

Report of the Directors

For the year ended 30 June 2004

The directors present their report and the audited financial statements of Vitop Bioenergy Holdings Limited (the "Company") and its subsidiaries (hereinafter collectively referred to as the "Group") for the year ended 30 June 2004.

PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding. The principal activities of its subsidiaries are manufacturing and trading of healthcare bedding, underclothing and other health products in the People's Republic of China, excluding Hong Kong.

RESULTS AND APPROPRIATIONS

The results of the Group for the year ended 30 June 2004 and the state of affairs of the Group and the Company as at that date are set out in the financial statements on pages 19 to 50.

The directors recommend the payment of a final dividend of HK1 cent per ordinary share in respect of the year ended 30 June 2004. Subject to shareholders' approval at the forthcoming annual general meeting of the Company, the final dividend will be paid in cash on or about 20 October 2004 to the shareholders whose names appear on the registers of members of the Company on 18 October 2004.

SUMMARY OF FINANCIAL INFORMATION

A summary of the published results and the assets and liabilities of the Group for the last four financial years is set out on page 51. This summary does not form part of the audited financial statements.

FIXED ASSETS

Details of the movements in the Group's fixed assets during the year are set out in note 11 to the financial statements.

INTANGIBLE ASSETS

Details of the movements in the Group's intangible assets during the year are set out in note 12 to the financial statements.

SHARE CAPITAL AND SHARE OPTIONS

Details of the movements in the Company's share capital and share options during the year, together with the reasons therefor, are set out in notes 21 and 22 to the financial statements, respectively.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's articles of association or the laws of the Cayman Islands, being the jurisdiction in which the Company was incorporated, which would oblige the Company to offer new shares on a pro rata basis to existing shareholders.

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PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES OF THE COMPANY

During the year, there were no purchases, sales or redemptions by the Company, or any of its subsidiaries, of the Company's listed securities.

RESERVES

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

DISTRIBUTABLE RESERVES

As at 30 June 2004, the Company's reserves available for distribution, calculated in accordance with the Companies Law, Cap. 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands, amounted to approximately HK\$61,310,000. This includes the Company's share premium account, in the capital amount of approximately HK\$53,296,000 as at 30 June 2004, which may be distributed provided that immediately following the date on which the dividend is proposed to be distributed, the Company will be in a position to pay off its debts as and when they fall due in the ordinary course of business. The share premium account may also be distributed in the form of fully paid bonus shares.

MAJOR CUSTOMERS AND SUPPLIERS

During the year under review, sales to the Group's five largest customers accounted for 30.6% of the total sales for the year and sales to the largest customer included therein amounted to 8.6%. Purchases from the Group's five largest suppliers accounted for 61.6% of the total purchases for the year and purchases from the largest supplier included therein amounted to 26.1%.

To the best knowledge of the directors, neither the directors, their associates, nor any shareholders who owned more than 5.0% of the Company's issued share capital, had any beneficial interest in the Group's five largest customers and/or five largest suppliers during the year.

DIRECTORS

The directors of the Company during the year and up to the date of this report were as follows:

Executive directors

Mr. Hung Kai So (*Chairman*)

Mr. Kam loi (*Managing director*)

Mr. Ma Yufeng

Ms. Sae-lao Rakchanok

Mr. Liu Jun

Mr. Lau Hin Hung

(resigned on 5 January 2004)

Mr. Lee Kwok Ming

(appointed on 5 January 2004)

Independent non-executive directors

Mr. Yuan Tsu I

Mr. Huang Ming Da

Mr. Yick Wing Fat, Simon

(appointed on 1 August 2004)

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DIRECTORS (Continued)

In accordance with article 86(3) of the articles of association of the Company, Mr. Lee Kwok Ming and Mr. Yick Wing Fat, Simon shall hold office only until the forthcoming annual general meeting of the Company and shall be eligible for re-election. These directors, being eligible, will offer themselves for re-election at the meeting.

In accordance with article 87(1) of the articles of association of the Company, Mr. Huang Ming Da will retire by rotation at the forthcoming annual general meeting of the Company. Mr. Huang Ming Da has indicated to the board of directors of the Company that he does not offer himself for re-election.

In accordance with article 87(2) of the articles of association of the Company, Ms. Sae-lao Rakchanok has informed the Company of her wish to retire at the forthcoming annual general meeting of the Company and does not offer herself for re-election.

