

Results

The Board of Directors (the “Board”) of Hualing Holdings Limited (the “Company”) announces the unaudited consolidated results of the Company and its subsidiaries (the “Group”) for the six months ended 30 June 2004 (the “Period”) as follows:

Condensed Consolidated Profit and Loss Account

		Six months ended 30 June	
		2004	2003
	Note	(Unaudited) HK\$'000	(Unaudited) HK\$'000
Turnover	2	1,199,522	909,857
Cost of sales		<u>(1,070,437)</u>	<u>(798,299)</u>
Gross profit		129,085	111,558
Other revenues	3	14,898	21,718
Distribution costs		(101,005)	(81,778)
Administrative expenses		(58,115)	(63,385)
Other operating expenses		<u>(5,019)</u>	<u>(732)</u>
Operating loss	4	(20,156)	(12,619)
Finance costs		(14,180)	(12,920)
Share of losses of associates		<u>(1,684)</u>	<u>(301)</u>
Loss before taxation		(36,020)	(25,840)
Taxation	5	<u>(2,117)</u>	<u>(1,307)</u>
Loss after taxation		(38,137)	(27,147)
Minority interests		<u>(6,488)</u>	<u>(452)</u>
Loss attributable to shareholders		<u><u>(44,625)</u></u>	<u><u>(27,599)</u></u>
Losses per share			
– basic	7	<u><u>(2.8) cents</u></u>	<u><u>(2.0) cents</u></u>
– diluted	7	<u><u>(2.8) cents</u></u>	<u><u>N/A</u></u>

Condensed Consolidated Balance Sheet

		30 June 2004 (Unaudited) HK\$'000	31 December 2003 (Audited) HK\$'000
	Note		
Non-current assets			
Property, plant and equipment		693,373	729,182
Other assets		56,067	41,110
		<u>749,440</u>	<u>770,292</u>
Current assets			
Inventories		516,670	549,900
Trade and other receivables	9	584,690	370,620
Prepaid value-added tax		33,127	61,839
Pledged bank deposit		198,067	128,059
Bank and cash balance		194,756	132,716
		<u>1,527,310</u>	<u>1,243,134</u>
Current Liabilities			
Trade and other payables	10	1,222,203	1,068,000
Tax payable		1,308	1,748
Short-term bank borrowings		581,044	510,637
		<u>1,804,555</u>	<u>1,580,385</u>
Net current liabilities		<u>(277,245)</u>	<u>(337,251)</u>
Total assets less current liabilities		<u>472,195</u>	<u>433,041</u>
Financed by:			
Share capital	11	158,204	138,204
Reserve		228,000	215,334
		<u>386,204</u>	<u>353,538</u>
Minority interests		57,840	51,352
Non-current liabilities			
Long-term bank borrowings		28,151	28,151
		<u>472,195</u>	<u>433,041</u>

Condensed Consolidated Cash Flow Statement

	Six months ended 30 June	
	2004 (Unaudited) HK\$'000	2003 (Unaudited) HK\$'000
Net cash inflow/(outflow) from operating activities	28,210	(6,119)
Net cash outflow from returns on investments and servicing of finance	(14,274)	(14,893)
Taxation paid	(9,465)	(58,205)
Net cash outflow from investing activities	<u>(20,100)</u>	<u>(11,773)</u>
Net cash outflow before financing	(15,629)	(90,990)
Net cash inflow from financing	<u>77,669</u>	<u>80,870</u>
Increase/(Decrease) in bank balance and cash	62,040	(10,120)
Bank balance and cash as at 1 January	<u>132,716</u>	<u>174,262</u>
Bank balance and cash as at 30 June	<u><u>194,756</u></u>	<u><u>164,142</u></u>

