



China Zenith Chemical Group Limited

中國天化工集團有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 362)



Interim Report
2008/2009

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Corporate Information

Board of Directors

Executive Directors

Mr. Chan Yuen Tung
Ms. Chan Yuk Foebe
Mr. Peng Zhanrong
Mr. Chiau Che Kong
Mr. Wu Jianwei

Independent Non-executive Directors

Mr. Ma Wing Yun Bryan
Mr. Yau Chung Hong
Mr. Tam Ching Ho
Dato' Dr. Wong Sin Just

Company Secretary

Mr. Tsang Chiu Hung

Registered Office

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Cayman Islands

Head Office and Principal Place of Business in Hong Kong

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Hong Kong

Authorised Representatives

Ms. Chan Yuk Foebe
Mr. Chiau Che Kong

Auditor

RSM Nelson Wheeler
Certified Public Accountants
29/F., Caroline Centre
Lee Gardens Two
28 Yun Ping Road
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Legal Advisers to the Company

Huen Wong & Co. in association with
Fried, Frank, Harris, Shriver & Jacobson LLP
9/F Gloucester Tower
The Landmark
15 Queen's Road Central
Hong Kong

Principal Bankers

Hang Seng Bank Limited
83 Des Voeux Road Central
Central
Hong Kong

Standard Chartered Bank
Shop A25–A27, Ground Floor
Kwai Chung Plaza
Hong Kong

Industrial And Commercial Bank of China
No. 155 Xisan Tiao Road
Mudanjiang City
Heilongjiang Province
PRC

Principal Share Registrar and Transfer Office

Bank of Bermuda (Cayman) Limited
P.O. Box 513 G.T.
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North Church Street
George Town
Grand Cayman
Cayman Islands
British West Indies

Hong Kong Branch Share Registrar and Transfer Office

Tricor Tengis Limited
26/F., Tesbury Centre
28 Queen's Road East
Hong Kong

Stock Code: 00362

Financial Highlights

	Six months ended 31 December		Change
	2008 <i>HK\$'000</i>	2007 <i>HK\$'000</i>	
TURNOVER	600,161	851,252	(29.5%)
PROFIT FOR THE PERIOD ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY	43,072	156,784	(72.5%)
BASIC EARNINGS PER SHARE	HK\$1.2 cents	HK\$4.4 cents	(72.7%)
INTERIM DIVIDEND PER SHARE	–	–	–

The Board of Directors (“Board” or “Directors”) of China Zenith Chemical Group Limited (the “Company”) is pleased to announce the unaudited condensed consolidated interim financial statements (“Interim Financial Statements”) of the Company and its subsidiaries (collectively the “Group”) for the six months ended 31 December 2008 (“Period”). The results had been reviewed by the Company’s audit committee (“Audit Committee”).

Condensed Consolidated Income Statement

		Unaudited six months ended 31 December	
	<i>Note</i>	2008 HK\$'000	2007 HK\$'000 (Restated)
TURNOVER	3	600,161	851,252
Cost of sales		(478,710)	(598,864)
Gross profit		121,451	252,388
Other income		15,535	15,076
Selling and distribution costs		(9,421)	(18,116)
Administrative expenses		(35,857)	(66,595)
Other operating expenses		(15,845)	(13,590)
PROFIT FROM OPERATIONS		75,863	169,163
Finance costs		(2,977)	(497)
PROFIT BEFORE TAX		72,886	168,666
Income tax (expense)/credit	5	(15,338)	22,408
PROFIT FOR THE PERIOD	6	57,548	191,074
ATTRIBUTABLE TO:			
Equity holders of the Company		43,072	156,784
Minority interests		14,476	34,290
		57,548	191,074
EARNINGS PER SHARE	7		
– Basic		HK1.2 cents	HK4.4 cents
– Diluted		HK1.2 cents	HK4.3 cents

Condensed Consolidated Balance Sheet

Note	Unaudited 31 December 2008 HK\$'000	Audited 30 June 2008 HK\$'000
Non-current assets		
	1,350,405	1,165,441
Fixed assets		
	359,446	363,087
Prepaid land leases payments		
	111,735	111,735
Goodwill		
	109,918	113,027
Other intangible assets		
	3,294	3,309
Deferred tax assets		
	1,934,798	1,756,599
Current assets		
	54,685	103,874
Inventories		
	516,758	401,819
Trade receivables	9	
Prepayments, deposits and other receivables		
	8,520	21,324
Financial assets at fair value through profit and loss		
Bank and cash balances		
	36,814	56,217
	779,299	887,147
TOTAL ASSETS	2,714,097	2,643,746
EQUITY		
	37,409	37,409
Capital and reserves		
	846,977	803,905
Issued capital	10	
Retained profits		
	1,227,992	1,232,545
Other reserves		
Equity attributable to equity holders of the Company	2,112,378	2,073,859
Minority interests	177,825	164,156
Total equity	2,290,203	2,238,015

Condensed Consolidated Balance Sheet (continued)

