

The directors of Stone Group Holdings Limited (the "Company", together with its subsidiaries, the "Group") have pleasure in submitting their annual report together with the audited financial statements for the year ended 31 March 2006 (the "Year").

PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding. The principal activities and other particulars of its principal subsidiaries are set out in note 47 on the financial statements.

The Group's turnover is derived principally from the manufacture, distribution and sale of healthcare products, electronic and electrical products, office equipment and the provision of related services, and the operation of media-related business.

The Group operates primarily in the People's Republic of China (the "PRC") where its existing manufacturing facilities and distribution network are based. The Group's activities in Hong Kong include the sourcing of electronic and electrical products, office equipment and component parts for processing, distribution and sale in the PRC.

SEGMENTAL INFORMATION

An analysis of the Group's turnover and contributions from operations by business segments for the Year is set out in note 15 on the financial statements. No analysis of the Group's turnover and contributions from operations by geographical segment has been presented as almost all the Group's operating activities are carried out in the PRC.

MAJOR CUSTOMERS AND SUPPLIERS

For the Year, the five largest customers in aggregate accounted for less than 30% of the Group's turnover. The five largest suppliers in aggregate and the largest supplier of the Group accounted for approximately 65% (period ended 31 March 2005: 75%) and 28% (period ended 31 March 2005: 37%) respectively by value of the Group's total purchases.

At no time during the Year have the directors of the Company, their associates or any shareholder of the Company (which to the knowledge of the directors of the Company owns more than 5% of the Company's share capital) had any interests in such major customers and suppliers.

RESULTS AND APPROPRIATIONS

The results of the Group for the Year and the state of the Company's and the Group's affairs as at 31 March 2006 are set out in this annual report on pages 36 to 134.

No interim dividend was paid during the Year (period ended 31 March 2005: Nil). The directors of the Company recommend the payment of a final dividend of HK0.8 cent per share for the Year (period ended 31 March 2005: HK1.3 cents per share) to the shareholders whose names appear on the register of members of the Company on 29 August 2006.

SHARE CAPITAL

Details of the Company's share capital are set out in note 34 on the financial statements.

TRANSFER TO RESERVES

Profits attributable to equity shareholders of the Company of HK\$63,908,000 (period ended 31 March 2005: HK\$160,426,000) have been transferred to reserves. Other movements in reserves are set out in note 35 on the financial statements.

PROPERTY, PLANT AND EQUIPMENT

Movements in property, plant and equipment during the Year are set out in note 17 on the financial statements.

BANK LOANS AND OTHER BORROWINGS

Particulars of bank loans and other borrowings of the Group as at 31 March 2006 are set out in notes 29 and 30 on the financial statements.

FIVE YEAR FINANCIAL SUMMARY

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on page 135.

CONVERTIBLE SECURITIES, OPTIONS, WARRANTS OR SIMILAR RIGHTS

Save as disclosed in the sections entitled "Directors' Interests in Shares, Underlying Shares and Debentures", "Share Option Scheme" and "Substantial Interests in the Share Capital of the Company" below and save for the particulars of convertible notes of the Group as at 31 March 2006 set out in note 32 on the financial statements, the Company had no other outstanding options, convertible securities, warrants or other similar rights as at 31 March 2006 and there were no other repurchases or exercises of options and convertible securities during the Year.

DIRECTORS

The directors of the Company during the Year and up to the date of this report were:

Executive directors

DUAN Yongji (*Chairman*)

SHI Yuzhu (*Chief Executive Officer*)

SHEN Guojun

ZHANG Disheng

CHEN Xiaotao

LIU Wei

Independent non-executive directors

NG Ming Wah, Charles

Andrew Y. YAN

LIU Ji (appointed on 20 May 2005)

YUAN Zhenyu (resigned on 20 May 2005)

LIU Jipeng (appointed on 18 April 2006)

In accordance with article 101 of the Company's articles of association, Mr. Chen Xiaotao, Mr. Zhang Disheng, Ms. Liu Wei and Mr. Andrew Y. Yan retire from office by rotation at the forthcoming annual general meeting and being eligible, offer themselves for re-election.