Consolidated Statement of Change in Equity

	Share Capital (unaudited) HK\$'000	Share Premium (unaudited) HK\$'000	General reserve fund (unaudited) HK\$'000	Enterprise expansion fund (unaudited) HK\$'000	Exchange reserves (unaudited) HK\$'000	Accumulated losses (unaudited) HK\$'000	Total (unaudited) HK\$'000
Balance as of 1 January 2003	138,188	509,383	37,361	16,958	28,339	(298,769)	431,460
Share of post-acquisition reserves			5				5
Currency translation difference					7		7
Net gain not recognised in the profit and loss account	138,188	509,383	37,366	16,958	28,346	(298,769)	431,472
Net loss for the period						(27,599)	(27,599)
Profit appropriation			6,947			(6,947)	-
Issue of share capital	16	18					34
Share issue expenses		(3)					(3)
Balance as of 30 June 2003	<u>138,204</u>	<u>509,398</u>	<u>44,313</u>	<u>16,958</u>	<u>28,346</u>	<u>(333,315)</u>	<u>403,904</u>
Balance as of 1 January 2004	138,204	509,398	37,361	16,958	27,362	(375,745)	353,538
Share of post-acquisition reserves							-
Currency translation difference					21		21
Net gain not recognised in the profit and loss account	138,204	509,398	37,361	16,958	27,383	(375,745)	353,559
Net loss for the period						(44,625)	(44,625)
Profit appropriation			610			(610)	-
Issue of share capital	20,000	60,000					80,000
share issue expenses		(2,730)					(2,730)
Balance as of 30 June 2004	<u>158,204</u>	<u>566,668</u>	<u>37,971</u>	<u>16,958</u>	<u>27,383</u>	<u>(420,980)</u>	<u>(386,204)</u>

Notes to Unaudited Condensed Financial Statements

1. Principal Accounting Policies and Basis of Preparation

These condensed consolidated interim financial statements (“interim financial statements”) are prepared in accordance with Statement of Standard Accounting Practice (“SSAP”) No. 25 “Interim Financial Reporting” issued by the Hong Kong Society of Accountants and with the applicable disclosure requirement of Appendix 16 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

These interim financial statements have not been audited by the Company’s auditors but have been reviewed by the Company’s Audit Committee.

The accounting policies and methods of computation used in the preparation of these condensed interim accounts are consistent with those used in the 2003 annual accounts.

2. Turnover and Segment Information

Substantially all turnover of the Group is attributable to the sales of household electrical appliances.

An analysis of the Group’s turnover and contribution to operating loss by products are summarized as follows:

	Turnover		Contribution to operating profit/(loss)	
	Six months ended		Six months ended	
	30 June 2004	30 June 2003	30 June 2004	30 June 2003
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
	HK\$’000	HK\$’000	HK\$’000	HK\$’000
Sales of refrigerators (Note 1)	164,477	186,439	(22,296)	(22,183)
Sales of air-conditioners (Note 2)	834,055	564,587	(4,575)	12,506
Sales of mini-refrigerators (Note 3)	200,990	158,831	14,738	2,253
Others	—	—	(8,023)	(5,195)
	<u>1,199,522</u>	<u>909,857</u>	<u>(20,156)</u>	<u>(12,619)</u>

Note 1: Analysis of sales of refrigerators into domestic sales in the PRC and export sales outside the PRC is as follows:

	Six months ended	
	30 June 2004 (Unaudited) HK\$'000	30 June 2003 (Unaudited) HK\$'000
Domestic sales in the PRC	128,273	163,178
Export sales outside the PRC		
Europe	24,857	11,001
America	119	259
Asia-Pacific	10,924	11,905
Africa	304	96
	<hr/>	<hr/>
Total export sales	36,204	23,261
	<hr/>	<hr/>
Total	<u>164,477</u>	<u>186,439</u>

Note 2: Analysis of sales of air-conditioners into domestic sales in the PRC and export sales outside the PRC is as follows:

	Six months ended	
	30 June 2004 (Unaudited) HK\$'000	30 June 2003 (Unaudited) HK\$'000
Domestic sales in the PRC	427,737	233,361
Export sales outside the PRC		
Europe	212,013	167,107
America	74,987	116,877
Asia-Pacific	56,536	46,563
Mid-east	61,024	—
Africa	1,758	679
	<hr/>	<hr/>
Total export sales	406,318	331,226
	<hr/>	<hr/>
Total	<u>834,055</u>	<u>564,587</u>

Note 3: Analysis of sales of mini-refrigerators into domestic sales in the PRC and export sales outside the PRC is as follows:

	Six months ended	
	30 June 2004 (Unaudited) HK\$'000	30 June 2003 (Unaudited) HK\$'000
Domestic sales in the PRC	42,512	54,201
Export sales outside the PRC		
Europe	53,883	6,961
America	60,221	44,184
Asia-Pacific	42,789	51,123
Africa	1,585	2,362
	<hr/>	<hr/>
Total export sales	158,478	104,630
	<hr/>	<hr/>
Total	<u>200,990</u>	<u>158,831</u>