DIRECTORS' AND SENIOR MANAGEMENT'S BIOGRAPHIES

Biographical details of the directors of the Company and the senior management of the Group are set out on pages 9 to 10 of the annual report.

DIRECTORS' SERVICE CONTRACTS

Each of the executive directors (other than Mr. Lee Kwok Ming) has entered into a director's service agreement with the Company for an initial term of two years commencing on 10 February 2003. The agreement will thereafter be automatically renewed for successive terms of one year each unless otherwise terminated in accordance with the terms of the relevant service agreement, or by either party to the service agreement giving to the other not less than six months' written notice expiring no earlier than the end of the initial term, or not less than three months' written notice during any renewed term.

Mr. Lee Kwok Ming has entered into a director's service agreement with the Company for an initial term of two years commencing on 5 January 2004. The agreement will thereafter be automatically renewed for successive terms of one year each unless otherwise terminated in accordance with the terms of the service agreement, or by either party to the service agreement giving to the other not less than six months' prior notice in writing at any time either during the initial term or anytime thereafter.

Each of the independent non-executive directors (other than Mr. Yick Wing Fat, Simon) has entered into a non-executive director's contract with the Company for an initial fixed period of one year commencing on 10 February 2003. The contract will continue thereafter for further successive periods of one year, provided that the Company may terminate the appointment at the end of each one-year period by giving to the director at least one month's written notice thereof.

The Company has not entered into service contract with Mr. Yick Wing Fat, Simon. He is not appointed for a specific term but is subject to retirement by rotation and re-election at the annual general meetings of the Company in accordance with the articles of association of the Company. Either the Company or he may terminate the appointment by giving at least one month's notice in writing.

Save as disclosed above, no director proposed for re-election at the forthcoming annual general meeting has a service contract with the Company which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

DIRECTORS' INTERESTS IN CONTRACTS

No director had a significant beneficial interest, either direct or indirect, in any contract of significance to the business of the Group to which the Company or any of its subsidiaries was a party during the year.

DIRECTORS' INTERESTS IN SECURITIES

As at 30 June 2004, the interests and short positions of the directors of the Company 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 (Chapter 571 of the Laws of Hong Kong) (the "SFO")) which are required to be notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they are taken or deemed to have under such provisions of the SFO), or are required, pursuant to section 352 of the SFO, to be entered in the register referred to therein, or are required to be notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies (the "Model Code"), were as follows:

Long positions in the shares and underlying shares of the Company

Name of director	Type of interest	Capacity	Number of shares held	Number of underlying shares held pursuant to share options	Aggregate interest	Approximate percentage of interest
Hung Kai So	Personal	Beneficial owner	130,131,229	1,600,000	131,731,229	19.42%
Kam loi	Personal	Beneficial owner	113,282,743	1,600,000	114,882,743	16.94%
Ma Yufeng	Corporate	Beneficial owner	44,467,115	—		
	(Note)					
	Personal	Beneficial owner	—	6,651,700	51,118,815	7.54%
Sae-lao Rakchanok	Personal	Beneficial owner	47,056,975	6,651,700	53,708,675	7.92%
Liu Jun	Personal	Beneficial owner	16,181,819	6,651,700	22,833,519	3.37%
Lee Kwok Ming	Personal	Beneficial owner	14,432,000	20,000,000	34,432,000	5.08%

Note: The 44,467,115 shares are held by Longway Group Ltd., a company incorporated in the British Virgin Islands and wholly-owned by Mr. Ma Yufeng.

Save as disclosed above, as at 30 June 2004, none of the directors of the Company had 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) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they were taken or deemed to have under such provisions of the SFO), or were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein, or were required to be notified to the Company and the Stock Exchange pursuant to the Model Code.

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DIRECTORS' RIGHTS TO ACQUIRE SHARES

Save as disclosed in the share option scheme disclosures in note 22 to the financial statements, at no time during the year was the Company or any of its subsidiaries a party to any arrangement to enable the directors of the Company to acquire benefits by means of acquisition of shares in, or debt securities including debentures of, the Company or any other body corporate and none of the directors or their spouses or children under the age of 18 had any right to subscribe for the securities of the Company, or had exercised any such right during the year.

SHARE OPTION SCHEME

Detailed disclosures relating to the Company's share option scheme are set out in note 22 to the financial statements.

