



China Water Industry Group Limited 中國水業集團有限公司*

(Incorporated in the Cayman Islands with limited liability)

Stock Code : 1129

Interim Report **2008**



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CORPORATE INFORMATION

BOARD OF DIRECTORS

Executive Directors

Mr. Li Yu Gui (*Chairman*)
Mr. Liu Peng Cheng (*Deputy Chairman*)
Mr. Zhong Wen Sheng (*Managing Director*)
Mr. Sze Chun Ning, Vincent (*Deputy Managing Director*)
Mr. Liu Bai Yue (*Chief Operating Officer*)
Mr. Shi De Mao
Ms. Chu Yin Yin, Georgiana
Mr. Wang Chia Chin (*Resigned on 10 June 2008*)

Non-Executive Directors

Mr. Huang Yuan Wen
Mr. Pan Shi Ying

Independent Non-Executive Directors

Mr. Chang Kin Man
Mr. Wu Tak Lung
Mr. Gu Wen Xuan

AUDIT COMMITTEE

Mr. Chang Kin Man (*Chairman*)
Mr. Wu Tak Lung
Mr. Gu Wen Xuan

REMUNERATION COMMITTEE

Mr. Chang Kin Man (*Chairman*)
Mr. Wu Tak Lung
Mr. Zhong Wen Sheng

QUALIFIED ACCOUNTANT AND COMPANY SECRETARY

Ms. Chu Yin Yin, Georgiana

PRINCIPAL BANKERS

PRC

Agricultural Bank of China
Bank of China
Industrial and Commercial Bank of China

Hong Kong

DBS Bank (Hong Kong) Limited
The Hongkong and Shanghai Banking Corporation Limited
Hang Seng Bank Limited
Bank of China (Hong Kong) Limited
Chiyu Banking Corporation Limited

LEGAL ADVISERS

CHINA

Guangdong Huaxida Lawyers

HONG KONG

Robertsons Solicitors & Notaries
William W. L. Fan & Company

AS TO CAYMAN ISLANDS LAWS

Conyers Dill & Pearman

AUDITORS

SHINEWING (HK) CPA Limited

PRINCIPAL SHARE REGISTRAR AND TRANSFER OFFICE

Butterfield Fund Services (Cayman) Limited
Cricket Square Hutchins Drive
P. O. Box 2681
Grand Cayman KY1-1111
Cayman Islands

HONG KONG BRANCH SHARE REGISTRAR TRANSFER OFFICE

Union Registrars Limited
Room 1901-1902, Fook Lee Commercial Centre
Town Place, 33 Lockhart Road
Wanchai, Hong Kong

HEAD OFFICE AND PRINCIPAL PLACE OF BUSINESS

Room 1207, 12th Floor
West Tower, Shun Tak Centre
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STOCK CODE

1129

CONDENSED CONSOLIDATED INCOME STATEMENT

For the six months ended 30 June 2008

	Notes	Six months ended 30 June	
		2008 HK\$'000 (Unaudited)	2007 HK\$'000 (Unaudited)
Continuing operations			
Turnover	3	54,592	26,526
Cost of sales		(31,386)	(25,052)
Gross profit		23,206	1,474
Net gain on disposal of debt securities		1,143	–
Net fair value change on listed trading securities		5,531	–
Increase in fair values of financial assets at fair value through profit or loss		2,435	–
Change in fair value of convertible bonds		1,461	–
Discount on acquisition of a business		24,166	–
Other operating income		6,825	3,030
Selling and distribution costs		(3,102)	(1,586)
Administrative expenses		(23,029)	(22,102)
Share-based payment expense		–	(40,432)
Share of results of associates		5,177	749
Finance costs		(2,719)	(19)
Profit (loss) before tax	4	41,094	(58,886)
Income tax expense	5	(284)	(70)
Profit (loss) for the period from continuing operations		40,810	(58,956)
Discontinued operations			
Loss for the period from discontinued operations	6	–	(6,096)
Profit (loss) for the period		40,810	(65,052)
Attributable to:			
Equity holders of the Company		33,613	(59,253)
Minority interests		7,197	297
		40,810	(58,956)
Earnings (loss) per share	7		
From the continuing and discontinued operations			
Basic		HK1.78 cents	HK(4.02) cents
Diluted		HK1.58 cents	N/A
From continuing operations			
Basic		HK1.78 cents	HK(3.65) cents
Diluted		HK1.58 cents	N/A
From discontinued operations			
Basic		–	HK(0.37) cents
Diluted		–	N/A

CONDENSED CONSOLIDATED BALANCE SHEET

As at 30 June 2008

	Notes	At 30 June 2008 HK\$'000 (Unaudited)	At 31 December 2007 HK\$'000 (Audited)
Non-current assets			
Property, plant and equipment	9	641,988	240,551
Prepaid lease payments		57,707	10,143
Goodwill		323,286	77,333
Interests in associates		71,321	7,617
Available-for-sale investments		64,756	–
Deposits paid for acquisition of subsidiaries		79,610	567,990
		1,238,668	903,634
Current assets			
Inventories		8,381	4,116
Trade and other receivables	10	146,674	58,514
Amounts due from related parties		–	213
Amount due from an associate		5,387	–
Amount due from a minority shareholder of a subsidiary		1,013	946
Financial assets at fair value through profit or loss		9,821	–
Held-for-trading investments		3,776	–
Prepaid lease payments		1,091	221
Cash held at financial institutions		9,624	30,000
Bank balances and cash		147,450	78,839
		333,217	172,849
Current liabilities			
Trade and other payables	11	231,912	29,770
Bank and other borrowings – due within one year	12	3,427	–
Amounts due to related parties		–	204
Amounts due to directors		93	223
Tax payable		236	281
Other loans		33,471	9,487
		269,139	39,965
Net current assets		64,078	132,884
Total assets less current liabilities		1,302,746	1,036,518

CONDENSED CONSOLIDATED BALANCE SHEET (Continued)

As at 30 June 2008

	Notes	At 30 June 2008 HK\$'000 (Unaudited)	At 31 December 2007 HK\$'000 (Audited)
Capital and reserves			
Share capital	13	189,090	189,090
Reserves		373,020	340,601
Equity attributable to equity holders of the parent		562,110	529,691
Minority interests		148,443	84,475
Total equity		710,553	614,166
Non-current liabilities			
Bank and other borrowings – due after one year	12	207,821	32,955
Loans from a minority shareholder		3,602	11,738
Convertible bonds	14	325,411	326,872
Government grants		55,359	50,787
		592,193	422,352
		1,302,746	1,036,518

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the six months ended 30 June 2008

	Attributable to equity holders of the company									
	Share capital	Share premium	Share options reserve	Translation reserve	Reserve funds	Investment revaluation reserve	Accumulated losses	Total	Minority interests	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
(Unaudited)										
At 1 January 2007	116,450	27,905	7,635	1,277	228	-	(101,767)	51,728	6,063	57,791
Issue of shares	53,000	377,700	-	-	-	-	-	430,700	-	430,700
Share issue expenses	-	(28,482)	-	-	-	-	-	(28,482)	-	(28,482)
Recognition of equity-settled share based payments	-	-	40,432	-	-	-	-	40,432	-	40,432
Exercise of share options	18,620	38,248	(10,432)	-	-	-	-	46,436	-	46,436
Capital contribution from a minority shareholder of a subsidiary	-	-	-	-	-	-	-	-	12,310	12,310
Acquisition of subsidiaries	-	-	-	-	-	-	-	-	38,213	38,213
Loss for the period	-	-	-	-	-	-	(65,349)	(65,349)	297	(65,052)
Exchange differences arising on translation of foreign operations	-	-	-	(610)	-	-	-	(610)	-	(610)
At 30 June 2007	188,070	415,371	37,635	667	228	-	(167,116)	474,855	56,883	531,738
(Unaudited)										
At 1 January 2008	189,090	418,093	727	11,080	-	-	(89,299)	529,691	84,475	614,166
Acquisition of subsidiaries	-	-	-	-	-	-	-	-	92,320	92,320
Loss on fair value changes of available-for-sale investments recognised directly in equity	-	-	-	-	-	(14,402)	-	(14,402)	(1,637)	(16,039)
Partial disposal of a subsidiary	-	-	-	-	-	-	-	-	13,111	13,111
Acquisition of additional interest in a subsidiary	-	-	-	-	-	-	-	-	(54,207)	(54,207)
Profit for the period	-	-	-	-	-	-	33,613	33,613	7,197	40,810
Share of reserves of associates	-	-	-	3,305	-	-	-	3,305	-	3,305
Exchange differences arising on translation of foreign operations	-	-	-	9,903	-	-	-	9,903	7,184	17,087
At 30 June 2008	189,090	418,093	727	24,288	-	(14,402)	(55,686)	562,110	148,443	710,553

CONDENSED CONSOLIDATED CASH FLOW STATEMENT

For the six months ended 30 June 2008

	Six months ended 30 June	
	2008 HK\$'000 (Unaudited)	2007 HK\$'000 (Unaudited)
NET CASH GENERATED FROM (USED IN) OPERATING ACTIVITIES	27,293	(30,619)
NET CASH GENERATED FROM (USED IN) INVESTING ACTIVITIES	28,932	(56,338)
NET CASH (USED IN) GENERATED FROM FINANCING ACTIVITIES	(11,201)	472,192
INCREASE IN CASH AND CASH EQUIVALENTS	45,024	385,235
CASH AND CASH EQUIVALENTS AT 1 JANUARY	108,839	5,045
EFFECT OF FOREIGN EXCHANGE RATE CHANGES	3,211	(610)
CASH AND CASH EQUIVALENTS AT 30 JUNE, represented by bank balances and cash and cash held at financial institutions	157,074	389,670

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION

For the six months ended 30 June 2008

1. COMPANY INFORMATION

China Water Industry Group Limited (the "Company") was incorporated in the Cayman Islands as an exempted company with limited liability and its shares are listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). The addresses of the registered office and principal place of business of the Company are disclosed in the "Corporate Information" section of the interim report.