3. Other Revenues

	Six months ended	
	30 June 2004 (Unaudited) HK\$'000	30 June 2003 (Unaudited) HK\$'000
Rental Income	2,002	4,016
Write-back of provision for obsolete stock	2,508	—
Write-back of provision for doubtful debts	—	8,900
Government subsidies	1,154	2,215
Sales of scrap material	6,872	5,362
Others	2,362	1,225
	<hr/>	<hr/>
	<u>14,898</u>	<u>21,718</u>

4. Operating Loss

	Six months ended	
	30 June 2004	30 June 2003
	(Unaudited)	(Unaudited)
	HK\$'000	HK\$'000

Operating loss is stated after charging the following:

Depreciation on fixed assets	34,762	36,452
Amortisation of goodwill	340	340
Interest on borrowings	15,859	17,465
	<u> </u>	<u> </u>

5. Taxation

No Hong Kong profits tax has been provided as the Group did not have any assessable income under Hong Kong Profit Tax. Overseas taxation has been calculated on the estimated assessable profit for the Period as the rate prevailing in the respective jurisdictions.

	For the Six months ended	
	30 June 2004	30 June 2003
	(Unaudited)	(Unaudited)
	HK\$'000	HK\$'000

PRC enterprise income tax	<u>2,117</u>	<u>1,307</u>
---------------------------	--------------	--------------

6. Interim Dividend

The directors do not recommend any payment of interim dividends for the Period (2003: nil).

7. Losses Per Share

The calculation of basic losses per share is based on the unaudited losses for the Period of HK\$44,625,000 (2003: HK\$27,599,000) and on the weighted average number of 1,568,849,595 shares (2003: 1,382,025,800 shares) in issue during the Period.

Diluted losses per share for the period is computed by number of 1,569,371,336 shares (2003: No diluted effect).

8. Investments in subsidiaries

Pursuant to a document (商資二批[2004]191號Shang Zi Er Pi [2004] No. 191) issued by 中華人民共和國商務部Ministry of Commerce of the PRC, 合肥華凌電器有限公司 Hefei Hualing Electrics Co., Ltd, an equity joint venture in which the Group has a 50.05% interest, has been converted into a joint stock limited company with effect from 28 February 2004.

9. Trade and Other Receivables

No specific credit term policy was adopted by the Group as the credit terms granted by the Group's varies towards different customers. The ageing analysis of trade receivables is as follows:

	30 June 2004 (Unaudited) HK\$'000	31 Dec 2003 (Audited) HK\$'000
within one year	400,090	226,552
over 1 year but within 2 years	7,130	14,750
over 2 years	5,647	5,647
	<u>412,867</u>	<u>246,949</u>

10. Trade and Other Payables

The ageing analysis of trade payables is as follows:

	30 June 2004 (Unaudited) HK\$'000	31 Dec 2003 (Audited) HK\$'000
within one year	634,524	543,774
over 1 year but within 2 years	24,391	18,628
over 2 years	5,741	2,254
	<u>664,656</u>	<u>564,656</u>

11. Share Capital

	30 June 2004 (Unaudited) HK\$'000	31 Dec 2003 (Audited) HK\$'000
--	---	--------------------------------------

Authorised:

3,000,000,000 Ordinary shares (as at 31 December 2003: 1,600,000,000 Ordinary shares) of HK\$0.1 each	300,000	160,000
---	---------	---------

Issued and fully paid:

1,582,036,408 (31 December 2003: 1,382,036,408) Ordinary shares of HK\$0.1 each	158,204	138,204
---	---------	---------

On 30 January 2004, Able Profit Investment Limited ("AP"), Profit Upsurge Limited ("PU"), a wholly owned subsidiary of AP, and the Company entered into a placing agreement with the placing agents, pursuant to which AP and PU have agreed to place or procure the placing through the placing agents of 80,000,000 placing shares and 120,000,000 placing shares respectively, to not less than six third-party investors, at a placing price of HK\$0.40 per placing share. At the same time, AP, PU and the Company entered into a subscription agreement, pursuant to which AP and PU have conditionally agreed to subscribe, or procure whom they may direct, to subscribe for 80,000,000 and 120,000,000 subscription shares respectively at a price of HK\$0.40 per subscription share.