Note	Unaudited 31 December 2008 HK\$'000	Audited 30 June 2008 HK\$'000
Non-current liabilities		
11	46,480	47,558
	141,342	141,154
	187,822	188,712
Current liabilities		
12	46,763	29,386
	124,777	146,515
11	57,459	30,398
	7,073	10,720
	236,072	217,019
Total liabilities	423,894	405,731
Total equity and liabilities	2,714,097	2,643,746
Net current assets	543,227	670,128
Total assets less current liabilities	2,478,025	2,426,727

Condensed Consolidated Statement of Changes in Equity

For the six months ended 31 December 2008 – Unaudited

	Attributable to equity holders of the Company								Total HK\$'000
	Issued share capital HK\$'000	Share premium account HK\$'000	Fixed asset revaluation reserve HK\$'000	Share option reserve HK\$'000	Exchange reserve HK\$'000	Retained profits HK\$'000	Sub-total HK\$'000	Minority interests HK\$'000	
At 1 July 2008	37,409	1,064,852	27,545	17,008	123,140	803,905	2,073,859	164,156	2,238,015
Profit for the period	-	-	-	-	-	43,072	43,072	14,476	57,548
Translation difference	-	-	-	-	(4,553)	-	(4,553)	(807)	(5,360)
At 31 December 2008	37,409	1,064,852	27,545	17,008	118,587	846,977	2,112,378	177,825	2,290,203

For the six months ended 31 December 2007 – Unaudited

	Attributable to equity holders of the Company								Total HK\$'000
	Issued share capital HK\$'000	Share premium account HK\$'000	Fixed asset revaluation reserve HK\$'000	Share option reserve HK\$'000	Exchange reserve HK\$'000	Retained profits HK\$'000	Sub-total HK\$'000	Minority interests HK\$'000	
At 1 July 2007	33,778	887,480	11,929	-	33,419	536,796	1,503,402	240,777	1,744,179
Profit for the period	-	-	-	-	-	156,784	156,784	34,290	191,074
Share option benefits									
- Grant of share options	-	-	-	26,934	-	-	26,934	-	26,934
- Exercise of share options	824	47,133	-	-	-	-	47,957	-	47,957
- Transfer to share premium	-	7,680	-	(7,680)	-	-	-	-	-
Issue of shares	1,749	73,436	-	-	-	-	75,185	-	75,185
Translation difference	-	-	-	-	25,537	-	25,537	6,379	31,916
At 31 December 2007	36,351	1,015,729	11,929	19,254	58,956	693,580	1,835,799	281,446	2,117,245

Condensed Consolidated Cash Flow Statement

	Unaudited six months ended 31 December	
	2008 HK\$'000	2007 HK\$'000
NET CASH INFLOW FROM OPERATING ACTIVITIES	32,881	94,056
NET CASH OUTFLOW FROM INVESTING ACTIVITIES	(75,439)	(167,260)
NET CASH INFLOW FROM FINANCING ACTIVITIES	26,111	123,142
NET (DECREASE)/INCREASE IN CASH AND CASH EQUIVALENTS	(16,447)	49,938
EFFECT OF FOREIGN EXCHANGE RATE CHANGES	(2,956)	1,948
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF PERIOD	56,217	170,047
CASH AND CASH EQUIVALENTS AT THE END OF PERIOD	36,814	221,933
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS		
Bank and cash balances	36,814	221,933

Notes to Condensed Consolidated Financial Statements

1. Basis of Preparation and Accounting Policies

This Interim Financial Statements was prepared in accordance with Hong Kong Accounting Standard 34 "Interim Financial Reporting" which is one of the Hong Kong Financial Reporting Standards ("HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants and the applicable disclosure requirements of Appendix 16 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

These condensed consolidated financial statements should be read in conjunction in with the 2008 annual financial statements of the Group.

The accounting policies and methods of computation used in the preparation of these condensed consolidated financial statements are consistent with those used in the 2008 annual financial statements of the Group.

2. Changes in Accounting Policies

In the Period, the Group has adopted all the new and revised HKFRSs that are relevant to its operations and effective for accounting period beginning on 1 July 2008. HKFRSs comprise Hong Kong Financial Reporting Standards ("HKFRS"); Hong Kong Accounting Standards; and Interpretations. The adoption of these new and revised HKFRSs did not result in substantial changes to the Group's accounting policies and amounts reported for the current and prior periods.

The Group has not applied the new HKFRSs that have been issued but are not yet effective. The Group has already commenced an assessment of the impact of these new HKFRSs but is not yet in a position to state whether these new HKFRSs would have a material impact on its results of operations and financial position.

3. Turnover

Turnover represents the net invoiced value of goods sold, after allowances for returns and trade discounts, and after eliminations of all significant intra-group transactions during the Period.

Notes to Condensed Consolidated Financial Statements (continued)

4. Segment Information

Segment information is presented by way of two segment formats: (i) on a primary segment reporting basis, by business segment; and (ii) on a secondary segment reporting basis, by geographical segment.

The Group's operating businesses are structured and managed separately, according to the nature of their operations and the products they provide. Each of the Group's business segments represents a strategic business unit that offers products which are subject to risks and returns that are different from those of the other business segments.

In determining the Group's geographical segments, revenues are attributed to the segments based on the location of the customers.