The Company and its subsidiaries (the "Group") are principally engaged in provision of water supply and sewage treatment in the People's Republic of China (the "PRC"), investments in financial and investment products and trading of watches and accessories.

Other than those operating subsidiaries established in the PRC and engaged in the provision of water supply and sewage treatment services, which functional currency is Renminbi ("RMB"), the functional currency of the Group is Hong Kong dollars. The condensed consolidated Interim Financial Information are presented in Hong Kong dollars. The reason for selecting Hong Kong dollars as its presentation currency is because the Company is a public company with its shares listed on the Stock Exchange.

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES

The unaudited condensed consolidated Interim Financial Information have been prepared in accordance with Hong Kong Accounting Standard ("HKAS") No. 34 "Interim Financial Reporting" issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") and with the applicable disclosure requirements of Appendix 16 to the Rules Governing the Listing of Securities on the Stock Exchange.

The condensed consolidated Interim Financial Information have been prepared under the historical cost basis, except for certain financial instruments, which are measured at fair values.

The condensed consolidated Interim Financial Information does not include all the information and disclosures required in the annual financial statements and should be read in conjunction with the Group's annual financial statements for the year ended 31 December 2007.

The accounting policies used in the preparation of the condensed consolidated Interim Financial Information for the six months ended 30 June 2008 are consistent with those used in the Group's annual financial statements for the year ended 31 December 2007, except as described below.

In the current interim period, the Group has applied, for the first time, a number of new standards, amendments and interpretations ("new HKFRSs") issued by the HKICPA, which are effective for accounting periods beginning 1 January 2008. The adoption of these new HKFRSs has had no material effect on how the results and financial position of the Group for the current or prior accounting periods have been prepared and presented. Accordingly, no prior period adjustment has been required.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (Continued)

The Group has not early applied the following new and revised standards, amendments or interpretations that have been issued but are not yet effective.

Hong Kong Accounting Standard ("HKAS") 1 (Revised)	Presentation of Financial Statements ¹
HKAS 1 & 32 (Amendment)	Puttable Financial Instruments and Obligations Arising on Liquidation ¹
HKAS 23 (Revised)	Borrowing Costs ¹
HKAS 27 (Revised)	Consolidated and Separate Financial Statements ³
HKFRS 2 (Amendment)	Share-based Payment – Vesting Conditions and Cancellations ¹
HKFRS 3 (Revised)	Business Combination ³
HKFRS 8	Operating Segments ¹
HK(IFRIC)-Interpretation ("INT") 13	Customer Loyalty Programmes ²
HK(IFRIC)-INT 15	Agreements for the Construction of Real Estate ¹
HK(IFRIC)-INT 16	Hedges of a Net Investment in a Foreign Operation ⁴

¹ Effective for annual periods beginning on or after 1 January 2009.

² Effective for annual periods beginning on or after 1 July 2008.

³ Effective for annual periods beginning on or after 1 July 2009.

⁴ Effective for annual periods beginning on or after 1 October 2008.

The directors of the Company anticipate that the application of these standards, amendments or interpretations will have no material impact on the results and financial position of the Group except for the adoption of HKFRS 3 (Revised) and HKAS 27 (Revised). The adoption of HKFRS 3 (Revised) may affect the accounting for business combination for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009. HKAS 27 (Revised) will affect the accounting treatment for changes in a parent's ownership interest in a subsidiary that do not result in a loss of control, which will be accounted for as equity transactions.

3. SEGMENT INFORMATION

Business segments

For management purposes, during the six months ended 30 June 2008, the Group is organised into three operating divisions – provision of water supply and sewage treatment in the PRC, investments in financial and investment products and trading of watches and accessories. These divisions are the basis on which the Group reports its primary segment information.

Principal activities are as follows:

- (a) Provision of water supply and sewage treatment in the PRC;
- (b) Investments in financial and investment products; and
- (c) Trading of watches and accessories.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

3. SEGMENT INFORMATION (Continued)

The unaudited segment information about these businesses is presented below:

For the six months ended 30 June (Unaudited)

	Continuing operations						Discontinued operations					
	Provision of water supply and sewage treatment in the PRC		Investments in financial and investment products		Trading of watches and accessories		Sub-total		Production and sales of computer peripherals		Total	
	2008	2007	2008	2007	2008	2007	2008	2007	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Sales to external customers	54,592	11,925	-	-	-	14,601	54,592	26,526	-	9,759	54,592	36,285
Segment results	11,013	724	6,905	-	-	(14,069)	17,918	(13,345)	-	(5,950)	17,918	(19,295)
Unallocated corporate income							1,924	2,285	-	-	1,924	2,285
Change in fair value of convertible bonds							1,461	-	-	-	1,461	-
Discount on acquisition of a business							24,166	-	-	-	24,166	-
Share-based payment expense							-	(40,432)	-	-	-	(40,432)
Unallocated corporate expenses							(6,833)	(8,124)	-	-	(6,833)	(8,124)
Finance costs							(2,719)	(19)	-	(146)	(2,719)	(165)
Share of results of associates							5,177	749	-	-	5,177	749
Profit (loss) before tax							41,094	(58,886)	-	(6,096)	41,094	(64,982)
Income tax expense							(284)	(70)	-	-	(284)	(70)
Profit (loss) for the period							40,810	(58,956)	-	(6,096)	40,810	(65,052)

The Group's operations are located in the PRC and Hong Kong. The Group's trading of watches and accessories division and investments in financial and investment products are located in Hong Kong. Provision of water supply and sewage treatment and production and sales of computer peripherals are carried out in the PRC.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

3. SEGMENT INFORMATION (Continued)

The following table provides an analysis of the Group's sales by geographical market, irrespective of the origin of the goods/services:

	Six months ended 30 June	
	2008	2007
	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)
Europe	–	2,465
Asia Pacific	–	21,539
North America	–	356
The PRC	54,592	11,925
	54,592	36,285

4. PROFIT (LOSS) BEFORE TAX

	Continuing operations		Discontinued operations		Total	
	Six months ended 30 June		Six months ended 30 June		Six months ended 30 June	
	2008	2007	2008	2007	2008	2007
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)

Profit (loss) before tax has been arrived at after charging (crediting):

Staff costs including directors' emoluments						
– salaries, wages and other benefits	11,549	4,941	–	2,981	11,549	7,922
– share-based payment expense	–	1,052	–	–	–	1,052
– retirement benefit scheme contributions	1,461	143	–	–	1,461	143
Total staff costs	13,010	6,136	–	2,981	13,010	9,117
Amortisation of prepaid lease payment for land use rights	270	25	–	–	270	25
Allowance for inventories (included in cost of sales)	–	738	–	3,977	–	4,715
Impairment loss on trade receivables	–	–	–	2,041	–	2,041
Share-based payment expense	–	39,380	–	–	–	39,380
Cost of inventories recognised as expenses	6,095	10,162	–	912	6,095	11,074
Depreciation of property, plant and equipment	9,459	1,432	–	1,776	9,459	3,208
Minimum lease payments under operating leases	1,458	590	–	1,161	1,458	1,751
Loss on disposal of property, plant and equipment	–	288	–	–	–	288
Loss on partial disposal of a subsidiary	140	–	–	–	140	–
Gain on disposal of convertible notes receivables	(1,328)	–	–	–	(1,328)	–
Interest income	(1,925)	(3,028)	–	–	(1,925)	(3,028)
Net foreign exchange (gain) loss	(1,070)	11	–	(28)	(1,070)	(17)

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

5. INCOME TAX EXPENSE

	Six months ended 30 June	
	2008	2007
	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)
Continuing operations		
Current tax in the PRC	284	70

No Hong Kong Profits Tax has been provided as the Group did not have estimated assessable profits arising in Hong Kong for the six months ended 30 June 2008 (six months ended 30 June 2007: Nil). Taxes arising in other jurisdictions are calculated at the rates of tax prevailing in the respective jurisdictions in which the Group operates, based on existing legislation, interpretations and practices in respect thereof.