The placing shares and the subscription shares represent approximately 14.47% of the share capital of the Company immediately before the subscription or approximately 12.64% of the issued share capital of the Company as enlarged by the subscription. The placing and the subscription were completed on 13 February 2004. The net proceeds from the subscription of approximately HK\$77,000,000 have been received by the Company.

The authorized share capital of the Company increases from HK\$160,000,000 to HK\$300,000,000 by the creation of an additional 1,400,000,000 new shares of HK\$0.10 each by passing of an ordinary resolution proposed at an Extraordinary General Meeting held on 29 June 2004.

12. Share Options

The share option scheme adopted by the Company on 26 November 1993 (“1993 Share Option Scheme”) expired on 25 November 2003. A new share option scheme (“2003 Share Option Scheme”) was approved by the shareholders at the Extraordinary General Meeting on 27 June 2003 and was adopted thereafter. 1993 Share Option Scheme was terminated immediately upon the adoption of 2003 Share Option Scheme. The options granted under 1993 Share Option Scheme will remain in force and effect.

There is no change in any terms of the 2003 Share Option Scheme during the six months ended 30 June 2004. The details terms of the scheme were disclosed in the 2003 annual accounts.

No option has been granted under the 2003 Share Option Scheme. No share option were exercised, cancelled or lapsed under the 1993 Share Option Scheme of the Company during the Period.

Movements of number of share options granted under the 1993 Share Option Scheme during the Period are as follows:

	Options				held at 30 Jun 2004	Exercise Price	Exercisable from	Exercisable until
	held as at 01 Jan 2004	grant during the Period	exercised during the Period	Lapsed/ cancelled during the Period				
Directors:								
Zhang Xin Hua	800,000	-	-	-	800,000	0.930	30 Sep 1997	30 Sep 2007
Lo Wing Sang, Vincent	2,000,000	-	-	-	2,000,000	0.244	17 Feb 2000	17 Feb 2010
	1,000,000	-	-	-	1,000,000	0.211	05 Jul 2000	04 Jul 2010
Chan Wai Dune	2,000,000	-	-	-	2,000,000	0.244	17 Feb 2000	17 Feb 2010
	1,000,000	-	-	-	1,000,000	0.211	05 Jul 2000	04 Jul 2010
Employees	160,000	-	-	-	160,000	0.211	05 Jul 2000	04 Jul 2010
	<u>6,960,000</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6,960,000</u>			

The share options are exercisable over a period of ten years from the date of granting the options.

13. Related Parties Transactions

Companies are considered to be related if one company has the ability, directly or indirectly, to control the other company or exercise significant influence over the other company in making financial and operating decisions. Companies are also considered to be related if they are subject to common control or common significant influence.

The Group had the following material transactions with related parties during the Period, which the directors considered were in the normal course of business and under normal commercial terms:

	Six months ended	
	30 June 2004 (Unaudited) HK\$'000	30 June 2003 (Unaudited) HK\$'000
Purchase from Guangzhou Hualing Polyfoam Co., Ltd	3,241	2,269
Purchase from and processing charges paid to Yunggang Plastic Co., Ltd	–	2,783
Rental paid to Guangzhou Baiyun Mechanical Industrial Corporation	1,234	1,189
	<u>4,475</u>	<u>6,241</u>

14. Banking Facilities and Pledge of Assets

As at 30 June 2004, the Group had banking facilities of approximately HK\$921,460,000 (as at 31 December 2003: approximately HK\$843,210,000) for overdrafts, bank borrowings and trade financing. As at that date, approximately HK\$797,390,000 (as at 31 December 2003: approximately HK\$690,958,000) was utilized. Property, plant and equipment with net book value of approximately HK\$390,033,000 as at 31 December 2003: HK\$245,975,000) were pledged as security for the Group's short-term bank loans.

15. Capital Commitment

As at 30 June 2004, the Group had authorized and contracted capital commitments in relation to purchase of fixed assets of approximately HK\$17,196,000 (as at 31 December 2003: approximately HK\$4,140,000).