(i) Business segments

	Polyvinyl- chloride <i>HK\$'000</i>	Vinyl acetate <i>HK\$'000</i>	Heat and power <i>HK\$'000</i>	Glucose and starch <i>HK\$'000</i>	Elimin- ations <i>HK\$'000</i>	Sub-total <i>HK\$'000</i>
Six months 31 December 2008						
Segment revenue	367,920	192,276	36,239	12,009	(8,283)	600,161
Segment results	77,472	47,917	(10,653)	(16,395)	–	98,341
Other income						1,197
Unallocated expenses						(23,675)
Consolidated profit from operations						75,863
Finance costs						(2,977)
Consolidated profit before tax						72,886
Income tax expense						(15,338)
Consolidated profit for the period						57,548

Notes to Condensed Consolidated Financial Statements (continued)

4. Segment Information (Cont'd)**(i) Business segments (Cont'd)**

	Polyvinyl- chloride <i>HK\$'000</i>	Vinyl acetate <i>HK\$'000</i>	Heat and power <i>HK\$'000</i>	Glucose and starch <i>HK\$'000</i>	Elimin- ations <i>HK\$'000</i>	Total <i>HK\$'000</i>
Six months 31 December 2007						
Segment revenue	445,498	223,509	50,703	151,219	(19,677)	851,252
Segment results	130,435	71,139	4,953	1,795	(773)	207,549
Other income						8,741
Unallocated expenses						(47,127)
Consolidated profit from operations						169,163
Finance costs						(497)
Consolidated profit before tax						168,666
Income tax credit						22,408
Consolidated profit for the period						191,074

Unallocated expenses represent corporate expenses.

(ii) Geographical segments

Over 90% of the Group's revenue and assets are derived from customers and operations based in the People's Republic of China (the "PRC" or "China") and accordingly, no further analysis of the Group's geographical segments is disclosed.

Notes to Condensed Consolidated Financial Statements (continued)

5. Income tax (expense)/credit

	Six months ended	
	31 December	
	2008	2007
	HK\$'000	HK\$'000
Current Period provision:		
Elsewhere in the PRC	15,338	7,014
Deferred tax	–	(29,422)
	15,338	(22,408)

No provision for Hong Kong Profits Tax has been made as the Group did not generate any assessable profits arising in Hong Kong during the Period (2007: Nil). Tax charge on profits assessable elsewhere have been calculated at the rates of tax prevailing in the countries in which the Group operates, based on existing legislation, interpretation and practices in respect thereof.

6. Profit for the Period

The Group's profit for the Period is stated at after charging/(crediting):

	Six months ended	
	31 December	
	2008	2007
	HK\$'000	HK\$'000
Depreciation	23,416	14,020
Amortisation of other intangible assets	3,053	2,775
Interest income	(200)	(2,801)
Allowance for receivables	4,400	10,000
Write-off of fixed assets	2,384	2,873
Gain on disposal of financial assets at fair value through profit and loss (held for trading)	–	(5,927)
Fair value loss on financial assets at fair value through profit and loss (held for trading)	12,804	9,939
Staff cost (including directors' remuneration):		
Wages, salaries and benefits in kinds	15,477	17,848
Employee share option benefits	–	26,934
Retirement benefits scheme contribution	2,488	1,713

Notes to Condensed Consolidated Financial Statements (continued)

7. Earnings Per Share

Basic earnings per share

The calculation of basic earnings per share attributable to equity holders of the Company is based on the profit for the Period attributable to equity holders of the Company of approximately HK\$43,072,000 (2007: HK\$156,784,000) and the weighted average number of ordinary shares of 3,740,887,824 (2007: 3,561,337,375) in issue during the Period.

Diluted earnings per share

The calculation of diluted earnings per share attributable to equity holders of the Company is based on the profit for the Period attributable to equity holders of the Company of approximately HK\$43,072,000 (2007: HK\$156,784,000) and the weighted average number of ordinary shares of 3,740,887,824 (2007: 3,561,337,375) in issue during the Period used in the basic earnings per share calculation plus the weighted average number of ordinary shares of nil (2007: 65,419,010) assumed to have been issued at no consideration on the deemed exercise of the share options and warrants outstanding at the balance sheet date.

8. Capital Expenditure

During the Period, the additions to fixed assets including the construction in progress in the PRC were approximately HK\$75.4 million (2007: HK\$136.2 million).

Notes to Condensed Consolidated Financial Statements (continued)

9. Trade Receivables

The Group's trading terms with customers are mainly on credit. The credit terms generally range from 30 to 150 days. The Group seeks to maintain strict control over its outstanding receivables. Overdue balances are reviewed regularly by the management.