6. DISCONTINUED OPERATIONS

On 13 November 2007, the Group entered into an agreement to dispose of its 100% interest in Pablo Enterprise Limited and its subsidiaries ("Pablo Group"), which carried out all of the Group's production and sale of computer peripherals operations. The disposal was effected in order to focus the Group's resources in its remaining businesses. The disposal was completed on 28 December 2007 on which date control of Pablo Enterprise Limited passed to the acquirer.

The results of the production and sale of computer peripherals operations for the six months ended 30 June 2007, which had been included in the condensed consolidated income statement, were as follows:

	Six months ended 30 June 2007 HK\$'000 (Unaudited)
Turnover	9,759
Cost of sales	(8,539)
Gross profit	1,220
Other operating income	675
Selling and distribution costs	(498)
Administrative expenses	(5,306)
Impairment loss on trade receivables	(2,041)
Finance costs	(146)
Loss before tax	(6,096)
Income tax expense	-
Loss for the period and attributable to equity holders of the Company	(6,096)

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

7. EARNINGS (LOSS) PER SHARE

From continuing and discontinued operations

The calculation of basic and diluted earnings (loss) per share attributable to equity holders of the Company is based on the following data:

	Six months ended 30 June	
	2008	2007
	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)
Earnings (loss)		
Profit (loss) for the purposes of basic earnings (loss) per share (Profit (loss) for the period attributable to equity holders of the Company)	33,613	(65,349)
Effect of dilutive potential shares:		
– Interest on convertible bonds	481	–
Earnings (loss) for the purposes of diluted earnings per share	34,094	(65,349)
Number of shares		
	'000	'000
Weighted average number of ordinary shares for the purpose of basic earnings (loss) per share	1,890,900	1,623,809
Effect of dilutive potential shares:		
– Share options issued by the Company	142	58,968
– Conversion of convertible bonds	271,127	–
Weighted average number of ordinary shares for the purpose of diluted earnings (loss) per share	2,162,169	1,682,777

From continuing operations

The calculation of the basic and diluted earnings (loss) per share from continuing operations attributable to equity holders of the Company is based on the following data:

	Six months ended 30 June	
	2008	2007
	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)
Profit (loss) for the period attributable to equity holders of the Company	33,613	(65,349)
Less: Loss for the period from discontinued operations attributable to equity holders of the Company (Note 6)	–	(6,096)
Earnings (loss) for the purpose of basic earnings (loss) per share from continuing operations	33,613	(59,253)
Effect of dilutive potential shares:		
– Interest on convertible bonds	481	–
Earnings (loss) for the purpose of diluted earnings (loss) per share from continuing operations	34,094	(59,253)

The denominators used are the same as those detailed above for both basic and diluted earnings (loss) per share.

From discontinued operations

Basic loss per share for discontinued operations was HK0.37 cents for the six months ended 30 June 2007 based on the loss for the period from the discontinued operations of approximately HK\$6,096,000 and the denominators detailed above for basic loss per share for the six months ended 30 June 2007.

No diluted loss per share for the six months ended 30 June 2007 had been presented as the effect of the conversion of the Company's outstanding share options was anti-dilutive.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

8. DIVIDENDS

No dividend was paid or proposed during the periods ended 30 June 2008 and 2007, nor has any dividend been proposed since the balance sheet date.

9. PROPERTY, PLANT AND EQUIPMENT

During the six months ended 30 June 2008, the Group's purchased property, plant and equipment amounted to approximately HK\$41,011,000 (six months ended 30 June 2007: approximately HK\$58,745,000).

During the six months ended 30 June 2007, property, plant and equipment with an aggregate amount of approximately HK\$12,310,000 was injected by a minority shareholder of a subsidiary as contribution to the registered capital of that subsidiary (six months ended 30 June 2008: Nil).

During the six months ended 30 June 2008, property, plant and equipment with an aggregate amount of approximately HK\$346,118,000 was acquired by the Group through acquisition of subsidiaries (six months ended 30 June 2007: HK\$76,563,000).

10. TRADE AND OTHER RECEIVABLES

	At 30 June 2008 HK\$'000 (Unaudited)	At 31 December 2007 HK\$'000 (Audited)
Trade receivables	15,427	10,114
Less: Impairment loss recognised in respect of trade receivables	(2,093)	(2,093)
	13,334	8,021
Other receivables	130,375	15,912
Deposits and prepayment	2,965	34,581
	146,674	58,514

The Group allows an average credit period of 90 days to 180 days given to the customers.

An aged analysis of trade receivables at the balance sheet dates, based on invoice date, and net of impairment losses recognised was as follows:

	At 30 June 2008 HK\$'000 (Unaudited)	At 31 December 2007 HK\$'000 (Audited)
Current to 90 days	6,627	3,564
91 to 180 days	3,097	4,046
181 to 365 days	1,305	344
Over 1 year	2,305	67
	13,334	8,021

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

11. TRADE AND OTHER PAYABLES

At the balance sheet date, the aging analysis of the trade payables were as follows:

	At 30 June 2008 HK\$'000 (Unaudited)	At 31 December 2007 HK\$'000 (Audited)
Current to 90 days	2,416	2,074
91 to 180 days	1,003	741
181 to 365 days	2,097	1,559
Over 1 year	30,414	868
	35,930	5,242
Other payables	195,982	24,528
	231,912	29,770

12. BANK AND OTHER BORROWINGS

Included in bank and other borrowings as at 30 June 2008 represented bank and other borrowings with an aggregate amount of approximately HK\$176,034,000 were acquired by the Group through acquisition of subsidiaries during the six months ended 30 June 2008.

13. SHARE CAPITAL

	At 30 June 2008 (Unaudited)		At 31 December 2007 (Audited)	
	Number of shares	Amount HK\$'000	Number of shares	Amount HK\$'000
Ordinary shares of HK\$0.1 each				
Authorised capital:				
At beginning and end of period/year	4,000,000,000	400,000	4,000,000,000	400,000
Issued and fully paid:				
At beginning of the period/year	1,890,900,000	189,090	1,164,500,000	116,450
Issue of shares (Notes a & b)	–	–	530,000,000	53,000
Exercise of share options (Note c)	–	–	196,400,000	19,640
At end of the period/year	1,890,900,000	189,090	1,890,900,000	189,090

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

13. SHARE CAPITAL (Continued)

Notes:

- (a) On 31 January 2007, the Company entered into a placing and subscription agreement to place up to 230,000,000 shares of the Company at the price of HK\$0.49 per share. On 2 February 2007, a total of 230,000,000 shares were issued under such placement arrangement.
- (b) On 23 March 2007, the Company entered into a placing agreement to place up to 300,000,000 new shares of the Company at the price of HK\$1.06 per share. On 29 March 2007, a total of 300,000,000 shares were issued under such placement arrangement.
- (c) During the year ended 31 December 2007, 196,400,000 share options were exercised. Details of which has been set out in note 17.

All new shares issued during the year ended 31 December 2007 rank pari passu in all respects with other shares in issue.

14. CONVERTIBLE BONDS

On 3 August 2007, the Company issued convertible bonds in aggregate principal amounts of HK\$385 million. The convertible bonds bear interest from 3 August 2007 at the rate of 0.25% per annum, payable semi-annually in arrear on 3 February and 3 August each year. The convertible bonds may be converted at the option of the convertible bonds holder at a conversion price of HK\$1.42 per ordinary share at any time on or after 13 September 2007 and up to 27 July 2012.

Since the conversion price for the bonds is subject to change, the conversion will not result in settlement by the exchange of a fixed number of equity instruments. Therefore, upon application of HKAS 32 and HKAS 39, it was determined that the bonds do not contain any equity component and the entire bonds were designated as "financial liabilities at fair value through profit or loss" which requires that bonds to be carried at fair value at the balance sheet date and the changes in fair values are recognised in the consolidated income statement. During the period, a gain on change in its fair value of approximately HK\$1,461,000 is recognised in the condensed consolidated income statement (six months ended 30 June 2007: Nil).

The fair value of the bonds at each of the balance sheet date was calculated using the market value basis.