In accordance with article 92 of the Company's articles of association, Mr. Liu Jipeng retires from office at the forthcoming annual general meeting and being eligible, offers himself for re-election.

DIRECTORS' SERVICE CONTRACTS

No director of the Company proposed for re-election at the forthcoming annual general meeting has an unexpired service contract which is not determinable by the Company or any of its subsidiaries within one year without payment of compensation, other than normal statutory obligations.

DIRECTORS' INTERESTS IN SHARES, UNDERLYING SHARES AND DEBENTURES

The directors of the Company who held office at 31 March 2006 had the following interests in the shares, underlying shares and debentures of the Company or its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) at that date as recorded in the register of directors' and chief executive's interests and short positions required to be kept under section 352 of the SFO:

Long positions in the shares and underlying shares of the Company:

Name of director	Nature of interests	Number of shares	Interest in underlying shares pursuant to share options	Interest in underlying shares pursuant to convertible notes	Aggregate interests	Approximate shareholding percentage (Note 3)
Duan Yongji	Personal (Note 1)	45,075,538	3,900,000	182,692,305	231,667,843	15.35
Shen Guojun	Personal (Note 1)	–	4,000,000	–	4,000,000	0.27
Chen Xiaotao	Personal (Note 1)	–	8,000,000	–	8,000,000	0.53
Zhang Disheng	Personal (Note 1)	–	10,400,000	–	10,400,000	0.69
Shi Yuzhu	Corporate (Note 2)	–	–	492,105,264	492,105,264	32.61

- Notes: (1) Beijing Stone Investment Company Limited together with its associates (as defined in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules")) holds a total of 407,110,053 shares in the Company. Beijing Stone Investment Company Limited is owned as to 42.3% by Stone Jiu Guang New Technology Development (Holdings) Co. Ltd., 6.7% by Stone Group Corporation ("SGC") and 51% by the Beijing Stone Investment Company Limited Employees' Shareholding Society. In addition, SGC indirectly holds 92,374,413 shares in the Company and directly holds 1,062,000 shares in the Company. Messrs. Duan Yongji, Shen Guojun, Chen Xiaotao and Zhang Disheng (collectively as the "said Directors") are also directors of SGC. So long as the said Directors remain as directors of SGC, each of them together with the other employees collectively own interests in the assets of SGC but none of them has any specific interests in SGC.
- (2) The interest is held by Ready Finance Limited ("Ready Finance") as beneficial owner. Ready Finance is wholly owned by Mr. Shi Yuzhu who is deemed under the SFO to be interested in the underlying shares held by Ready Finance.
- (3) The number of issued ordinary shares of the Company as at 31 March 2006 ("31 March 2006 Issued Share Capital") is 1,508,913,889 and is applied to calculate the relevant percentage.

DIRECTORS' INTERESTS IN SHARES, UNDERLYING SHARES AND DEBENTURES *(Continued)*

Save as disclosed herein and in the sections entitled "Share Option Scheme" and "Substantial Interests in the Share Capital of the Company" set out below, none of the directors and the chief executive of the Company had any interests or short positions in the shares, underlying shares or debentures of the Company or its associated corporations, as recorded in the register required to be kept under section 352 of the SFO or as otherwise notified to the Company pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers set out in Appendix 10 of the Listing Rules.

DIRECTORS' INTERESTS IN CONTRACTS

Save for the Repurchase Agreement (as defined below) disclosed in the section entitled "Connected Transactions", no contracts of significance to which the Company, any of its holding companies, subsidiaries or fellow subsidiaries was a party and in which a director of the Company had a material interest, subsisted at the end of the Year or at any time during the Year.

SHARE OPTION SCHEME

The Company has adopted a share option scheme on 12 April 2002 (the "Scheme"). The purpose of the Scheme is to encourage the participants to perform their best in achieving the goals of the Group and at the same time allow the participants to enjoy the results of the Company attained through their effort and contribution. Participants include any employee and director of the Company or any of its subsidiaries or associated companies as absolutely determined by the directors of the Company.

The directors of the Company may, at their discretion, invite any participant to take up options. An option is deemed to have been accepted by the grantee upon his or her signing the duplicate letter comprising acceptance of the option and paying HK\$1 by way of consideration for the grant thereof.