The ageing analysis of trade receivables, based on the invoice date, and net of allowance, is as follows:

	31 December 2008 HK\$'000	30 June 2008 HK\$'000
Within 30 days	105,108	102,990
31 to 60 days	89,277	111,542
61 to 90 days	95,196	66,297
91 to 120 days	77,207	27,412
121 to 150 days	56,492	18,532
151 to 180 days	38,436	18,099
181 to 240 days	29,449	22,893
241 to 330 days	21,762	30,223
331 to 365 days	3,831	3,484
Over 365 days	–	347
	516,758	401,819

**10. Share Capital
Shares**

	31 December 2008 HK\$'000	30 June 2008 HK\$'000
Authorised:		
10,000,000,000 (30 June 2008: 10,000,000,000) ordinary shares of HK\$0.01 each	100,000	100,000
Issued and fully paid:		
3,740,887,824 (30 June 2008: 3,740,887,824) ordinary shares of HK\$0.01 each	37,409	37,409

Notes to Condensed Consolidated Financial Statements (continued)

11. Bank Loans

The Group's bank loans are repayable as follows:

	31 December 2008 HK\$'000	30 June 2008 HK\$'000
Within one year	57,459	30,398
In the second year	2,136	2,069
In the third to fifth years inclusive	6,682	6,502
After five years	37,662	38,987
	103,939	77,956
Less: Amounts due for settlement within 12 months (shown under current liabilities)	(57,459)	(30,398)
	46,480	47,558

The carrying amounts of the Group's bank loans are denominated in the following currencies:

	31 December 2008 HK\$'000	30 June 2008 HK\$'000
Hong Kong dollars	48,572	49,579
RMB	55,367	28,377
	103,939	77,956

Bank loan of approximately HK\$55,367,000 (30 June 2008: HK\$28,377,000) is arranged at fixed interest rate of 8.217% (30 June 2008: 7.524%) p.a. and exposes the Group to fair value interest rate risk. At 31 December 2008, bank loan of approximately HK\$48,572,000 (30 June 2008: HK\$49,579,000) is arranged at floating rate of 2.10% p.a. (30 June 2008: 2.35%), thus exposing the Group to cash flow interest rate risk. Bank loans are secured by the pledge of the Group's fixed assets and prepaid land lease payments.

Notes to Condensed Consolidated Financial Statements (continued)

12. Trade Payables

The Group normally obtains credit terms ranging from 30 to 120 days from its suppliers.

The ageing analysis of trade payables, based on the date of receipt of goods, is as follows:

	31 December 2008 HK\$'000	30 June 2008 HK\$'000
Within 30 days	10,957	12,613
31 to 60 days	4,978	1,511
61 to 90 days	4,525	3,061
91 to 120 days	5,624	4,215
121 to 365 days	15,715	5,848
Over 1 year	4,964	2,138
	46,763	29,386

Notes to Condensed Consolidated Financial Statements (continued)

13. Share Option Scheme

The Company's share option scheme (the "Scheme") was adopted on 18 November 2002 for a period of 10 years. Under the Scheme, the directors may, at their sole discretion, grant to any eligible participants options to subscribe for ordinary shares of the Company. The exercise period of the share options granted is determinable by the directors and in any event not later than 10 years from the date of grant of share options, subject to the provisions for early termination thereof.

The following share options were outstanding under the Scheme during the Period:

Grantee	Number of share options			Date of grant of share options (note (a))	Exercise period of share options	Exercise price of share options (note (b)) HK\$	Price of Company's shares		
	At 1 July 2008	Granted during the Period	Exercised during the Period				At 31 December 2008	At grant date of shares options (note (c)) HK\$	At exercise date of shares options HK\$
Other employees									
In aggregate	86,100,000	-	-	86,100,000	20 July 2007	24 July 2007 to 23 July 2010	0.582	0.582	N/A
	134,800,000	-	-	134,800,000	22 August 2007	24 August 2007 to 23 August 2010	0.420	0.420	N/A
	220,900,000	-	-	220,900,000					

Notes:

- The vesting period of the share options is from the date of the grant until the commencement of the exercise period.
- The exercise price of the share options is subject to adjustment in the case of a rights or bonus issue, or other similar changes in the Company's share capital.
- The price of the Company's shares disclosed as at the date of the grant of the share options is the higher of the average Stock Exchange closing price on the five business days immediately preceding the date of the grant of the share options or the Stock Exchange closing price on the date of grant of share option.

14. Related Party Transactions

There is no significant related party transaction during the Period (2007: Nil).

15. Contingent Liabilities

The Group did not have any significant contingent liabilities as at the balance sheet date (30 June 2008: Nil).

Notes to Condensed Consolidated Financial Statements (continued)

16. Lease Commitments

At 31 December 2008 the total future minimum lease payments under non-cancellable operating leases are payable as follows:

	31 December 2008 HK\$'000	30 June 2008 HK\$'000
Within one year	1,859	2,028
In the second to fifth years inclusive	338	1,352
	2,197	3,380

Operating lease payments represent rentals payable by the Group for certain of its offices. Leases are negotiated for lease terms ranging from 2 to 3 years and rentals are fixed over the lease terms and do not include contingent rentals.

17. Capital Commitments

The Group's capital commitments at the balance sheet date are as follows:

	31 December 2008 HK\$'000	30 June 2008 HK\$'000
Contracted, but not provided for:		
Buildings, land use rights and construction in progress	221,815	306,575

18. Comparative figures

During the Period, the Company changed its presentation of administrative expenses and other operating expenses in respect of fair value loss on financial assets at fair value through profit and loss (held for trading). The fair value loss on financial assets at fair value through profit and loss (held for trading) is now included in other operating expenses instead of including in administrative expenses. The comparatives have been reclassified accordingly such that the fair value loss on financial assets at fair value through profit and loss (held for trading) is grouped under other operating expenses.