16. Contingent Liabilities

As at 30 June 2004, the balance of discounted letters of credit with recourse of the Group was amounted to approximately HK\$39,458,000 (as at 31 December 2003: approximately HK\$26,260,000), and there was no bill of exchange discounted/endorsed with recourse (as at 31 December 2003: approximately HK\$1,385,000).

FINANCIAL PERFORMANCE

The Group's sales volume for the period ended 30 June 2004 was approximately 35% increase from the same period last year. Turnover reached approximately HK\$1,199,522,000, representing an approximately 32% increase over the same period last year (2003: HK\$909,857,000). The Group recorded an operating loss of approximately HK\$20,156,000 (2003: HK\$12,619,000). Loss attributable to shareholders was approximately HK\$44,625,000 (2003: HK\$27,599,000). As at 30 June 2004, cash on hand was approximately HK\$194,756,000. The bank borrowings of the Group amounted to approximately HK\$609,195,000, including short-term bank loans of approximately HK\$581,044,000. As at the period end, the debt to equity ratio, calculation based on total of short-term and long-term loans against consolidated shareholders' equity was about 1.6 (as at 31 December 2003: 1.5).

INTERIM DIVIDEND

The Board has resolved not to pay any interim dividend for the period ended 30 June 2004 (2003: nil).

INDUSTRY OVERVIEW

Like all kinds of industries, household appliance enterprises also opt for the strategy of globalization development. PRC is currently one of the most important production bases and exporting countries for household appliances in the world with an export value up to US\$12.58 billion, among which the total export of air-conditioners amounted to 16,438,800 units, representing one fold increase from last year. The export amount of the refrigerators was 8,807,300 units, jumping 44.3%. Approaching the gradual liberation of World Trade, the PRC, as a world factory is further consolidated. It is anticipated that the export market of household appliances in the PRC has a huge potential for development. Simultaneously, with a growing living standard of Chinese people, the household appliances such as air-conditioners have become necessities from luxuries. All these favorable factors created a promising operational environment for household appliance enterprises in the PRC.

Reviewing the first half of this year, the Central Government introduced a series of macroeconomics adjustment and control measures in order to suppress the surging price of raw materials. But the surging prices of major raw materials like steel, copper and plastic during the first half of this year, and adjustment of export tax rebate led to the rise in production cost and the subsequent severe impact on the profit margin of household appliance products. The elimination of market competitors over the past few years signified a better competition environment for the air-conditioner industry.

BUSINESS REVIEW

Faced with the complicated economic environment such as surging price of raw materials in the PRC, continuously decreasing market prices of products and change of export tax rebate policy, the Group adopted prudent operational strategies and aggressive development measures. The Group achieved remarkable results in areas like business management, sales and marketing, product development, quality control, brand building and information management, maintaining a stable and healthy business performance with a promising growth in both domestic and export markets.

Under the review period, the total sales volume of the Group's products reached 1,202,200 units, representing a 35% increase over the same period last year. Among the total sales volume, 503,000 units and 699,200 units were sold for PRC consumption and export sales, a 35% and 37% increase respectively from the same period last year.

To further generate revenue and minimize expenditure, the Group introduced the cost control in product development, procurement of raw materials and manufacturing process, particularly the cost control over the procurement of raw materials and the introduction of a bidding system and made allies with strategic partners. All measures of cost control achieved an effective result.

Both air-conditioners and refrigerators recorded a significant growth of overall sales volume over the same period last year, among which the total sales volume of air-conditioners amounted to 663,500 units while that of refrigerators amounted to 538,700 units, a 49% and 21% increase respectively over the same period last year. In particular, for the air-conditioners, there were around 20 major brands distributed throughout all major channels in the PRC market in which about one-half was domestic brands. With such an extremely fierce competition in the industry, the warfare for market share among different brands was keen, the sales volume of the Group's air-conditioners in the PRC market still recorded a 87% growth over the same period last year.

Air-conditioner Business Analysis

During the period under review, the total sales volume of air-conditioners amounted to approximately 663,500 units, a 49% growth from the same period last year. Turnover of air-conditioners amounted to approximately HK\$834,055,000 during the period under review, a 48% period-on-period growth.

Regarding the sales distribution of air-conditioning products, sales of window-type air-conditioners accounted for approximately 22% of the total sales volume, a decrease of approximately 19% compared to 41% of last year. Corresponding figures for cabinet-type and split-type air-conditioners were 6% and 72%. Cabinet-type air-conditioners maintained the same level compared with the same period last year whereas split-type air-conditioners represented an increase of approximately 18%.