The subscription price for shares in the Company under the Scheme will be the highest of (i) the closing price of the shares of the Company as stated in the daily quotations sheet of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") on the date on which the option is offered, which date must be a business day, (ii) a price being the average of the closing prices of the shares of the Company as stated in the Stock Exchange's daily quotations sheets for the five business days immediately preceding the date of the option being offered, and (iii) the nominal value of a share of the Company.

The total number of shares of the Company which may be issued upon exercise of all options to be granted under the Scheme and any other share option schemes of the Company must not in aggregate exceed 10% of the total number of shares of the Company in issue as at the date of approval of the Scheme. The Company may seek approval of its shareholders in general meeting to renew the said 10% limit such that the total number of shares in respect of options that may be granted under the Scheme or any other share option schemes of the Company shall not exceed 10% of the total number of shares of the Company in issue as at the date of approval to renew the limit. Notwithstanding the above, the maximum number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the Scheme and any other share option schemes of the Company shall not exceed 30% of the total number of shares of the Company in issue from time to time.

SHARE OPTION SCHEME *(Continued)*

The maximum entitlement for any one participant is that the total number of shares issued and to be issued upon exercise of the options granted to each participant (including exercised or outstanding options) in any 12-month period must not exceed 1% of the total number of shares of the Company in issue. Any further grant of options in excess of the said 1% limit shall be subject to shareholders' approval in general meeting with such participant and his or her associates abstaining from voting. An option may be exercised during a period to be determined by the directors of the Company in their absolute discretion and in any event such period shall not be longer than 10 years after the date of the grant of the option. The Scheme will remain in force for a period of 10 years from 12 April 2002.

The total number of shares available for issue under the Scheme as at 31 March 2006 was 191,312,000 shares, which represented 12.68% of 31 March 2006 Issued Share Capital. The minimum period (if any) for which an option must be held before it can be exercised is at the discretion of the directors of the Company and is set out in the table below.

Each option gives the holder the right to subscribe for one share in the Company. At 31 March 2006, the directors and employees of the Group had the following interests in options to subscribe for shares of the Company:

	Number of options				Date of grant	Exercisable period	Exercise price HK\$	% of the total issued shares (Note f)
	Outstanding at 1.4.2005	Exercised during the Year	Lapsed during the Year	Outstanding at 31.3.2006				
Duan Yongji (Note a)	3,900,000	–	–	3,900,000	22-05-2002	22-08-2002 to 21-05-2012	0.792	0.26
Shen Guojun (Note a)	4,000,000	–	–	4,000,000	22-05-2002	22-08-2002 to 21-05-2012	0.792	0.27
Chen Xiaotao (Note b)	8,000,000	–	–	8,000,000	22-05-2002	22-05-2002 to 21-05-2012	0.792	0.53
Zhang Disheng (Note c)	10,400,000	–	–	10,400,000	22-05-2002	22-05-2002 to 21-05-2012	0.792	0.69
Contracted employees (Note d)	55,156,000	–	–	55,156,000	22-05-2002	22-05-2002 to 21-05-2012	0.792	3.66
Contracted employees (Note a)	6,000,000	–	–	6,000,000	22-05-2002	22-08-2002 to 21-05-2012	0.792	0.40
Contracted employees (Note e)	103,856,000	–	–	103,856,000	31-12-2002	31-12-2002 to 30-12-2012	0.476	6.88

SHARE OPTION SCHEME *(Continued)*

Notes:

- (a) The options granted to these grantees shall be exercisable in the following four batches (the "Vesting Period"):
 - (i) Not more than 25% of options granted exercisable from 22-08-2002 to 21-08-2003;
 - (ii) Not more than 50% of options granted exercisable from 22-08-2003 to 21-08-2004;
 - (iii) Not more than 75% of options granted exercisable from 22-08-2004 to 21-08-2005; and
 - (iv) Free to exercise from 22-08-2005 to 21-05-2012.
- (b) Free to exercise 4,000,000 options from 22-05-2002 to 21-05-2012 and the remaining 4,000,000 options are subject to the Vesting Period set out in Note (a).
- (c) Free to exercise 5,000,000 options from 22-05-2002 to 21-05-2012 and the remaining 5,400,000 options are subject to the Vesting Period set out in Note (a).
- (d) Free to exercise 8,356,000 options from 22-05-2002 to 21-05-2012 and the remaining 46,800,000 options are subject to the Vesting Period set out in Note (a).
- (e) Free to exercise 103,856,000 options from 31-12-2002 to 30-12-2012.
- (f) 31 March 2006 Issued Share Capital is applied to calculate the relevant percentage.