Management Discussion and Analysis

INTERIM DIVIDEND

The Directors have resolved that no interim dividend will be declared in respect of the Period (2007: Nil).

MANAGEMENT DISCUSSION AND ANALYSIS

Business Environment

The financial turmoil, which has taken the world by storm, has had a major impact on the global economy. China's export has been adversely affected. Likewise, China's domestic consumption has also been weakened. Moreover, after the Beijing Olympic Games 2008, the development of new large scale infrastructure construction project was generally slowed down to avoid overheated economy and over investment. The PRC government has also imposed more stringent macro economic measures to stabilize the growth of both financial and properties markets. The decline in export, local consumption and both public and private investment made the downturn of the economy of China becoming surprisingly rapid and drastic.

Facing the formidable external operating environment, the Group's operation was inevitably and unfavorably affected by the weakening of demand from our downstream customers including: construction and building industries, automobile accessories' material manufacturing, healthcare products industries, manufacture of chemical fibers, emulsifiers and paper-making industries. Moreover, the unprecedented volatilities in key raw materials prices had also raised our overall cost of production.

For the six months ended 31 December 2008, turnover of the Group amounted to approximately HK\$600.2 million representing a decrease of 29.5% compared with last corresponding period. Profit attributable to shareholders amounted to approximately HK\$43.1 million representing a decrease of 72.5% compared with last corresponding period. During the financial period under review, the decline in turnover was owing to the decrease in prices of all product segments. At the same time, the prices of the key raw material, e.g. calcium carbide and coal for the Group did not decrease in line with the price of our products.

In review of the change in the performance of the Group's business, a Profit Warning was announced on 16 March 2009.

The Group's selling expenses for the Period was approximately HK\$9.4 million representing a decrease of 48.0% compared with last corresponding period. The significant drop was due to the temporary suspension of production of glucose and starch.

Disregarding the effect of the allowance for receivables of approximately HK\$4.4 million, the Group's normal administrative expenses for the six months ended 31 December 2008 was approximately HK\$31.5 million. Taking out the effect of the share option benefit expenses of approximately HK\$26.9 million and the allowance for receivables of approximately HK\$10.0 million, the Group's normal administrative expenses for the six months ended 31 December 2007 was approximately HK\$29.7 million.

The Group's normal administrative expenses for the Period increased slightly by approximately HK\$1.8 million compared with last corresponding period.

Management Discussion and Analysis (continued)

Management Discussion and Analysis (Cont'd)

Business Review

Polyvinyl – chloride (“PVC”)

During the Period, the PVC segment recorded a turnover of approximately HK\$367.9 million representing a decrease of 17.4% over the corresponding period of the previous year. Operating profit of approximately HK\$77.5 million represented a significant decrease of 40.6% over the corresponding period of the previous year. The decline in turnover is mainly due to the fall in price of PVC. The reduction in production volume made an undesirable effect on the economies scales of production previously attained by the segment.

Vinyl acetate

During the Period, turnover was approximately HK\$192.3 million, representing a decrease of 14.0% over the corresponding period of the previous year. Operating profit was approximately HK\$47.9 million, representing a decrease of 32.6% over the corresponding period of the previous year. The price of the major raw materials, namely calcium carbide remained at high level during the Period. However, we could not shift our cost burden to our customers. The average selling price of vinyl acetate dropped. Consequently, operating profit of the segment was squeezed during the Period.

Bio-chemical products division

During the Period, turnover was approximately HK\$12.0 million, representing a decrease of 92.1% over the corresponding period of the previous year. Operating loss of approximately HK\$16.4 million was attained during the Period, while there was an operating profit of approximately HK\$1.8 million in the corresponding period of the previous year.

The production of starch and glucose has been temporarily suspended since May 2008 while the modification and refurbishment of the existing vitamin C production facilities have been scheduled. Therefore, it was not possible to avoid the fixed factory overhead to keep the machinery in working condition.

The Group has employed highly experienced management expertise in the production of vitamin C to oversee the modification and refurbishment. The experts concluded that the plant and machinery originally designed to produce vitamin C remains intact and could be re-utilised. The application to the State Food and Drug Administration, PRC for resumption of the GMP license to produce vitamin C has been submitted.

Heat and Power division

During the Period, turnover was approximately HK\$29.4 million (after elimination of intra-group sales of approximately HK\$6.8 million), representing a decrease of 6.2% over the corresponding period of the previous year. Operating loss of approximately HK\$17.5 million (after elimination of intra-group sales of approximately HK\$6.8 million) was attained during the Period representing an increase of loss of 21.7% over the corresponding period of the previous year. The Group's existing heat and power generation facilities are coal powered. The sustained high coal price had slightly worsened the results of this segment.

Management Discussion and Analysis (continued)

Management Discussion and Analysis (Cont'd)

Capital structure, liquidity and financial resources

Capital structure

The Group maintained a stable financial position throughout the Period. The Group financed its operations and business development with internally generated resources and equity funding.

