 20.4% owned property development declared dividends to the Group.

Information and Technology

The Group consolidated its IT portfolio to divest loss-making interests and pooled together its product base and market resources. The turnover of the IT business declined by 55% to HK$37.4 million, with an aggregated loss of HK$4.5 million in 2003. For each separate IT joint venture on Mainland China, our strategic direction was to focus heavily on market development, which has given us a head start for the coming year. Furthermore, our joint ventures continue to provide low-cost programming services to strengthen our Hong Kong products, of which our turn-key stock-trading solution is expected to be marketed in the near future.

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Agricultural Business

The Group's agricultural business in the PRC was not profitable in 2003, as fluctuating market prices and operational difficulties made this a challenging period. The plantation of lychee and longan trees in Zhengcheng and Boluo, Guangdong had much lower average production costs taking advantage of economies of scale as more trees matured to become fruit bearing. The lake farm in Nanjing has been changed from a pure crab rearing farm to one which rears several species of fish. This will have lower margins, but it is considered justified by its lower risk factor and higher diversification. The Group commenced investment in a new plantation farm of winter dates ("dongzhao") in Haixing County Hebei Province, the PRC at the end of December 2003.

LIQUIDITY AND FINANCIAL RESOURCES

As at 31 December 2003, the Group had a current ratio of 1.1 and a gearing ratio of 10.4% (31 December 2002: 1.2 and 10.9% respectively). The gearing ratio is computed by comparing the Group's total long-term bank borrowings of HK$75.1 million to the Group's shareholders' funds of HK$724.2 million. The Group's operations continue to be financed by internal resources and bank borrowings. The Directors believe that the Group has sufficient banking facilities and working capital for its operations.

EXPOSURE TO FLUCTUATIONS IN EXCHANGE RATES AND RELATED HEDGES

As at 31 December 2003, the Group had no significant exposure to fluctuations in exchange rates and any related hedges.

CAPITAL STRUCTURE

The Group had no other debt securities or capital instruments as at 31 December 2003 and up to the date of this report.

PROSPECTS

Trading and Manufacturing

A number of industry-wide challenges continue to impact our toy manufacturing business. Amongst them are mounting price reduction pressure from customers and, the ever-increasing manufacturing costs exacerbated by stringent product and workplace safety requirements, market demand for more products and wider variety of novelty designs, and pressure on the revaluation of the Renminbi. To meet these challenges, Wah Shing is striving to enhance its own product development and design capabilities, to upgrade the machinery and equipment, and to improve the production workflow and factory environment in order to capture larger volume orders. Wah Shing will also continue to identify sources of lower cost fabric and raw materials to save on the overall procurement costs. The progress of its new factory in Yunan, Guangdong, which started operation in the second half of 2003, is being closely monitored.

WSE is experiencing good sales on a few new projects and is likely to return to the profitability.

In March 2004, our shoes business won Wal-Mart's "International Supplier of the Year 2003" award in recognition of its quality, on-time shipment and good co-operation. In view of the positive impact on turnover resulting from this, our strategy in the coming months is to focus on building up a strong customer base and continue to push our production units to fuller capacity.

Nority has a sound financial position and is seeking to diversify its income.

We have obtained a final judgment dated 20 December 2003 in favour of the Group from The Supreme Court of The People's Republic of China in respect of the litigation between a wholly-owned subsidiary of the Company and Nanjing Micromotor Co., our Nanjing joint venture partner. The joint venture owns a street of valuable investment properties located in the prime commercial area at the heart of the city (the "Properties"). The Properties presently generate annual rental income of over RMB11 million. Under the final judgment, the joint venture partner was ordered to compensate the Group for the damages suffered as a result of the breach of the joint venture agreement. We are planning to use the compensation to buy out the entire group companies of our joint venture partners and the negotiation process is now underway.

Travel and Related Services

The agency side of the businesses remains the strength and central focus of the travel and related services. Backed by year 2003's performance, the Group is confident that our travel business is on the road to success. Fourseas, having proven that it is highly competitive in ticketing consolidation, will further develop its corporate travel services and certain related services in Mainland China.

Property Investment and Development

The PRC government policy to extend the Individual Travel Permit Scheme for more cities in Mainland China will boost the local economy. The Group's rental properties around tourist districts are expected to generate higher rental income on renewals or new leases. The improved market sentiment should attract more investment in Hong Kong and greater demand for high quality offices. We expect the rental income from The Centrium in Central to continue to rise and expect full occupancy very soon.

Looking forward to a rising property market, we shall re-tune our property portfolio to divest non-core assets and seek attractive investment properties in both Hong Kong and Mainland China.

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Information and Technology

The operating environment is still difficult due to the keen competition in the IT market in the PRC. The Group's target is to make a profit in the IT segment in 2004 and the prospects of our mainland IT joint ventures are improving. In Hong Kong, plans to further develop in-house platforms at a low cost structure should benefit the Group's customer products and overall operation efficiency.

Agricultural Business

Management maintains the view that the agricultural industry in Mainland China has great potential. Having already gained control of 36 square kilometers of agricultural land and lake areas across Jiangsu, Guangdong and Hebei provinces, we intend to further expand, so as to attain the size and diversification we need to guarantee a promising future. Government support in developing agricultural sector provides a promising future where we can take advantage of subsidies and stable markets in the years to come.

MATERIAL ACQUISITIONS AND DISPOSALS OF SUBSIDIARIES

During the year, the Group acquired the entire equity interest of Spring Joy Industrial Limited which held the investment of agricultural fruit plantation in the PRC for a consideration of HK$10 million.

PLEDGES OF ASSETS

As at 31 December 2003, details of pledges of assets of the Group are set out in note 43 to the financial statements.

CONTINGENT LIABILITIES

As at 31 December 2003, details of the Group's contingent liabilities are set out in note 42 to the financial statements.

EMPLOYEES

As at 31 December 2003, the total number of employees of the Group was approximately 15,000. Employees' cost (including directors' emoluments) amounted to approximately HK$414.6 million for the year.

The Group considers its employees as its most valuable asset. In addition to salary, other fringe benefits such as medical subsidies, provident fund and subsidised training programmes are offered to all employees of the Group. Performance of the employees is normally reviewed on an annual basis with adjustment compatible to the market. Individual employee may also receive a discretionary bonus at the end of each year based on performance. The Company adopted an employee share option scheme on 31 May 2002.

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APPRECIATION

On behalf of the Board, I wish to express my gratitude to our customers and shareholders for their continued support and all our staff members for their hard work and dedicated services.

On behalf of the Board

Ng Hung Sang, Robert
Chairman

Hong Kong Special Administrative Region
of the People's Republic of China
24 April 2004