The consideration paid by each of the above directors and employees for the share options granted was HK\$1.

No options were granted, exercised or cancelled during the Year.

Save as disclosed above and in the sections entitled "Directors' Interests in Shares, Underlying Shares and Debentures" and "Substantial Interests in the Share Capital of the Company", at no time during the Year was the Company, or any of its holding companies, subsidiaries or fellow subsidiaries a party to any arrangement to enable the directors or the chief executive of the Company or any of their spouses or children under eighteen years of age to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate.

MANAGEMENT CONTRACTS

Pursuant to an agreement dated 24 September 2003 between the Company and SGC, the latter agreed to provide, inter alia, secretarial and other related services and the use of office equipment to the Group for a term of five years commencing from 23 July 2003 at reimbursement costs which shall not exceed HK\$3,500,000 per annum. Details of the aforesaid agreement are also disclosed in the section entitled "Connected Transactions" below.

Save as disclosed in the section entitled "Connected Transactions" below and other related party transactions during the Year as set out in note 41 on the financial statements, no contracts of significance were entered into or subsisted between the Company or its subsidiaries and the Company's controlling shareholders or its subsidiaries during the Year.

SUBSTANTIAL INTERESTS IN THE SHARE CAPITAL OF THE COMPANY

As at 31 March 2006, to the best knowledge of the directors of the Company, the following parties recorded in the register kept by the Company under section 336 of the SFO were directly or indirectly interested in 5% or more of the issued share capital of the Company:

Long positions in the shares and underlying shares of the Company:

Name	Nature of interest	Interest in shares	Interest in underlying shares pursuant to share options	Interest in underlying shares pursuant to the convertible notes	Aggregate interests	Approximate shareholding percentage (Note vi)
Beijing Stone Investment Company Limited	Corporate (Note i)	407,110,053	–	–	407,110,053	26.98
Beijing Stone Investment Company Limited Employees' Shareholding Society	Corporate (Note ii)	407,110,053	–	–	407,110,053	26.98
Stone Jiu Guang New Technology Development (Holdings) Co. Ltd.	Corporate (Note ii)	407,110,053	–	–	407,110,053	26.98
Shenyang Huguang Group Co. Ltd.	Corporate (Note ii)	407,110,053	–	–	407,110,053	26.98
SGC	Corporate (Note ii)	500,546,466	–	–	500,546,466	33.17
深圳發展銀行深圳人民橋支行	Corporate (Note iii)	230,000,000	–	–	230,000,000	15.24
Ready Finance	Corporate (Note iv)	–	–	492,105,264	492,105,264	32.61
Duan Yongji	Personal (Note v)	45,075,538	3,900,000	182,692,305	231,667,843	15.35
Shi Yuzhu	Corporate (Note iv)	–	–	492,105,264	492,105,264	32.61

SUBSTANTIAL INTERESTS IN THE SHARE CAPITAL OF THE COMPANY *(Continued)*

Notes:

- i. The shareholding of 407,110,053 shares comprised the combined shareholdings of Beijing Stone Investment Company Limited and its associates (as defined in the Listing Rules).
- ii. Beijing Stone Investment Company Limited is owned as to 42.3% by Stone Jiu Guang New Technology Development (Holdings) Co. Ltd., 6.7% by SGC and 51% by the Beijing Stone Investment Company Limited Employees' Shareholding Society which are accordingly deemed to be interested in the said 407,110,053 shares. Stone Jiu Guang New Technology Development (Holdings) Co. Ltd. is owned as to 56.14% by Shenyang Huguang Group Co. Ltd. which is accordingly also deemed to be interested in the said 407,110,053 shares. In addition, SGC also beneficially holds 92,374,413 shares indirectly and 1,062,000 shares directly.
- iii. The interest of 深圳發展銀行深圳人民橋支行 is held by it as person having a security interest in shares.
- iv. The interest of Ready Finance is held by it as beneficial owner. Please also refer to Note (2) on page 17.
- v. The interest of Mr. Duan Yongji is held by him as beneficial owner. Please also refer to Note (1) on page 17.
- vi. 31 March 2006 Issued Share Capital is applied to calculate the relevant percentage.