Equity funding

During the year ended 30 June 2008, the Company raised funds by issuing 188,100,000 new shares through the exercise of share options by option holders. The net proceeds raised from the exercise of share options granted to the senior management of the Group was approximately HK\$89 million. As at the date of this report, the whole amount was utilised as working capital of the Group.

Liquidity and Financial Ratios

As at 31 December 2008, the Group had total assets of approximately HK\$2,714.1 million (30 June 2008: HK\$2,643.7 million) which were financed by current liabilities of approximately HK\$236.1 million (30 June 2008: HK\$217.0 million), non-current liabilities of approximately HK\$187.8 million (30 June 2008: HK\$188.7 million), minority interests of approximately HK\$177.8 million (30 June 2008: HK\$164.1 million) and shareholders' equity of approximately HK\$2,112.4 million (30 June 2008: HK\$2,073.9 million).

As at 31 December 2008, the current assets of the Group amounted to approximately HK\$779.3 million (30 June 2008: HK\$887.1 million) comprising inventories of approximately HK\$54.7 million (30 June 2008: HK\$103.9 million), trade receivables of approximately HK\$516.8 million (30 June 2008: HK\$401.8 million), prepayments, deposits and other receivables of approximately HK\$162.5 million (30 June 2008: HK\$303.9 million), financial assets at fair value through profit and loss of approximately HK\$8.5 million (30 June 2008: 21.3 million), cash and cash equivalents of approximately HK\$36.8 million (30 June 2008: HK\$56.2 million).

As at 31 December 2008, the Group's current ratio (current assets/current liabilities), quick ratio ((current assets – inventories)/(current liabilities)), gearing ratio (total debts/total assets) and debts to equity ratio (total debts/shareholders' equity) of the Group were approximately 3.3 (30 June 2008: 4.1), 3.1 (30 June 2008: 3.6), 15.6% (30 June 2008: 15.3%) and 20.1% (30 June 2008: 19.6%), respectively.

The financial health of the Group attains at a satisfactory status throughout the Period as indicated by the above figures. During this Period, the management has made an effort in the collection of debts from our customers to avoid bad debts. More frequent review on customers' credit term was performed to prevent further credit sales to customers with bad repayment history and to proactively recover the long outstanding receivables in time.

Management Discussion and Analysis (continued)

Management Discussion and Analysis (Cont'd)

Capital structure, liquidity and financial resources (Cont'd)

Significant investment held by the Company

As at 31 December 2008, the Company did not have any significant investments except the financial assets at fair value through profit and loss of approximately HK\$8.5 million, the Company had recorded a fair value loss on financial assets at fair value through profit and loss of approximately HK\$12.8 million for the Period.

Charges on the Group's assets

As at 31 December 2008, bank loan of approximately HK\$103.9 million is secured by charges over the Group's certain fixed assets and prepaid land lease payments.

Contingent liabilities

As at 31 December 2008, the Group did not have any significant contingent liabilities.

Foreign Exchange Exposure

Although most of the operations of the Company were carried out in the PRC in which transactions were denominated in RMB, the Directors consider that the Group has no significant exposure to foreign exchange fluctuations in view of the stability of the RMB in recent years. The Directors also consider that there will be sufficient cash resources denominated in Hong Kong dollars for the repayment of borrowings and future dividends. During the Period, the Group did not use any financial instrument for hedging purposes and the Group did not have any hedging instrument outstanding as at 31 December 2008.

Number and remuneration of Employees

As at 31 December 2008, the Group had 1,638 full time employees in the PRC and Hong Kong. The Group recognises the importance of human resources to its success. Remuneration is maintained at competitive levels with discretionary bonuses payable on a merit basis and in line with industry practice. Other staff benefits provided by the Group include mandatory provident fund, insurance schemes and performance related commissions.

PROSPECT

Calcium carbide project status

The production of both vinyl acetate and PVC consumes considerable amount of calcium carbide as major raw materials. Faced with challenge from increasing cost and unstable supply of calcium carbide and in view of the underlying strength of the Group's coal related chemical businesses, the Group is confident that the vertical integration to the production of calcium carbide will be the best solution for the challenges.

Management Discussion and Analysis (continued)

Prospect (Cont'd)

Calcium carbide project status (Cont'd)

The first phase of construction of our own calcium carbide production facilities for internal consumption has been started in November 2007. For the first phase, the designed annual production capacities of calcium carbide is expected to be 100,000 tonnes. After completion of the whole project, the calcium carbide will be internally produced and will further lower the cost for the coal related chemical products division. The construction of the factory buildings of the first phase was completed in last September and the installation of production equipment is re-scheduled to be completed by the end of this year.

Heat and power project status

The increase in production capacities of vinyl acetate, PVC, and calcium carbide will in turn provide an opportunity for the heat and power division to expand. Plans have been formulated to build another two sets of coal powered generation facilities to house the increased aforesaid demand. Provincial government approval has been obtained for such expansion.

The Group has started to construct the first set of coal powered generation facilities as the first phase expansion in October 2007. In addition, application on the preferential tariff on electricity generated and supplied for new PVC and calcium carbide expansion project of the Group have been filed and common view has been reached. The Board is confident that the approval will be obtained when the first phase expansion is completed.