	At 30 June 2008	At 31 December 2007
Stock price	HK\$0.255	HK\$0.50
Exercise price	Subject to adjustment but not less than 80% of HK\$1.42	Subject to adjustment but not less than 80% of HK\$1.42
Expected volatility	49.15%	45.94%
Risk-free rate	3.111%	3.0165%
Option life	4.100 year	4.592 year

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

15. CAPITAL COMMITMENT

	At 30 June 2008 HK\$'000 (Unaudited)	At 31 December 2007 HK\$'000 (Audited)
Capital commitments contracted but not provided for:		
– acquisition of property, plant and equipment	208	25,561
– addition capital injection in a subsidiary	29,274	–
	29,482	25,561

16. OPERATING LEASE COMMITMENTS

At the balance sheet date, the Group had future minimum lease payments under non-cancellable operating leases which fall due as follows:

	At 30 June 2008 HK\$'000 (Unaudited)	At 31 December 2007 HK\$'000 (Audited)
Within one year	1,275	1,045
In the second to fifth years, inclusive	250	70
	1,525	1,115

17. SHARE-BASED PAYMENT TRANSACTIONS

Equity-settled share option scheme:

The Company's share option scheme (the "Scheme"), became effective on 17 January 2002 for the primary purpose of providing incentives to directors and eligible employees or persons and, unless otherwise cancelled or amended, will remain in force for 10 years from that date. Under the Scheme, the board of directors of the Company may grant options to eligible employees, including directors of the Company and its subsidiaries, to subscribe for shares in the Company. Additionally, the Company may, from time to time, grant share options to outside third parties for settlement in respect of goods or services provided to the Company.

At 30 June 2008 and 31 December 2007, the number of shares in respect of which options had been granted and remained outstanding under the Scheme was 18,000,000, representing 0.95% of the shares of the Company in issue at that date.

The total number of shares in respect of which options may be granted under the Scheme is not permitted to exceed 30% of the shares of the Company in issue at any point in time, without prior approval from the Company's shareholders. The number of shares issued and to be issued in respect of which options granted and may be granted to any individual in any one year is not permitted to exceed 1% of the shares of the Company in issue at any point in time, without prior approval from the Company's shareholders. Options granted to substantial shareholders or independent non-executive directors in excess of 0.1% of the Company's share capital or with a value in excess of HK\$5 million, within one year, must be approved in advance by the Company's shareholders.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

17. SHARE-BASED PAYMENT TRANSACTIONS (Continued)

Options granted must be taken up within twelve months of the date of grant, upon payment of HK\$1 per option. Options may be exercised at any time from the date of grant of the share option to the tenth anniversary of the date of grant. The exercise price is determined by the directors of the Company, and will not be less than the higher of (i) the closing price of the Company's shares on the date of grant, (ii) the average closing price of the shares for the five business days immediately preceding the date of grant; and (iii) the nominal value of the Company's share.

The following table discloses movements of the Company's share options held by directors and other eligible persons during both years:

	Outstanding at 1 January 2007	Granted during the year	Exercised during the year	Cancelled during the year	Outstanding at 31 December 2007 and 30 June 2008
Directors	–	28,200,000	(10,200,000)	–	18,000,000
Eligible persons	98,400,000	427,800,000	(186,200,000)	(340,000,000)	–
	98,400,000	456,000,000	(196,400,000)	(340,000,000)	18,000,000

During the year ended 31 December 2007, options were granted on 11 January 2007, 17 January 2007, 4 April 2007 and 28 June 2007 respectively. The estimated fair value of the options granted was approximately HK\$40,432,000.

The fair value was calculated using the Black-Scholes pricing model. The inputs into the model were as follows:

	Share options granted on			
	11 January 2007	17 January 2007	4 April 2007	28 June 2007
Grant date share price	HK\$0.31	HK\$0.42	HK\$1.03	HK\$1.14
Exercise price	HK\$0.34	HK\$0.42	HK\$1.078	HK\$1.14
Expected volatility	50.27%	50.42%	44.41%	40.29%
Option life	0.5 year	0.5 year	0.5 year	0.5 year
Risk-free rate	3.63%	3.69%	3.40% to 3.52%	3.84% to 3.96%
Expected dividend yield	0%	0%	0%	0%

Expected volatility was determined by using the historical volatility of the Company's share price over the previous one year. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non transferability, exercise restrictions and behavioral considerations.

The Group recognised the total expense of approximately HK\$40,432,000 for the six months ended 30 June 2007 in relation to share options granted by the Company.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

18. ACQUISITIONS OF SUBSIDIARIES AND BUSINESS

- (a) On 14 February 2008, the Group acquired 67.32% of the issued share capital of iMerchants Limited, a public limited company incorporated in Hong Kong with its shares being listed on the Growth Enterprise Market (the "GEM") of the Stock Exchange at a consideration of approximately HK\$198,021,000. The acquisition has been accounted for using the purchase method. The amount of goodwill arising as a result of acquisition was approximately HK\$45,310,000.

The net assets acquired in the transaction and the goodwill arising are as follows:

	14 February 2008
	<i>HK\$'000</i>
Net assets acquired:	
Property, plant and equipment	771
Investment in an associate	4,000
Other receivables	2,138
Financial assets at fair value through profit or loss	16,554
Available-for-sale investments	18,535
Held-for-trading investments	64,701
Convertible notes receivables	2,672
Cash held at financial institutions	62,077
Bank balances and cash	60,026
Other payables	(1,249)
Minority interests	(75,237)
	<hr/> 154,988
Goodwill	45,310
	<hr/> 200,298
Total consideration	<hr/> 200,298
Satisfied by:	
Direct costs relating to the acquisition	2,277
Deposits paid for acquisition of subsidiaries	198,021
	<hr/> 200,298
Net cash inflow arising on acquisition:	
Direct costs relating to the acquisition	(2,277)
Cash and bank balances acquired	60,026
Cash held at financial institutions acquired	62,077
	<hr/> 119,826

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

For the six months ended 30 June 2008

18. ACQUISITIONS OF SUBSIDIARIES AND BUSINESS *(Continued)*

(a) *(Continued)*

iMerchants Limited contributed approximately HK\$7,629,000 profit to the Group's profit for the period between the date of acquisition and the balance sheet date.

If the acquisition had been completed on 1 January 2008, total Group's turnover for the six months ended 30 June 2008 would have been remain unchanged and profit for the six months ended 30 June 2008 would have been increased by approximately HK\$5,040,000. The proforma information is for illustrative purposes only and is not necessarily an indication of revenue and results of operations of the Group that actually would have been achieved had the acquisition been completed on 1 January 2008, nor is it intended to be a projection of future results.

In accordance with Rule 26 of the Hong Kong Code on Takeovers and Mergers, the Group is required to make an unconditional mandatory general cash offer for all the issued shares of iMerchants Limited other than those iMerchants Limited's shares already owned by the Group and parties acting in concert with it (the "Share Offer").

At the close of the Share Offer on 13 March 2008, an additional 23.36% of the issued share capital of iMerchants Limited was acquired through the Share Offer with a consideration of approximately HK\$69,384,000, and a goodwill of approximately HK\$15,176,000 was resulted. Upon the close of the Share Offer, 9.32% of the issued capital of iMerchants Limited remains in public hands. To restore to the minimum 15% public float requirement under the Rules Governing the Listing of Securities on the GEM of the Stock Exchange, the Group entered into a placing agreement with Pacific Foundation Securities Limited to place out 6,450,000 ordinary shares of HK\$1 each (representing 5.7% of issued share capital) of iMerchants Limited to independent third parties at a consideration of approximately HK\$16,770,000. Upon the completion of the placing on 14 April 2008, a loss on the partial disposal amounting approximately HK\$140,000 was resulted.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

18. ACQUISITIONS OF SUBSIDIARIES AND BUSINESS (Continued)

- (b) On 18 January 2008, the Group acquired the entire issued share capital of Blue Mountain Hong Kong Group Limited ("Blue Mountain") and a shareholder's loan of approximately HK\$47,730,000 at a consideration of approximately HK\$230,000,000. Blue Mountain is an investment holding company and its sole asset is the 35% equity interest in an associate, Jinan Hongquan Water Production Co., Limited* (濟南泓泉制水有限公司) which has obtained a business license and exclusive right from relevant PRC authority for operation of 30 years for the supply of drinkable water in Jinan City, Shandong Province. The acquisition has been accounted for using the purchase method. The amount of goodwill arising as a result of acquisition was approximately HK\$186,092,000.

The net assets acquired in the transaction and the goodwill arising are as follows:

	18 January 2008 HK\$'000
Net assets acquired:	
Interest in an associate	60,592
Bank balances and cash	6
Loan from a shareholder	(47,730)
	<hr/>
	12,868
Shareholder's loan	47,730
Goodwill	186,092
	<hr/>
Total consideration	246,690
	<hr/>
Satisfied by:	
Deposits paid for acquisition of subsidiaries	230,000
Direct costs relating to the acquisition	16,690
	<hr/>
	246,690
	<hr/>
Net cash outflow arising on acquisition:	
Direct costs relating to the acquisition	(16,690)
Cash and bank balances acquired	6
	<hr/>
	(16,684)
	<hr/>

Blue Mountain contributed approximately HK\$7,424,000 profit to the Group's profit for period between the date of acquisition and the balance sheet date.

