

Chairman's Statement

On behalf of the board of directors (the "Board"), I am pleased to present to the shareholders the annual results of China Water Industry Group Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") for the year ended 31 December 2006.

RESULTS

During the year under review, the Group achieved the turnover of HK\$70.1 million, an increase of 14.5% against HK\$61.2 million in 2005. Total gross profit for the year was HK\$11.6 million, 45.6% more than that of last year. However, the Group recorded a net loss of HK\$95.7 million due to inventories written off of HK\$35.3 million and bad and doubtful debts provision of HK\$14.9 million being provided in computer peripherals business and HK\$14.0 million of advertising expenses spent in promotion of the TechnoMarine watches business.

BUSINESS REVIEW

Computer Peripherals business review

During 2006, the Group's computer peripherals business encountered tough challenges. Given the rising costs of raw materials and increasing market competition, the business sector faced a general decline in profit margin, which affected most small and medium-sized manufacturers. Under the intense competition from industry peers who rely on domestic source of supply for raw materials, the Group experienced heavy pressure in product pricing. Despite the various measures taken to tighten cost control, to improve production and operation efficiency, the Group's computer peripheral business still could not generate a positive profit figure. The performance of computer peripherals business segment was disappointing to the Directors again. In view of successive losses making records, the Directors decided not to inject further resources and would maintain the existing scale of operation with primary focus on achieving effective cost saving methods.

TechnoMarine Watches business review

Although Hong Kong's economy appears to be on the way back to steady growth with improving unemployment rate and rising income level, the operating environment of the segment was still challenging due to escalating rental for shops, growing staff costs as well as rising commodities prices. All these have added extensive cost pressure to us. The expansion of distribution points in Asia Pacific region was stagnant. Brand development was running far behind the management's expectation in the brand management strategic plan and schedule. In addition, the customers could easily purchase homogeneous watches via internet or small watch shops which had seriously affected sales growth and selling price. The management is considering focusing more on wholesale and distribution of TechnoMarine products in order to stay away from the fast and accelerative increase in shop rental and staff costs.

Water supply and water related business segment

The Group has realigned its business focus on water supply and water-related industries in the People's Republic of China (the "PRC"). Consequently, the Company has changed its name to China Water Industry Group Limited to signify this strategic move. Following the new business direction, the Group had acquired 2 water supply plants and 2 sewage treatment plants in the PRC. The Group is now providing water and/or sewage treatment services to more than 0.6 million people in Jiangxi, Anhui and Shangdong provinces in the PRC. In addition to the provision of water supply and sewage treatment service, the Group is also providing water meter installation service to customers and will undertake several water supply and water related construction projects to further strengthen the Group's revenue and earning bases. The Three Acquisitions would be a significant milestone of the Group on its business strategy to transform the core business into the water supply and other water-related industries in the PRC.



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PROSPECTS

Like all other industries, the Group's performance was affected by external economic and the surging price of materials beyond its control. The Directors thought that the future developments of the computer peripherals business and the TechnoMarine watches business of the Group were relatively limited. On the other hand, water supply and water related industry in PRC is comparatively immunized and less affected by fluctuations in economic cycles. The Directors believe that our new investments will provide the Group with stable return on investment and long term profitability.

China, with per capita available water resources only one fourth of the world average, is one of the few countries with an acute shortage of water. Besides, its unequal distribution of water resources makes the situation even worse for some mainland regions, particularly the northern ones. Clean and safe-to-consume water has become a scarce resource.

China is experiencing an unprecedented phase of urbanization. Its rural population, accounting for around 70% of its general population, is migrating at a rapid pace to urban cities, which are also all expanding in leaps and bounds. The demand for urban water supply is growing with a strong momentum.

While China economy's continued brisk growth has created a picture of prosperity that has been unseen till recently, its impact on the environment is just as immense. In particular, water pollution is an increasingly serious issue, which has led to new demand that promotes the development of the sewage treatment industry.

In the face of the above, the PRC government has adopted a range of proactive measures. Firstly, a water tariff reform has been carried out to promote the continued increase of water tariffs. It is expected that higher water tariffs will create a water saving tendency in society and support the water service sector to grow in a sustainable manner. Secondly, the property right reform has been taken to a new level to restructure the capital structure of water service operators, which used to be wholly state-owned, in order to attract more foreign and private capital to satisfy the demand for investments in the urban water supply and sewage treatment market.

The implementation of the above measures has given a huge boost to the growth of the water service market. As a result, the sector has turned into a massive emerging industry with active investments, increasing efficiency and unlimited opportunities.

Having considered all these, the Group has determined to redirect its principle business to the water service market in China. Moreover, its business focus will be set on the urban water supply and sewage treatment industry, which are the most well-developed and capital efficient segments of the market.

The Group will mainly expand its presence in the water service market by acquiring water supply and sewage treatment facilities that are currently operating. This ensures all new investments in the water service sector will start generating revenues and returns to the Group immediately.

Medium mainland cities will be targeted as the Group's major growth market. We expect to start our base from there and then move on to secure projects in large and small cities in order to establish an all-rounded and extensive business coverage in the water service market in China.



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The Group will identify investment opportunities mainly in the urban water supply sector. Its approach is to establish a complete supply chain by acquiring control in the water supply market of a city before extending its reach downstream to the sewage treatment sector.

The Group has built up a team of high calibre mainland water service professionals. Relying on their extensive project knowledge and management experience, the Group has successfully set up its first water service platforms in China. Besides, it is in negotiations with a number of cities in pursuit of various business initiatives. So far, these projects have been progressing on schedule. The water service assets acquired or to be acquired are expected to generate a substantial stream of revenues and a considerable profit contribution for the Group in the future.

APPRECIATION

Finally, I would like to take this opportunity to express my gratitude to my fellow directors, management and employees for their contributions and dedication to the development of the Group and deep thanks to our shareholders, customers, suppliers and business partners for their continued supports.

Wang Chia Chin

Chairman

Hong Kong, 25 April 2006