The aim of the expansion of our coal powered generation facilities is to cover the demand of electricity consumed by the new calcium carbide production facilities. During the production of calcium carbide, the carbon monoxide will be produced as a by-product and will be transmitted to the new coal powered generation facilities.

The cost of production of heat and power division will be further reduced since the carbon monoxide can be used as a side ignition fuel for the coal powered boiler of the power generation facilities. Therefore, the overall cost of producing calcium carbide internally will be much lower than purchasing from the existing calcium carbide suppliers.

At the date of this report, the progress of the above expansion projects is satisfactory.

Vitamin C development plan

The production facilities for sorbitol liquid (a intermediate product) and vitamin C are being idle at the moment. The valuation of such production facilities was over HK\$160 million when the Group acquired the Bio-chemical business. The estimated investment in the refurbishment and streamlining works on the production facilities for vitamin C is HK\$20 million and will take approximately one year to complete.

Management Discussion and Analysis (continued)

Prospect (Cont'd)

Financing for new calcium carbide expansion, new coal powered generation facilities and refurbishment of vitamin C production facilities

Even though the Group has a stable cash position currently, the construction of calcium carbide production facilities, expansion of the heat and power business and refurbishment of vitamin C production facilities demands much capital expenditure. The Group has re-negotiated the payment schedules with the main contractors of the first 100,000 tonnes calcium carbide production facilities and the first set of coal powered generation facilities. The aforesaid expansion projects are planned to be completed by phrases according to the financial resources of the Group.

Owing to the worldwide financial turmoil, the Chinese economy could never be stand alone in the global economy and was also adversely affected. The PRC government lately imposed expansionary fiscal policy in order to stimulate the economy. Following the policy, the banks in the PRC will widen the credit policy for capital expenditure projects in recent times. In view of this, the Group may consider bank loans and other means of financing to meet the expected capital expenditure.

PRC government economic stimulus plan

During the 11th National People's Congress of the People's Republic of China held on March 2009, the Premier Wen Jiabao has announced RMB 4 trillion economic stimulus plan in the PRC. The National Development and Reform Commission, the Ministry of Finance and the People's Bank of China further explained the details of the aforesaid plan. Around RMB3 trillion is planned to be spend on public infrastructure, housing and technology reform projects in the next five years. Such large scale of nationwide construction project will absolutely consume enormous amount of construction materials and in turn, the demand of PVC in the PRC will be expected to be substantial in the near future.

The Group will inevitably grow by expansion of heat and power business, developing and production of both calcium carbide and vitamin C. They will be the new milestones in the development of the Group. The Board is confident that both businesses will contribute brilliant future and success to the Group and will benefit the shareholders as a whole.

Disclosure of Additional Information

Directors' Interests or Short Positions in Shares and Underlying Shares

As at 31 December 2008, the interests of the Directors and chief executive of the Company in the shares (the "Shares") of the Company, underlying shares and debentures of the Company and its associated corporation (within the meaning of Part XV of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) ("SFO")), which were required to be notified to the Company and the Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions in which they were taken or deemed to have under such provisions of the SFO) or which were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein or which were required to be notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers in the Listing Rules were as follows:

Interests in the Shares and underlying Shares

Name of director	Name of company	Type of interest	Number of ordinary Shares held (long position) (% of issued share capital of the Company)		Share options held
Mr. Chan Yuen Tung	The Company	Beneficial Interest	1,057,400,287	28.27%	Nil
Ms. Chan Yuk Foebe	The Company	Beneficial Interest	14,750,000	0.39%	Nil
Mr. Chiau Che Kong	The Company	Beneficial Interest	82,780,000	2.21%	Nil
Mr. Tam Ching Ho	The Company	Beneficial Interest	1,920,000	0.05%	Nil

Save as disclosed above, as at 31 December 2008, none of the Directors and chief executive of the Company had or was deemed to have any interest or short position in the Shares, underlying Shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the SFO), which were 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 and short positions in which they were taken or deemed to have under such provisions of the SFO) which has been recorded in the register maintained by the Company pursuant to section 352 of the SFO or which has been notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers.

Disclosure of Additional Information (continued)

Interests of Shareholders Discloseable under the SFO

So far as the directors of the Company are aware, as at 31 December 2008, the following persons, other than a Director or chief executive of the Company, had an interest or a short position in the Shares and underlying shares in the Company as recorded in the register required to be kept under section 336 of the SFO:

Name of shareholder	Number of ordinary shares	Capacity	Approximate percentage of interest
Metage Capital Limited	Long position 431,370,000 <i>(note 1)</i>	Investment manager	11.53%
Mr. Webb Richard Ian	Long position 431,370,000 <i>(note 1)</i>	Interest of controlled corporation	11.53%
Pope Asset Management, LLC	Long position 410,186,000	Investment manager	10.96%
UBS AG	Long position 310,500,000	Having a security interest in shares	8.30%
Deutsche Bank Aktiengesellschaft	Long position 42,503,085 <u>331,221,915</u>	Beneficial interest Having a security interest in shares	1.14% <u>8.85%</u>
	<u>373,725,000</u>		<u>9.99%</u>
QVT Financial GP LLC	Long position 334,746,000 <i>(note 2)</i>	Interest of controlled corporation	8.95%
QVT Financial LP	Long position 370,075,000 <i>(note 2)</i>	Investment manager	9.89%
QVT Associates GP LLC	Long position 327,987,023 <i>(note 3)</i>	Interest of controlled corporation	8.77%
QVT Fund LP	Long position 294,933,822 <i>(note 3)</i>	Beneficial owner	7.88%