Overseas Export Market

The Group's air-conditioner export business continued to maintain a rapid growth. The export volume was approximately 359,200 units during the period under review, increased by approximately 27%. Turnover of export sales reached approximately US\$52.09 million, which accounted for approximately 49% of the total sales of air-conditioners. The Group's export volume of air-conditioners to North America and Europe remained stable. Export volume to Europe increased by about 27% over the corresponding period last year. The Group also actively explored the emerging markets such as the Middle East and the export sales to the Middle East amounted to US\$7.82 million.

The Directors believe, with its established international brand name and strength, the development of overseas export business will be promising.

The PRC Market

Though with the effect of a drop in sales price resulted from market competition, the withdrawal of some competitors created a better operational environment and an upsurge of the cost of raw materials, leading to an upturn in sales price during the middle of the year. The sales volume amounted to approximately 304,300 units, increased by 87% when compared to the same period of last year. The turnover increased by approximately 83% and amounted to approximately HK\$427,737,000. Split-type air-conditioners accounted for approximately 85% of the total sales volume in the PRC market and shared the largest portion among other segments.



The Directors believe, under the new mode of sales and marketing management and olive-scale marketing management structure, the market reflection rate of the overall sales and marketing system can be greatly enhanced with an operation of following closer to market, contributing a more satisfactory performance in the PRC market exploration.

Refrigerator Business Analysis

During the period under review, the Group's refrigerator sales volume increased by approximately 21% compared to the corresponding period last year, amounted to approximately 538,700 units. Turnover amounted to approximately HK\$365,467,000, representing an increase of approximately 6% over the same period last year. Among them, refrigerator and mini-refrigerator business amounted to 170,900 units and 367,800 units, accounted for 32% and 68% of the total sales volume, representing a 5% drop and 38% growth over the same period last year, respectively.

During the period under review, Hefei Hualing Electrics Co Ltd, the Group's subsidiary which is the major production base of mini-refrigerators, has been converted from an equity joint venture into a joint stock limited company.

The Directors believe, the refrigerator business in the PRC will be upgraded from low-end frozen refrigerators to high-end frozen-free refrigerators. The Group has speed up the consolidation of foundation of frozen-free production. In September 2004, China Refrigeration Industry Co., Ltd ("China Refrigeration") in which the Group has 95% interest, acquired the land use right of two pieces of land among which the land use right of No.8, Tongbao Road in Baiyun District, Guangzhou which is the existing production base, offices and inventories of China Refrigeration as well as land use right of the land and buildings situated at No.10 Tonghe North Road at a consideration of RMB54.3 million. The Group believes that this acquisition ensures the continuity and possibility of future expansion for China Refrigeration and thus is the best interests of the Company and shareholders as a whole.

Overseas Export Market

During the period under review, the export sales volume of the Group's refrigerators was satisfactory, with export volume surged 50% to approximately 340,000 units. Among which, refrigerators and mini-refrigerators amounted to 38,000 units and 302,000 units respectively. Total turnover increased approximately 52% to approximately HK\$194,682,000.

The PRC Market

During the period under review, the sales volume of refrigerators in the PRC dropped 10% compared to the corresponding period last year, reached approximately 198,700 units. Turnover decreased by approximately 21% and amounted to approximately HK\$170,785,000.

The Directors consider that the drop in the sales volume of refrigerators is mainly due to the 20% substantial price reduction of similar models of other producers, affecting the sales volume.

OVERALL BUSINESS ANALYSIS OF THE GROUP

Business Management

The Group reformed the internal management system and the implementation of operation accountable system in the refrigerator company and achieved a satisfactory result. After the introduction of the innovative management system, the Group's management and all staff achieved higher operation efficiency, leading to better cost control of different departments and further enhancing productivity. The Group also dedicated to improving the management quality of Hualing air-conditioning business. The "production, logistics and procurement management and regulation plan" was devised and implemented during the period under review. The Group strictly followed the management objectives of "tapping new sources of revenue and cutting down expenditures, attaining clear and definite responsibility, implementing resolute practice and executing reward and punishment".