Concerning the share options granted during the year to the directors, employees, suppliers and others as detailed in note 22 to the financial statements, the directors do not consider it appropriate to disclose a theoretical value of the options granted because a number of factors crucial for the valuation cannot be determined. Accordingly, any valuation of the options based on various speculative assumptions might not be meaningful, and could be misleading to the shareholders of the Company.

SUBSTANTIAL SHAREHOLDERS

Long positions in the shares and underlying shares of the Company

According to the records entered into the register required to be kept by the Company pursuant to section 336 of the SFO, so far as the directors of the Company are aware of and having made due enquiries, as at 30 June 2004, the interests and short positions of the persons (other than the directors of the Company) in the shares and underlying shares of the Company were as follows:

Name	Capacity	Number of shares held	Percentage of the Company's issued share capital
Martin Currie China Hedge Fund Limited	Beneficial owner	44,830,000 (Note)	6.61%
Martin Currie Investment Management Limited	Investment manager	44,830,000 (Note)	6.61%
UBS AG	Security interest	40,600,000	5.98%

Note: These shares refer to the same block of shares.

Save as disclosed above, as at 30 June 2004, no person, other than the directors of the Company whose interests are set out in the section "Directors' interests in securities" above, had an interest or a short position in the shares or underlying shares of the Company as recorded in the register required to be kept by the Company under section 336 of the SFO.

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DIRECTORS' INTERESTS IN COMPETING BUSINESS

During the year and up to the date of this report, none of the directors of the Company is interested in any business apart from the Group's business, which competes or is likely to compete, either directly or indirectly, with the business of the Group.

CORPORATE GOVERNANCE

In the opinion of the directors, the Company has complied with the Code of Best Practice (the "Code") as set out in Appendix 14 to the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules") throughout the year.

AUDIT COMMITTEE

The Company has established an audit committee in accordance with the requirements of the Code. The audit committee consists of three independent non-executive directors of the Company, namely Mr. Yick Wing Fat, Simon, Mr. Yuan Tsu I and Mr. Huang Ming Da, and Mr. Yick Wing Fat, Simon has been appointed as the chairman of the audit committee of the Company since 1 August 2004. The principal duties of the audit committee of the Company include the review of the completeness, accuracy and fairness of the Company's financial statements and the effectiveness of the Company's internal control system. During the year, two regular meetings of the audit committee have been held. The audited financial statements of the Company for the year ended 30 June 2004 have been reviewed by the audit committee.

MODEL CODE

During the year, the Company has adopted the Model Code as set out in Appendix 10 to the Listing Rules to govern purchase and sales of the Company's securities by the directors of the Company. The Company has also made enquiry in writing with each director as to whether he/she has complied with the Model Code. Each director replied to the Company in writing and confirmed that he/she has complied with the Model Code.

PUBLIC FLOAT

As far as the information publicly available to the Company is concerned and to the best knowledge of the directors of the Company, at least 25% of the Company's issued share capital were held by members of the public as at 3 September 2004 (being the latest practicable date prior to the printing of this annual report for the purpose of ascertaining the relevant information contained in this report).

INDEPENDENT NON-EXECUTIVE DIRECTORS

The Company has received from each of its independent non-executive directors the written confirmation of his independence pursuant to Rule 3.13 of the Listing Rules. The Company, based on such confirmation, considers Mr. Yuan Tsu I, Mr. Huang Ming Da and Mr. Yick Wing Fat, Simon to be independent.

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AUDITORS

The financial statements of the Company for the year ended 30 June 2004 were audited by Messrs. Grant Thornton. A resolution to re-appoint the retiring auditors, Messrs. Grant Thornton, will be put at the forthcoming annual general meeting of the Company.

Messrs. Ernst & Young tendered their resignation as auditors of the Company with effect from 2 July 2004 and Messrs. Grant Thornton were appointed as auditors of the Company to fill the casual vacancy created by the resignation of Messrs. Ernst & Young, by the shareholders of the Company at the extraordinary general meeting of the Company held on 30 July 2004.

The financial statements of the Company for the years ended 30 June 2002 and 2003 were audited by Messrs. Ernst & Young and there have been no other changes of the auditors of the Company in the past three years.

On behalf of the Board

Kam loi
Managing Director

Hong Kong, 25 August 2004