If the acquisition had been completed on 1 January 2008, total Group's turnover for the six months ended 30 June 2008 would remain unchanged and profit for the six months ended 30 June 2008 would have been increased by approximately HK\$7,624,000. The proforma information is for illustrative purposes only and is not necessarily an indication of revenue and results of operations of the Group that actually would have been achieved had the acquisition been completed on 1 January 2008, nor is it intended to be a projection of future results.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

18. ACQUISITIONS OF SUBSIDIARIES AND BUSINESS (Continued)

- (c) During the period, the Group acquired the entire assets and liabilities, the water supply business (the "Water Supply Business") and a shareholder's loan of approximately RMB24,814,000 (equivalent to HK\$26,857,000) from 儋州市自來水公司 at a consideration of approximately HK\$27,500,000. The amount of discount arising as a result of acquisition was approximately HK\$24,166,000.

The assets and liabilities arising from the acquisition are as follows:

	HK\$'000
Net assets acquired:	
Property, plant and equipment	138,415
Prepaid lease payments	14,620
Amount due from an associate	5,387
Inventories	958
Trade and other receivables	8,391
Bank balances and cash	510
Trade and other payables	(63,726)
Other loan	(23,652)
Bank and other borrowings	(29,031)
Loan from a shareholder	(26,857)
	25,015
Shareholder's loan	26,857
Discount on acquisition	(24,166)
Total consideration	27,706
Satisfy by:	
Cash	7,500
Deposit paid for acquisition of a business	20,000
Direct cost relating to the acquisition	206
	27,706
Net cash outflow arising on acquisition:	
Cash consideration paid	(7,500)
Direct costs relating to the acquisition	(206)
Bank balances and cash acquired	510
	(7,196)

The Water Supply Business contributed approximately HK\$829,000 loss to the Group's profit for the period between the date of acquisition and the balance sheet date.

If the acquisition had been completed on 1 January 2008, total Group's turnover for the six months ended 30 June 2008 would have been increased by approximately HK\$8,360,000 and profit for the six months ended 30 June 2008 would have been decreased by approximately HK\$124,000. The proforma information is for illustrative purposes only and is not necessarily an indication of revenue and results of operations of the Group that actually would have been achieved had the acquisition been completed on 1 January 2008, nor is it intended to be a projection of future results.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

18. ACQUISITIONS OF SUBSIDIARIES AND BUSINESS (Continued)

- (d) On 22 April 2008, the Group acquired additional 21.85% equity interests in an existing 29.15% held associate, Shangqiu Zhengyuan Water Industry Company Limited* ("Shangqiu Zhengyuan") (商丘市正源水務有限公司) for a consideration of approximately HK\$15,584,000. The acquisition has been accounted for using the purchase method. The amount of goodwill arising as a result of acquisition was approximately HK\$3,174,000.

The net assets acquired in the transaction and the goodwill arising are as follows:

	22 April 2008
	<i>HK\$'000</i>
Net assets acquired:	
Property, plant and equipment	206,932
Prepaid lease payments	32,427
Inventories	2,198
Trade and other receivables	41,677
Bank balances and cash	684
Trade and other payables	(102,052)
Bank and other borrowings	(147,003)
Minority interests	(17,083)
	17,780
Less: 29.15% equity interests acquired previously recognised as interest in an associate	(5,370)
	12,410
Goodwill	3,174
Total consideration	15,584
Satisfied by:	
Cash	15,584
Net cash outflow arising on acquisition:	
Cash consideration paid	(15,584)
Bank balances and cash acquired	684
	(14,900)

Shangqiu Zhengyuan contributed approximately HK\$2,185,000 loss to the Group's profit for the period between the date of acquisition and the balance sheet date.

If the acquisition had been completed on 1 January 2008, total Group's turnover for the six months ended 30 June 2008 would have been increased by approximately HK\$10,368,000 and profit for the six months ended 30 June 2008 would have been decreased by approximately HK\$9,895,000. The proforma information is for illustrative purposes only and is not necessarily an indication of revenue and results of operations of the Group that actually would have been achieved had the acquisition been completed on 1 January 2008, nor is it intended to be a projection of future results.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

For the six months ended 30 June 2008

19. SUBSEQUENT EVENTS

- (a) On 14 July 2008, China Water Industry (Hong Kong) Limited (“China Water (HK)”), an indirect wholly-owned subsidiary of the Company, entered into a letter of intent with Yunfu City Deyu Environment Protection Company Limited* (the “JV Partner”) (雲浮市德禹環保有限公司), pursuant to which China Water (HK) has agreed to form a joint venture company to engage in water supply and sewage treatment for urban areas in Yunfu City* (雲浮市). Upon the establishment of the joint venture company, it will be held as to not less than 51% by China Water (HK) and not more than 49% by the JV Partner.
- (b) On 12 August 2008, Swift Surplus Holdings Limited (“Swift Surplus”), a wholly-owned subsidiary of the Company, entered into an agreement with an independent third party, Ms. Yuen Tak Chun, pursuant to which the Swift Surplus has conditionally agreed to acquire the entire issued share capital and a shareholder’s loan with an amount of approximately HK\$159,849,000 of Affluent Boom Enterprises Limited (“Affluent Boom”) at a consideration of HK\$700,000,000. Affluent Boom is an investment holding company with its subsidiaries engaged in sewage treatment and water supply business in the PRC.
- (c) On 21 August 2008, the Company and Pacific Foundation Securities Limited (“Placing Agent”) entered into a placing agreement, pursuant to which the Placing Agent has agreed to place a maximum of 378,180,000 ordinary shares of HK\$0.1 each of the Company on a best effort basis, at a price of HK\$0.182 per share.
- (d) On 6 November 2007, the People’s Government of Danzhou City and Super Sino Investment Limited (“Super Sino”), an indirect wholly-owned subsidiary of the Company, entered into a net asset transfer agreement, pursuant to which the assets and liabilities of Danzhou City Water Company are transferred to Super Sino. Subsequent to the balance sheet date, Super Sino was notified that Agricultural Bank of China, Danzhou Branch filed a claim with the Intermediate People’s Court of Hainan against Danzhou City Water Company, Super Sino and the third party People’s Government of Danzhou for the repayment of the loan principal of RMB26 million and the interests arising therefrom from the defendants Danzhou City Water Company and Super Sino to the plaintiff. As advised by the Company’s solicitor, the borrowing contract lawsuit is under out-of-court negotiation and is expected to reach a settlement agreement to reduce the loan interests and extend the repayment period. The respective loan principal and the interest arising therefrom are included in 2008 interim report. The director of the Company believed that the lawsuit is unlikely to have material adverse financial impact on the Group.

MANAGEMENT DISCUSSION AND ANALYSIS

FINANCIAL PERFORMANCE

Financial Results

With the management's dedicated efforts to streamline the Group's businesses including computer peripherals and trading of watch and accessories and to focus on the development of water supply and sewage treatment operations, the Group's interim results achieved a remarkable turnaround from a loss of approximately HK\$65.05 million in the first-half of 2007 to a profit of approximately HK\$40.81 million in the first-half of 2008. This represented an increase of HK\$105.86 million as compared with the corresponding period. The improvement was attributable to many factors. Amongst them, the contribution from water supply segment made an eloquent appeal for the Group's strategic business development over the past two years. During the Interim Period, the segment of the provision of Water Supply and Sewage Treatment achieved a profit of HK\$11.01 million, which represented an increase of 1,421.13% comparing to the profit of HK\$0.72 million last year. Besides, iMerchants Limited ("iMerchants") (Stock Code: 8009), which the Group has acquired 84.98% equity interest during the period, has contributed HK\$7.63 million to the Group's consolidated results. The Group has also recognised a discount of HK\$24.17 million on acquisition of a business, in Danzhou City, and shared net profit of associated companies amounted to HK\$5.18 million. During the period, no share-based payment expenses has been accounted for as no share options has been granted, while HK\$40.43 million was recognized in previous interim period and no loss from the discontinued operation being recognized due to the disposal of loss-making business of production and sales of computer peripherals in last year. This interim results are well demonstrated the achievement and insight of the Group's strategy to diversify its business in the water industry sector in the PRC.

Turnover and Gross Profit

The Group's turnover and gross profit for the year 2008 was HK\$54.59 million and HK\$23.21 million respectively, which represented a growth of 105.81% in turnover and 1,474.36% in gross profit as compared with the corresponding interim period. The turnover and gross profit were solely contributed by those water supply and sewage treatment projects in the Mainland China which the Group has acquired in the last two years. Following the disposal of computer peripherals business and cessation of watch and accessories retail and wholesales businesses in last year, these two segments did not contributed any turnover and gross profit in this interim financial statements.