Sales and Marketing

During the review period, while consolidating relationship with existing customers, the Group also actively explored new markets. By using marketing strategies, integrated marketing communications, market segmentation and highly selected media etc, the Group kicked off promotion campaigns for different products in the major cities in the PRC like Chongqing, Sichuan, Zhejiang and Hunan.

To ensure the momentum of sales growth, the Group will actively form a strategic alliance with distributors in the PRC so as to increase the operational efficiency of marketing network. After providing Suning electrical appliance chain stores with 150,000 units of air-conditioners, the Group entered into a pact with the largest retail chain enterprise in the PRC, GOME, underwrote 100,000 units of air conditioners with an aggregate value of RMB220 million.



Product Research and Development (“R&D”)

To satisfy different market needs, 2 different ranked air-conditioners with more than 50 products were launched in the PRC, among which the V series split-type and P series cabinet-type air-conditioners with characteristics of small scale and low cost, have become the new focus in the household electrical appliance market. Y series split-type and H series cabinet-type air-conditioners, with their highly effective, multi-functional, healthy, gorgeous and refined appearance, manifest the high quality image of Hualing. They not only built the brand image, but also are major models that generate profits. Development of the new models for exports was responded to the important customers from the regions in Europe and North America. With the quality assurance, the Group also implemented a strategy of product differentiation and fully utilized the technological edge.

The new product of refrigerator business is designed on the theme of “Healthy, Energy saving”. On the basis of Mitsubishi Vitamin Fresh-Retaining Technology (「三菱維他命保鮮技術」), a new image of a professional and healthy product was established.

In addition, the Group is undergoing technological cooperation with a major U.S. company in the refrigerant industry, which jointly developed the most globally advanced CRV digital central air-conditioners. It helped enhance the R&D ability and product quality of the Group.

Quality Control

During the period under review, the quality of the Group’s products maintained a stable level of high standard and has been waiting for the proclamation of assessment results after completing the application for accreditation of three national brand names. Among them are “China Famous Brands”, currently the most authoritative and the greatest honor for product brand in the PRC, in September has already been awarded to the Group’s air-conditioners and refrigerators, “China Famous Goods for Export”, the only national honor for export product brand, and “Product Exemption from Quality Surveillance Inspection”, the authoritative certification for quality of product brand by the highest state authority for inspection of product quality. All of these honors significantly increase the reputation of the Group’s products.

Besides, the Group was awarded “Quality and Efficient Advanced Enterprise in Guangdong Province” and the “Three Satisfaction” title for users of the provinces. (Satisfactory products for provincial users, Satisfactory enterprise for provincial users and Satisfactory service for provincial users).

Information System Management

The Group, during the period, continued to promote the information establishment and strengthened the existing information system to enhance the operating efficiency. During the period under review, SAP system recorded an output of 638,000 units, a 22.5% increase from the same period last year. Among them, a historic record high of monthly output reached 150,000 units in the months of May and June, making a record of average daily output of 5,000 units.

The reform of production management mode not only laid a solid foundation for the completion of the production task this year, but also satisfied the needs of sales growth, reinforcing the Group's confidence in completing the higher production goal in 2005.

Prospects

Due to the fierce competition from other large scale household appliance enterprises in the PRC, and the remaining higher cost of raw materials, the Group continues to increase the sales volume and to maintain a stringent cost control. Under such operating environment, leveraging on the existing dominance and various patent technologies, the Group, being market-oriented and profit-concerned, will adopt the innovative management concepts for business expansion.

Residential construction industry remained a steady growth over last three years. The market volume of mini-central air-conditioners recorded one-fold increase every year on average. According to statistics, the market volume of mini-central air-conditioners reached RMB5.5 billion in 2003 and is expected to rise to RMB10 billion in 2006. In 2010, the growth may reach a range from RMB15 billion to RMB20 billion. The Group expects the prospect for the mini-central air-conditioner is bright.

Maintaining its product design, the Group will strengthen the "generalization" and "standardization" of the products. With two production lines in the PRC and overseas as a research and development platform, profit analysis and investment forecast on both export and domestic models will be conducted via cost of raw materials, market price, sales volume and moulding cost in order to achieve the goals of production efficiency enhancement and of manufacturing cost reduction.