Saved as disclosed above, the Company has not been notified of any other interests representing 5% or more of the issued share capital of the Company and recorded in the register of interests maintained under section 336 of the SFO as at 31 March 2006.

CONNECTED TRANSACTIONS

- (a) On 10 March 1999, Beijing Stone New Technology Industrial Company Limited ("Beijing New Technology") (a subsidiary of the Company) and SGC, a controlling shareholder of the Company, entered into an agreement (the "I/E Agreement"), pursuant to which Beijing New Technology appointed SGC to act as its agent to deal with all import procedural matters during the year 1999. Details of the I/E Agreement are set out below and have been published in the Company's announcement dated 17 December 1999:

Services to be provided: arrangement for shipment of goods from Hong Kong to the PRC and for remittance of the price of the goods to Hong Kong for Beijing New Technology by Stone Group Corporation Import and Export Company ("Stone I/E") as directed by SGC

Term: for the year 1999 and renewable on annual basis thereafter

Handling fee: 1.3% of the costs of goods for every shipment of goods arranged by Stone I/E provided that the annual aggregate handling fee shall not exceed HK\$5,000,000, or 3% of the net tangible assets of the Company as shown in its latest published audited consolidated financial statements

CONNECTED TRANSACTIONS *(Continued)*

- (b) On 24 September 2003, SGC and the Company entered into a service agreement (the "Service Agreement"), pursuant to which SGC agreed to provide the Group with general services as directed by the board of directors of the Company from time to time in connection with the business and operations of the Group. Details of the Service Agreement are set out below and have been published in the Company's announcement dated 10 December 2003:

Services to be provided: provision of management staffing services for the overall management, administration and control of the business of the Group; provision of company secretarial services; dispatch of documents and materials as the Company may request for distribution to its shareholders and/or warrant holders and related preparations and arrangements; provision of office machines, facilities and equipment; and provision of public relation services (collectively, the "Services")

Purpose of the transaction: more economical and cost-effective for the Group to engage SGC to perform the Services

Term: 5 years commencing from 23 July 2003 and expiring on 22 July 2008 (both days inclusive)

Service fee: on reimbursement basis of not more than HK\$3,500,000 per annum

- (c) On 20 December, 2005, the Company and Ready Finance entered into a conditional agreement in relation to the repurchase of HK\$191,955,403 nominal value of the Company's approximately HK\$566,000,000 outstanding zero-coupon convertible notes maturing on 3 March 2009 (with conversion price of HK\$0.76) held by Ready Finance for a cash consideration of HK\$145,406,003 (the "Repurchase Agreement"). Details of the Repurchase Agreement (including parties, purpose and major terms) have been published in the Company's announcement dated 28 December 2005 (the "RA Announcement").

Ready Finance is wholly owned by Mr. Shi Yuzhu, a director of the Company, and therefore is a connected person of the Company.

The entering into of the Repurchase Agreement constituted a discloseable and connected transaction of the Company, which requires the approval of the Independent Shareholders (as defined in the RA Announcement). A circular containing, amongst other matters, details of the Repurchase Agreement, a letter of advice from the independent board committee to the Independent Shareholders and the opinion of the independent financial adviser has been dispatched to the shareholders of the Company and the transactions contemplated under the Repurchase Agreement have been approved at an extraordinary general meeting of the Company held on 9 February 2006.