Other Income

Other operating income has increased by HK\$3.80 million to HK\$6.83 million. They were mainly bank interest income of HK\$1.93 million, net foreign exchange gain of HK\$1.07 million and gain on disposal on convertible notes receivable of HK\$1.33 million.

Discount on acquisition of water supply business and a shareholder's loan from Danzhou City Water Supply Company has been recognized in accordance with the Hong Kong Financial Reporting Standard 3. The acquisition cost was lower than the net fair value of the identifiable assets acquired. The discount of HK\$24.17 million was recognized in the income statement.

iMerchants, a GEM board listed subsidiary of the Company, contributed HK\$7.63 million to the Group's interim results. The operating income of iMerchants consisted of a net gain on disposal of debt securities of HK\$1.14 million, net fair value change on listed trading securities amounted to HK\$5.53 million, as well as an increase in fair values of financial assets of HK\$2.44 million.

MANAGEMENT DISCUSSION AND ANALYSIS *(Continued)*

FINANCIAL PERFORMANCE *(Continued)*

Other Expenses

Selling and distribution costs increased by 95.59% to HK\$3.10 million (2007: HK\$1.59 million). The increase in selling and distribution costs was due to several water plants and sewage treatment plants have been acquired and have commenced operation in 2008.

Finance cost increased sharply by HK\$2.70 million to HK\$2.72 million as compared with the corresponding period. The increase was mainly attributable to the interest expenses on convertible bonds of HK\$0.48 million and other loan interest of HK\$2.22 million.

Share of results from associates

For the interim period under review, the Group's acquired 35% equity interest in Jinan Hongquan Water Production Co., Limited* ("Jinan Water") (濟南泓泉制水有限公司). Share of post acquisition results of Jinan Water amounted to HK\$7.43 million has been taken up in this interim financial statements. The acquisition of Jinan Water was a major breakthrough for the Company to secure stake in a water supply enterprise of provincial level.

The Group share loss of HK2.25 million from another associate company, Shangqiu Zhengyuan Water Industry Company Limited* ("Shangqiu Zhengyuan") (商丘市正源水務有限公司). During the Interim Period, the Group has acquired additional 21.85% interest of Shangqiu Zhengyuan. Shangqiu Zhengyuan is now a subsidiary of the Group. It's financial results has been fully consolidated into the Group's financial statement since 22 April 2008, when the further acquisition was completed.

BUSINESS SEGMENTS REVIEW

Water Supply and Sewage Treatment Business in China

Entering 2008, the Group has been completely transforming its core business development on water supply and sewage treatment in the PRC after offloading the computer peripherals and discontinued investment in the watches and accessories businesses last year. At present, the Group has already acquired 7 water supply plants and 3 sewage treatment facilities in the PRC with the planned aggregate water supply capacity of 2,300,000 tonnes per day and the planned aggregate sewage treatment capacity of 100,000 tonnes per day respectively, which allows the Group's footprints in water supply and sewage treatment extended to cover Jiangxi Province, Anhui Province, Shandong Province, Henan Province and Hainan Province.

On top of its solid foundation in water business industry, the Group has further expansion its network to the Southern of the PRC by entering into the agreement to acquire 100% share capital of Affluent Boom Enterprises Limited ("Affluent Boom") on 12 August 2008. Affluent Boom held a large water service group currently operating 7 sewage treatment plants in Guangdong Province and Shaanxi Province and 1 water supply plant in Hebei Province with the aggregate sewage treatment capacity of 480,000 tonnes per day and the aggregate water supply capacity of 180,000 tonnes per day respectively. If the above capacity is added to the water supply capacity of 3,050,000 tonnes per day and sewage treatment capacity of 835,000 tonnes per day of projects with signed Letters of Intend, the total water supply capacity and sewage treatment capacity of the Group will reach daily 5,530,000 tonnes and 1,415,000 tonnes respectively. The Group is getting more closer and closer to its goal of attaining water supply capacity of 10,000,000 per day and sewage treatment capacity of 2,000,000 tonnes per day in 3 years.

MANAGEMENT DISCUSSION AND ANALYSIS (Continued)

BUSINESS SEGMENTS REVIEW (Continued)

Trading of Watches and Accessories Business

Following the closure of image shop last year, the management has discontinued investment in business of watches and accessories. At the date of this report, the management does not have any concrete plan of the exit policy.

LIQUIDITY AND FINANCIAL RESOURCES

As at 30 June 2008, the Group continues to be in a healthy financial position with cash and cash equivalents amount to HK\$157.07 million (compare with HK\$108.84 million on 31 December 2007). With the steady cash flows that are generated from the water supply segment and the existing available financial resources, the Group is in a very strong position to expand further in the PRC water supply industry.

Total borrowings of the Group as at 30 June 2008 are HK\$629.09 million (compare with HK\$431.84 million on 31 December 2007) comprising of the issuance of Convertible Bonds of HK\$325.41 million, bank and other borrowings HK\$211.25 million, interest free government loans of HK\$55.36 million and other borrowings HK\$37.07 million. The Convertible Bonds is denominated in HK dollars and loans are mainly denominated in Renminbi and the interest rates of which were fixed.

The Group's gearing ratio as at 30 June 2008 is 54.80% (compare with 42.95% on 31 December 2007), which is calculated by dividing total liabilities of HK\$861.33 million over total assets of the Group of HK\$1,571.89 million.

At the period end, the net current assets of the Group is HK\$64.08 million (compare with the net current assets of HK\$132.88 million on 31 December 2007) and the current ratio of the Group was approximately 1.24 times (compare with 4.33 times on 31 December 2007).

CAPITAL RAISING AND USE OF PROCEEDS

The Company has not conducted any equity fund raising activities during the interim period. Subsequent to the interim period, the Company and Pacific Foundation Securities Limited ("Placing Agent") entered into a placing agreement on 21 August 2008, pursuant to which the Placing Agent has agreed to place a maximum of 378,180,000 shares at a price of HK\$0.182 per share, on a best effort basis. The placement has not been completed as of the report date.

As of the balance sheet date, the Group's capital expenditure amounted to HK\$48.72 million (compare with HK\$677.70 million on 31 December 2007). The expenditure is mainly on the strategic acquisitions for investing in water supply and sewage treatment projects in the PRC, the remaining balance of HK\$147.45 million being placed in bank. The unutilized amounts will continue to be invested in the committed projects.

FOREIGN EXCHANGE RISK

The Group's exposure to foreign exchange risk is minimal as most of the Group's subsidiaries operate in the PRC and most of transactions, assets and liabilities are denominated in Renminbi. Accordingly, the Group does not have derivative financial instruments to hedge its foreign currency risks.

CAPITAL COMMITMENTS

As at 30 June 2008, the Group has the capital commitments contracted but not provided for acquisition of property, plant and equipment approximately HK\$0.21 million and addition capital injection in of a subsidiary HK\$29.27 million (2007: HK\$25.56 million).

MANAGEMENT DISCUSSION AND ANALYSIS (Continued)

EMPLOYEES AND REMUNERATION POLICES

As at 30 June 2008, the Group had approximately 2,338 full-time employees (2007: 2,200 full-time employees). Most of them station in the PRC while the remaining in Hong Kong. The remuneration package of the employees is determined by various factors including the employees' experience and performance, the market condition, industry practice and applicable employment law.

STRATEGIC INVESTMENT DURING THE PERIOD UNDER REVIEW

During the reviewing period, the Group had entered into/completed the following acquisitions and letter of intend:

Acquisition of Subsidiaries and Business

On 3 July 2007, the China Water Industry (HK) Limited ("China Water (HK)"), an indirect wholly-owned subsidiary of the Company, entered into an agreement with Huge Summit Management Limited, pursuant to which China Water (HK) and Huge Summit have agreed to sell and purchase the entire issued share capital of Longwide Investment Limited ("Longwide") at a consideration of RMB67.5 million. Longwide is an investment holding company holding 51% equity interests in each of Shangqiu Zhengyuan Water Industry Company Limited* ("Shangqiu Zhengyuan") (商丘市正源水務有限公司) and Linyi Ganghua Water Industry Company Limited* (臨沂港華水務有限公司); The acquisition of Linyi Ganghua Water Industry Company Limited was completed in 2007, whereas Shangqiu Zhengyuan was acquired as an associate in 2007. On 22 April 2008, China Water (HK) acquired additional 21.85% equity interests in an existing 29.15% held in Shangqiu to become subsidiary.

On 6 November 2007, Super Sino Investment Limited ("Super Sino"), an indirect wholly-owned subsidiary of the Company, entered into a net asset transfer agreement with the People's Government of Danzhou City, Hainan Province to purchase 49% equity interest in Danzhou Water Pipe, other assets and liabilities and a shareholder's loan of Danzhou City Water Company* (儋州市自來水公司) for a consideration of RMB25.3 million. The transaction has been completed on 21 February 2008.