EMPLOYMENT, TRAINING, DEVELOPMENT AND REMUNERATION POLICY

As at 30 June 2004, the Group employed approximately 3,900 staff, of which 11 are stationed in Hong Kong. The Group remunerates its employees based on their performance, experience and prevailing industry practice. The Group has set up a share option scheme and provides retirement benefits, in the form of Mandatory Provident Fund etc. and other benefits, which are similar to the employees in the PRC. The Group will also grant bonus and other kinds of remuneration according to individual performance and the performance of the Group's overall profit.

LIQUIDITY AND CAPITAL RESOURCES

The Group generally financed its operations with cash flow generated internally and facilities provided by banks in the PRC.

DIRECTORS' AND CHIEF EXECUTIVE INTERESTS IN EQUITY AND DEBT SECURITIES

As at 30 June 2004, none of the director or chief executive of the Company was interested in the equity and debt securities of the Company or any associated corporation (within the meaning of the Securities and Futures Ordinance ("SFO")). The interests of each director and chief executive in the options of the Company and its associated corporations (within the meaning of the SFO), as recorded in the register maintained by the Company under Section 352 of the SFO Ordinance or as notified to the Company were as follows:

		Options		
		As at 1 January 2004	Exercise	As at 30 June 2004
ZHANG Xin Hua	Long positions	800,000	–	800,000
LO Wing Sang Vincent	Long positions	3,000,000	–	3,000,000
CHAN Wai Dune	Long positions	3,000,000	–	3,000,000

Share options are granted to directors under the 1993 Share Option Scheme. Summary of the scheme and movement of share options held by the Company's directors during the Period are set out in Note 12 to the Unaudited Condensed Financial Statements.

Other than those interests disclosed above, at no time during the Period, the directors and chief executives (including their spouse and children under 18 years of age) had any interest in, or had been granted, or exercised, any rights to subscribe for shares of the Company and its associated corporations (within the meaning of the SFO).

Other than those interests disclosed above, at no time during the Period was the Company, its subsidiaries, its associated companies, its fellow subsidiaries or its holding company, a party to any arrangements to enable the directors and chief executives of the Company to hold any interests or short positions in the shares in, or debentures of, the Company or its associated corporations.

SUBSTANTIAL SHAREHOLDERS' INTERESTS

The register of substantial shareholders maintained under Section 336 of the SFO shows that as at 30 June 2004, the Company had been notified of the following substantial shareholders' interests, being 5% or more of the Company's issued share capital. These interests are in addition to those disclosed above in respect of the directors.

Name of Shareholder		Number of shares held	Percentage of shareholding
Guangzhou International Group Co., Limited ("GIG")*	Long positions	670,076,808 **	42.4%
Able Profit Investment Limited*	Long positions	670,076,808 **	42.4%
Guangzhou Baiyun Agriculture Industry & Commerce Corporation	Long positions	162,960,000	10.3%

* As part of the reorganization of Guangzhou Municipal Government ("GMG"), the aggregate shares of the Company held by Guangzhou International Trust & Investment Corporation ("GZITIC") were transferred to Able Profit Investment Co., Limited ("AP") ("the Transfer"). After the Transfer, AP's immediate holdings company, GIG, will be the largest shareholder of the Company. The Company was informed by GZITIC and GIG on 29 May 2003 that the Transfer had been completed by 29 May 2003.

** 670,076,808 shares were pledged as share mortgage in exchange of a loan facility of US\$20,000,000 to GIG and were registered under the name of Bright Asia Assets Ltd., as nominee shareholder of the lender.



PURCHASE, SALES AND REDEMPTION OF SECURITIES

The Company has not redeemed any of its shares during the Period. Neither the Company nor any of its subsidiaries has purchased or sold any of the Company's shares during the Period.

AUDIT COMMITTEE

The Audit Committee has reviewed with management the accounting principles and practices adopted by the Group and discussed internal controls and financial reporting matters including a review of the unaudited condensed accounts for the six months ended 30 June 2004 with the directors.

COMPLIANCE WITH THE CODE OF BEST PRACTICE OF THE LISTING RULES

Throughout the Period, the Company was in compliance with the Code of Best Practice as set out in the Listing Rules except that no independent non-executive directors are appointed for a specific term as they are subject to retirement by rotation and re-election at the Annual General Meeting of the Company in accordance with the provisions of the Company's Articles of Association.

By Order of the Board
LI YU JUN
Chairman

Hong Kong, 21 September, 2004