CONNECTED TRANSACTIONS *(Continued)*

(d) On 30 May 2006, Beijing New Technology, Mr. Guan Jizhen ("Mr. Guan") and Beijing Metoyou Information Technology Limited ("Beijing MTY") (an associated company of the Company) entered into a sale and purchase agreement (the "S&P Agreement"), pursuant to which Beijing New Technology agreed to sell to Mr. Guan 20% equity interest (the "Guan Sale Interest") in Beijing Stone Intelligent Transportation System Integration Company Limited ("Stone Intelligent Transportation Company") at a consideration of RMB2,000,000 and agreed to sell to Beijing MTY 20% equity interest (the "MTY Sale Interest") in Stone Intelligent Transportation Company at a consideration of RMB2,000,000. Details of the S&P Agreement are set out below:

Parties:	(i) Beijing New Technology as vendor (ii) Mr. Guan and Beijing MTY as purchasers
Assets disposed of:	40% equity interest in Stone Intelligent Transportation Company
Consideration:	within 10 business days after completion of the registration procedure with the relevant authority in the PRC for the transfer of the Guan Sale Interest and the transfer of the MTY Sale Interest, Mr. Guan will pay Beijing New Technology RMB2,000,000 in one lump sum and Beijing MTY will pay Beijing New Technology RMB2,000,000 in one lump sum
Purpose of the transaction:	to lead to a synergy for the business of Stone Intelligent Transportation Company and the business of Beijing MTY

Since Mr. Guan is a director and a substantial shareholder of Stone Intelligent Transportation Company holding 20% equity interest in Stone Intelligent Transportation Company, the disposal of the Guan Sale Interest was a connected transaction of the Company. Details of the S&P Agreement have been published in the Company's announcement dated 29 June 2006.

Other material related party transactions entered by the Group during the Year are set out in note 41 on the financial statements.

ANNUAL REVIEW OF CONTINUING CONNECTED TRANSACTIONS

The transactions contemplated under the I/E Agreement and the Service Agreement constitute continuing connected transactions of the Company under the Listing Rules.

The independent non-executive directors of the Company had reviewed the transactions contemplated under the I/E Agreement and the Service Agreement for the Year (collectively, the "Transactions") and confirmed that the Transactions were entered into:

- (a) in the ordinary and usual course of business of the Group;
- (b) on normal commercial terms; and
- (c) in accordance with the terms of each of the I/E Agreement and the Service Agreement that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

The auditors of the Company had reviewed the Transactions and reported that:

- (a) the directors of the Company have approved the Transactions;
- (b) the Transactions have been entered into in accordance with the terms of each of the I/E Agreement and the Service Agreement; and
- (c) the Transactions have not exceeded the annual caps as disclosed in the subsections (a) and (b) of the section entitled "Connected Transactions" above.

PURCHASE, SALE AND REDEMPTION OF THE COMPANY'S LISTED SECURITIES

During the Year, certain shares in the Company were repurchased by the Company on the Stock Exchange and those shares were subsequently cancelled by the Company. Details of the share repurchases are set out in note 34 on the financial statements.

Save as disclosed above, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's listed securities during the Year.

PROPERTIES

Particulars of the major properties and property interests of the Group are shown on page 136 of this annual report.

RETIREMENT SCHEMES

Particulars of the retirement schemes of the Group are set out in note 14 on the financial statements.

PUBLIC FLOAT

Based on the information that is publicly available to the Company and within the knowledge of its directors, as at the date of this report, there is sufficient public float of not less than 25% of the Company's issued shares as required under the Listing Rules.

REVIEW BY AUDIT COMMITTEE

The audit committee of the Company comprises four independent non-executive directors, namely, Mr. Ng Ming Wah, Charles, Mr. Andrew Y. Yan, Mr. Liu Ji and Mr. Liu Jipeng. The audit committee has reviewed the audited financial statements for the Year and has also discussed auditing, internal control and financial reporting matters including the review of accounting practices and principles by the Group.

AUDITORS

The financial statements have been audited by Messrs. KPMG who retire and, being eligible, offer themselves for reappointment. A resolution for the reappointment of Messrs. KPMG as auditors of the Company is to be proposed at the forthcoming annual general meeting.

There is no change in auditors of the Company in the past 3 years.

POST BALANCE SHEET EVENT

Details are set out in note 42 on the financial statements.

On behalf of the Board

DUAN Yongji

Chairman

Hong Kong, 18 July 2006