On 26 November 2007, Smart Giant Group Limited ("Smart Giant"), a direct wholly-owned subsidiary of the Company, entered into an agreement with Mega Mount Group Limited, to acquire the entire share capital and a shareholder's loan of Blue Mountain Hong Kong Group Limited ("Blue Mountain") for an aggregate consideration of HK\$230 million. Blue Mountain is an investment holding company and its sole asset is the 35% equity interest in Jinan Water. The transaction was completed on 18 January 2008.

On 1 December 2007, the Bonus Raider Investments Limited ("Bonus Raider"), a direct wholly-owned subsidiary of the Company, entered into an agreement to acquire approximately 67.32% equity interest of iMerchants at an aggregate consideration of approximately HK\$198 million. The transaction was completed on 14 February 2008. Owing to the acquisition triggered the Takeover Code, the Group is required to make an unconditional mandatory general cash offer for all the issued shares of iMerchants. On 13 March 2008, the Group held approximately 90.68% of iMerchants' issued share capital which was exceeding the minimum 15% of public float requirement under the GEM rules. On 14 April 2008, the Group entered into placing agreement to dispose 6.28% interest in iMerchants. As at the reporting date, the Group held approximately 84.98% interest of issued share capital in iMerchants.

On 4 February 2008, China Water (HK) entered into a JV Agreement with Yingtan Water Supply Company* (the "JV Partner") (鷹潭市供水公司), a state-owned enterprise incorporated in the PRC and subordinated to Construction Bureau of Yingtan City* (鷹潭市建設局), to establish the JV Company named Yingtan Water Company Limited* (鷹潭市水業有限公司) with the JV Partner to principally engage in water supply plants to urban areas in Yingtan City in Jiangxi Province of the PRC. The aggregate water supply capacities of JV Company are 100,000 tonnes per day. The acquisition has not been completed at the date of this report.

MANAGEMENT DISCUSSION AND ANALYSIS (Continued)

STRATEGIC INVESTMENT DURING THE PERIOD UNDER REVIEW (Continued)

Acquisition of Subsidiaries and Business (Continued)

On 26 May 2008, Shine Gain Holdings Limited, a wholly-owned subsidiary of the iMerchants entered into the Sales and Purchase Agreement with Da Luz, Sergio Augusto Josue Junior to acquire the entire issued share capital of Plenty One Limited for an aggregate consideration of HK\$55 million, which directly holds 80% equity interest in Ping Xiang City San He Lian Chuang Water Technology Company Limited (萍鄉市三和聯創水務科技有限公司). The transaction was completed on 12 August 2008.

On 6 November 2007, Super Sino entered into a share transfer agreement with Hainan Nanshenghe Company Limited* (海南南聖河有限公司) to purchase 51% equity interest in and the shareholder's loan due by Danzhou Lian Shun Tong Water Pipe Company Limited* ("Danzhou Water Pipe") (儋州聯順通自來水管網有限公司) for a consideration of RMB8.68 million. The acquisition has not been completed at the date of this report.

Letter of Intent

On 16 June 2008, China Water (HK) entered into a letter of intent with Stated-owned Assets Supervisory Committee of Geermu Municipal Government* (the "JV Partner") (格爾木市政府國有資產監督委員會), pursuant to which China Water (HK) has agreed to form a joint venture company (the "JV Company") with the JV Partner to principally engage in the water supply and sewage treatment for Geermu City* (格爾木市) in Qinghai Province (青海省) of the PRC. Upon the establishment of the JV Company, it will be held as to 80% by China Water (HK) and 20% by the JV Partner. The term of operation of the JV Company shall be 30 years.

On 26 June 2008, China Water (HK) entered into a letter of intent with Shenyang Water Development Limited* (the "JV Partner") (瀋陽水務發展有限公司), pursuant to which China Water (HK) has agreed to form a joint venture company (the "JV Company") with the JV Partner to principally engage in the water supply projects in Changbai District* (長白地區), Hutai New City* (胡台新城), Qipan Hill* (棋盤山), Huanggu Northern Industrial Zone* (皇姑北部工業園), Sujiatun District* (蘇家屯區) and Shenyang Northern Development Zone* (瀋北開發區) in Shenyang City (瀋陽市) of the PRC. The estimated aggregate water supply capacity of the JV Company is 120,000 tones per day. Upon the establishment of the JV Company, it will be held as to 50% by China Water (HK) and 50% by the JV Partner.

PENDING LITIGATION

(i) Technostore Limited, a subsidiary of the Company

On 30 May 2007, a Petition was filed under sections 168A and 177 of the Company Ordinance (Cap. 32) to wind-up Technostore Limited ("Technostore"), a company in which the Company held 50.01% of the issued shares. The Petition was commenced by Mao Chi Fai ("Petitioner"), the minority shareholder of Technostore holding 49.99% of the issued shares.

Following court hearings regarding the winding-up proceeding in preceding year, on 29 August 2008, the court has made an order to appoint Kenny Tam & Company, Certified Public Accountant as an liquidator of Technostore and Happy Hours Limited and Mao Chi Fai as members in the committee of inspection. The matter is still in the liquidation process and is handled by Official Receiver's Office. The directors of the Company believe that no material future outflows resources from the Group is expected and sufficient provision on assets related to Technostore have been provided. It is unlikely to have material adverse financial impact on the Group.

MANAGEMENT DISCUSSION AND ANALYSIS *(Continued)*

PENDING LITIGATION *(Continued)*

(ii) **Super Sino Investment Limited, an indirect wholly-owned subsidiary of the Company**

On 6 November 2007, the People's Government of Danzhou City and Super Sino Investment Limited ("Super Sino") an indirect wholly-owned subsidiary of the Company, entered into a net asset transfer agreement, pursuant to which the assets and liabilities of Danzhou City Water Company are transferred to Super Sino. Subsequent to the balance sheet date, Super Sino was notified that Agricultural Bank of China, Danzhou Branch filed a claim with the Intermediate People's Court of Hainan against Danzhou City Water Company, Super Sino and the third party People's Government of Danzhou for the repayment of the loan principal of RMB26 million and the interests arising therefrom from the defendants Danzhou City Water Company and Super Sino to the plaintiff. As advised by the Company's solicitor, the borrowing contract lawsuit is under out-of-court negotiation and is expected to reach a settlement agreement to reduce the loan interests and extend the repayment period. The respective loan principal and the interest arising therefrom are included in 2008 interim report. The director of the Company believed that the lawsuit is unlikely to have material adverse financial impact on the Group.

Save and except for this, the Company is not aware of any other significant proceedings instituted against the Company.

PROSPECTS

Following the business realignment over the past two years, the Group has completely discontinued the production of computer peripherals and the sales of high-end watches and accessories and focused its resources on expanding the water industry related investments and operations in order to become a specialized water investment corporation, which focuses on expanding its water supply, sewage treatment and water related businesses in China.

The Board of the Group believes that with the fast-growing economy of China and the acceleration of large-scale urbanization and industrialization, the investment demand for water business in China will grow significantly. There is huge appreciation potential for the value of city water. As the overall water sector becomes more open and the operating standards of the market economy are fully complied with, tremendous business opportunities have emerged. As the pioneer in the industry, it is certain that the Group is able to reap fruitful returns arising therefrom.

For city water supply, the Group has completed the reform and consolidation of the previously acquired water supply enterprises, including organizational integration and operational system conversion, and recorded operating achievements. Meanwhile, the Group has entered into a letter of intent with certain middle-to-large cities so as to complete the construction and the acquisition of a number of water enterprises by phases, thus significantly expanding the water supply of the Group.

For city sewage treatment, a number of sewage treatment plants previously invested by the Group have been completed and have commenced production. Such plants are operating smoothly and have begun to achieve operating efficiency. The Group plans to increase its investments in the sewage treatment and reclaimed water reuse businesses so as to enjoy various preferential treatments promulgated by the PRC government in respect of the sewage treatment sector.

Apart from business expansion which focuses on the investment in the middle-to-large cities, the Group has begun to consider the acquisition of water investment and operation enterprises in China in order to quickly expand the size and profitability of the Group's city water supply and sewage treatment businesses. Meanwhile, the Group also considers the acquisition or construction of water services engineering entities, improve the Group's water sector structure as well as expand the revenue base of the Group's water business.

The directors of the Group believe that, leverage on the consolidation of the existing water enterprises and the fast expansion of business size, the Group is determined to achieve the stated objective as a large-scale water enterprise to become a leading water investment and operation enterprise in the water industry in China, and generate attractive returns to its shareholders and general investors.

SUPPLEMENTARY INFORMATION

INTERIM DIVIDENDS

The Board does not recommend payment of interim dividend for the six months ended 30 June 2008 (six months ended 30 June 2007: Nil).