Disclosure of Additional Information (continued)

Interests of Shareholders Discloseable under the SFO (Cont'd)

Name of shareholder	Number of ordinary shares	Capacity	Approximate percentage of interest
Polygon Global Opportunities Master Fund	Long position 310,500,000 (note 4)	Beneficial owner	8.30%
Polygon Investment Partners LLP	Long position 310,500,000 (note 4)	Investment manager	8.30%
Polygon Investment Partners LP	Long position 310,500,000 (note 4)	Investment manager	8.30%
Polygon Investment Partners HK Limited	Long position 310,500,000 (note 4)	Investment manager	8.30%

Notes:

1. Mr. Webb Richard Ian is a controlling shareholder of Metage Capital Limited. In accordance with the SFO, the interests of Metage Capital Limited are deemed to be, and have therefore been included in the interests of Mr. Webb Richard Ian.
2. QVT Financial GP LLC is deemed to be interested in the shares of the Company through its controlled corporation, QVT Financial LP. In accordance with the SFO, the interests of QVT Financial LP are deemed to be, and have therefore been included in the interests of QVT Financial GP LLC.
3. QVT Associates GP LLC is deemed to be interested in the shares of the Company through its controlled corporation, QVT Fund LP. In accordance with the SFO, the interests of QVT Fund LP are deemed to be, and have therefore been included in the interests of QVT Associates GP LLC.
4. Each of Polygon Investment Partners LLP, Polygon Investment Partners LP and Polygon Investment Partners HK Limited acts as an investment manager of Polygon Global Opportunities Master Fund. In accordance with the SFO, the interests of Polygon Global Opportunities Master Fund are deemed to be, and have therefore been included in each of the interests of Polygon Investment Partners LLP, Polygon Investment Partners LP and Polygon Investment Partners HK Limited.

Save as disclosed above, as at 31 December 2008, no other person had an interest or a short position in the shares and underlying shares in the Company as recorded in the register required to be kept under section 336 of the SFO.

Sufficiency of Public Float

Based on the information that is publicly available to the Company and within the knowledge of the Directors as at the date of this report, there is sufficient public float of more than 25% of the Company's shares in the market as required under the Listing Rules.

Purchase, Redemption Or Sale Of Listed Securities Of The Company

Neither the Company, nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities during the Period.

Disclosure of Additional Information (continued)

Pre-emptive Rights

There are no provisions for pre-emptive rights under the Company's articles of association or the Companies Law (Law 3 of 1961, as consolidated and revised) of the Cayman Islands, being the jurisdiction in which the Company was incorporated, which would oblige the Company to offer new shares on a pro rata basis to the existing shareholders.

Model Code for Securities Transactions

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuer (the "Model Code") as set out in Appendix 10 of the Rules Governing the Listing of Securities on the Stock Exchange ("Listing Rules") as its own code of conduct regarding Directors' securities trading. Having made specific enquiry of all Directors of the Company, all of them confirmed that they have complied with the required standard of dealings as set out in the Model Code during the Period.

Corporate Governance

Code on Corporate Governance Practices

In the opinion of the Directors, the Company has during the Period complied with the Code on Corporate Governance Practices as set out in Appendix 14 of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited ("Listing Rules").

Audit Committee

The Company set up the Audit Committee on 8 April 2001, with written terms of reference, for the purposes of reviewing and providing supervision on the Group's financial reporting process and internal control systems. The Audit Committee comprises the three independent non-executive Directors of the Company, namely, Mr. Ma Wing Yun Bryan, Mr. Yau Chung Hong and Mr. Tam Ching Ho. The Audit Committee has reviewed with the management the accounting principles and practices adopted by the Group and the auditing, internal control and financial reporting aspects of the Company including the review of the unaudited interim results of the Company for the Period and there was no disagreement by the Audit Committee with the accounting treatment adopted by the Company.

Remuneration Committee

A remuneration committee (the "Remuneration Committee") was established by the Company on 1 July 2005 with specific written terms of reference which set out clearly its authority and duties. The Remuneration Committee, currently comprises Ms. Chan Yuk Foebe (executive director), Mr. Ma Wing Yun Bryan, Mr. Yau Chung Hong and Mr. Tam Ching Ho (both are independent non-executive Directors), is responsible for advising the Board on the remuneration policy and framework for all remuneration of the Directors and senior management of the Company, as well as reviewing and determining the remuneration packages of Directors and senior management with reference to the Company's objectives from time to time.

By order of the Board
Chan Yuk Foebe
Chief Executive Officer

Hong Kong, 26 March 2009