

On behalf of the board of directors ("Board") of Shanghai Merchants Holdings Limited (the "Company"), I am pleased to present to the shareholders the results of the Company and its subsidiaries (the "Group") for the year ended 31 December 2005.

## MANAGEMENT DISCUSSION AND ANALYSIS

### Business Review

Turnover of the Group for the year ended 31 December 2005 was approximately HK\$68,393,000 (2004: HK\$22,305,000), which was up 207% from that of last year.

Profit of HK\$6,501,000 was recorded for the current year, as compared to a loss of HK\$36,299,000 in 2004.

### *Trading in base metals*

Turnover for this sector for the year was approximately HK\$44,937,000 (2004: HK\$13,522,000). A growth of 232% was recorded as compared with last year. Following the resumption of the base metals trading business in last year, the Group has scaled up its operation in this sector in the year 2005. The base metals trading business segment contributed HK\$110,000 (2004: HK\$121,000) to the Group's operating profits which represented a drop of 9%.

### *Trading in fabric products and other merchandises*

The Group's turnover for fabric products and other merchandises trading business segment reached HK\$23,456,000 during the year (2004: HK\$8,783,000), an increase of 167% over that of 2004. Segment profit attributable to the Group during the year amounted to HK\$966,000 (2004: HK\$393,000), an increase of 146% as compared with 2004. The Group's management has been taking active actions to expand the operations under the constraints of available working capital.

### Business Outlook

With a view to expanding the Group's business operations and enhancing its financial performance, the Group and its controlling shareholder, Profit Harbour Investments Limited ("Profit Harbour"), entered into a deed of assignment on 12 April 2006. Pursuant to which Profit Harbour has conditionally agreed to acquire from the Group its receivable due from Great Center Limited of US\$4.5 million (approximately HK\$35.1 million) in full at its face value. The assignment of debt is conditional upon the approval by the independent shareholders at the forthcoming special general meeting.

The Company proposes to raise approximately HK\$82.6 million before expenses by way of a rights issue.

During the year ended 31 December 2005, the Company entered into a heads of terms with the shareholders of an acquisition target in the PRC, which is engaged in the trading of electronic component business, to acquire their interests in the entire issued share capital of the target at a consideration which will be settled by issuance of convertible bonds by the Company. The Board considers that the proposed acquisition will keep the Company abreast of the lucrative growth opportunities that the PRC market presents, thereby strengthening the Company's ability to meet the rising demand from its customers.

### DIVIDEND

The Board does not recommend the payment of a dividend for the year ended 31 December 2005 (2004: Nil).

### LITIGATION AND CONTINGENT LIABILITIES

Details of the material litigation and contingent liabilities are set out in note 24 to the financial statements.

## **PLEDGE OF ASSETS**

Details of the pledge of assets are set out in note 25 to the financial statements.

## **LIQUIDITY AND FINANCIAL RESOURCES**

As at 31 December 2005, the Group had secured other loans of HK\$15 million (2004: HK\$15 million), and bank balances and cash were at approximately HK\$5,477,000 (2004: HK\$14,929,000).

## **FOREIGN EXCHANGE EXPOSURE**

Since most business transactions conducted by the Group and payments made to suppliers are either in Hong Kong Dollars, or US Dollars, no use of financial instruments for hedging purposes is considered necessary.

## **EMPLOYEES AND REMUNERATION POLICY**

As at 31 December 2005, the Group had 3 (2004: 5) managerial, administrative and trading staff in Hong Kong.

The Group remunerates its employees largely based on the prevailing industry practice.

## **APPRECIATION**

The operating result of the Group is achieved due to the support of our shareholders and business partners, the commitment of the directors and the dedication of all our staff members. On behalf of the Board, I would like to take this opportunity to extend my sincere appreciation for their contributions and endeavor.

On behalf of the Board

Yue Jialin  
*Chairman*

Hong Kong, 24 April 2006