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS IN SECURITIES

As at 30 June 2008, the interests and short positions of the Directors and Chief Executive of the Company, or their associates in the shares, underlying shares and debentures of the Company and 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 had been 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 in which they were deemed or taken to have under such provisions of the SFO) or which were required pursuant to the Model Code for Securities Transactions by Directors of Listed Companies (the "Model Code") contained in the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules"), to be notified to Company and the Stock Exchange were as follows:

(i) Interest in the Shares

Name of director	Nature of interest	Number of issued ordinary shares held	Total interest	Percentage of the issued share capital of the Company
Sze Chun Ning, Vincent	Interest in controlled corporation (<i>Note</i>)	55,000,000	55,000,000 (L)	2.91%
	Beneficial owner	1,008,000	1,008,000 (L)	0.05%
Chu Yin Yin, Georgiana	Beneficial owner	6,432,000	6,432,000 (L)	0.39%

For the purpose of this section, the shareholding percentage in the Company is calculated on the basis of 1,890,900,000 Shares in issue as at 30 June 2008.

The letter "L" denotes a long position in shares of the Company.

Note: These Shares are held by Sure Ability Limited, a company beneficially wholly-owned with sole directorship by Mr. Sze Chun Ning, Vincent.

SUPPLEMENTARY INFORMATION *(Continued)*

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS IN SECURITIES *(Continued)*

(ii) Interest in Underlying Shares

Name of director	Exercise price <i>HK\$</i>	Exercise period	Number of underlying Shares (under share options of the Company)	Approximate shareholding % <i>(Note)</i>
Sze Chun Ning, Vincent	0.335	11 January 2007 to 10 January 2017	10,000,000	0.53%
Chu Yin Yin, Georgiana	0.335	11 January 2007 to 10 January 2017	3,000,000	0.16%
Liu Bai Yue	0.420	17 January 2007 to 16 January 2017	5,000,000	0.26%

Note: For the purpose of this section, the shareholding percentage in the Company is calculated on the basis of 1,890,900,000 Shares in issue as at 30 June 2008.

Save as disclosed above, as at 30 June 2008, none of the Directors or Chief Executive of the Company had any interest or short position in any shares, underlying shares or debenture of the Company or any of its associated corporations (as defined in Part XV of the SFO) which are 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 which they were taken or deemed to have under SFO) or were recorded in the register required to be kept by the Company under Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code.

SUPPLEMENTARY INFORMATION *(Continued)*

SUBSTANTIAL SHAREHOLDERS

As at 30 June 2008, as far as known to the Directors or Chief Executive of the Company, the following persons (other than a Director or Chief Executive of the Company disclosed under the section "Directors' and Chief Executive's interests in Securities" above) had an interest in the shares and underlying shares of the Company which would fall to be disclosed to the company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO, or who was directly or indirectly interested in 10% or more of the nominal value of any class of Shares carrying rights to vote in all circumstances at general meetings of the Company or any other member of the Group:

Name of shareholder	Capacity	Number of issued Shares held	Approximate percentage of the issued share capital of the Company
Qu Xiao Sheng	Beneficial owner	310,150,000 <i>(Note 1)</i>	16.40%
Abax Arhat Fund	Interest of controlled corporation	228,873,239 <i>(Note 2)</i>	12.10%
Abax Claremont Limited	Interest of controlled corporation	228,873,239 <i>(Note 2)</i>	12.10%
Abax Global Capital	Interest of controlled corporation	228,873,239 <i>(Note 2)</i>	12.10%
Abax Global Opportunities Fund	Interest of controlled corporation	228,873,239 <i>(Note 2)</i>	12.10%
Abax Upland Fund, LLC	Interest of controlled corporation	228,873,239 <i>(Note 2)</i>	12.10%
Abax Lotus Limited	Beneficial owner	228,873,239 <i>(Note 2)</i>	12.10%
Ward Ferry Management (BVI) Limited	Investment Manager	132,092,000	6.99%

Note 1: These Shares are held by Boost Skill Investments Limited (as to 180,000,000 Shares) and Favor Jumbo Investments Limited (as to 130,150,000 Shares), each of which is wholly and beneficially owned by Mr. Qu Xiao Sheng who, after becoming a substantial shareholder on 17 March 2008, does not hold any position in the Group.

Note 2: These 228,873,239 underlying Shares are those Shares which would be issued upon exercise of the convertible rights attaching to the convertible bonds issued by the Company as disclosed in the announcement of the Company dated 31 July 2007. As the issued share capital of Abax Lotus Limited is held indirectly or directly by Abax Arhat Fund, Abax Claremont Limited, Abax Global Capital, Abax Global Opportunities Fund and Abax Upland Fund, LLC, they are deemed to be interested in the underlying Shares under SFO.

Note 3: For the purpose of this section, the shareholding percentage in the Company is calculated on the basis of 1,890,900,000 Shares in issue as at 30 June 2008.

SUPPLEMENTARY INFORMATION *(Continued)*

SUBSTANTIAL SHAREHOLDERS *(Continued)*

Save as disclosed herein, there is no person known to the Directors or Chief Executive of the Company, no other person (other than a Director or Chief Executive of the Company), who, as at 30 June 2008, had an interest or short position in the Shares and underlying Shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or who was directly or indirectly interested in 10% or more of the normal value of any class of shares carrying rights to vote in all circumstances at general of the Company or any other members of the group and none of the Directors held any directorship or employment in a company which has an interest or short position in the Shares and underlying Shares which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO.

SHARE OPTION SCHEME

The Company had adopted share option scheme on 17 January 2002 (the "Scheme"). During the six months ended 30 June 2008, no shares options were granted by the Company. Other than the said share option scheme, the Company and its subsidiaries have not adopted any share option scheme. Details of the movements in the share options during the period ended 30 June 2008 under the Scheme are as follows:

Name or category of participant	Date of grant	Outstanding as at 1 January 2008	Granted during the year	Exercised during the year	Lapsed during the year	Outstanding as at 30 June 2008	Exercisable period	Exercise price per share of the Company HK\$
Directors								
Sze Chun Ning, Vincent	11 January 2007	10,000,000	-	-	-	10,000,000	11 January 2007 to 10 January 2017	0.335
Chu Yin Yin, Georgiana	11 January 2007	3,000,000	-	-	-	3,000,000	11 January 2007 to 10 January 2017	0.335
Liu Bai Yue	17 January 2007	5,000,000	-	-	-	5,000,000	17 January 2007 to 16 January 2017	0.420
Total as at 30 June 2008		18,000,000	-	-	-	18,000,000		

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S SECURITIES

During the six months ended 30 June 2008, the Company had not redeemed, and neither the Company nor any of its subsidiaries had purchased or sold any of the Company's listed securities.

SUPPLEMENTARY INFORMATION *(Continued)*

CORPORATE GOVERNANCE PRACTICES

The Group recognizes the importance of transparency and accountability to shareholders. The Board will continually review and enhance its corporate governance practices to ensure that they meet shareholders' expectation and comply with relevant standards.

During the six months ended 30 June 2008, the corporate governance practices adopted by the Company has complied with the code provisions set out in the Code of Corporate Governance Practices contained in Appendix 14 of the Listing Rules (the "CGP Code") except for the deviations from the following provisions of the CGP Code:

1. Code provision A4.1 stipulates that non-executive Directors should be appointed for a specific term. However, none of the existing non-executive Directors of the Company (including independent non-executive) is appointed for a specific term since all non-executive Directors of the Company (including independent non-executive) are subject to retirement by rotation and re-election at annual general meetings of the Company in line with the Company's Articles of Association. The Company considers that sufficient measures have been taken to ensure that the Company's corporate governance practices are no less exacting than those in the CGP Code.

MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 to the Listing Rules as its own Code of Conduct regarding securities transactions by the Directors of the Company. All Directors have confirmed that they have complied with the required standard set out in the Model Code throughout the six months ended 30 June 2008.

AUDIT COMMITTEE

The Audit Committee comprises three independent non-executive Directors of the Company, has reviewed with the management of the Company the accounting principles and practices adopted by the Group and discussed auditing internal controls and financial reporting matters including the review of the unaudited interim financial statements for the six months ended 30 June 2008.

REMUNERATION COMMITTEE

The Remuneration Committee comprises two independent non-executive Directors of the Company and one executive Director of the Company, is responsibility for reviewing and evaluating the remuneration polices of executive directors and senior management and making recommendations to the Board from time to time.

SUPPLEMENTARY INFORMATION *(Continued)*

PUBLICATION OF THE INTERIM RESULTS AND REPORT

This interim results announcement is published on the websites of the Company (www.chinawaterind.com) and Hong Kong Exchanges and Clearing Limited (<http://www.hkex.com.hk>). The interim report of the Company for 2008 containing all information required by the Listing Rules will be dispatched to Shareholders and made available on the above websites in due course.

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.

By order of the Board

China Water Industry Group Limited

Li Yu Gui

Chairman

Hong Kong, 26 September 2008

* *For identification purposes only*