

*I*NVESTMENT MANAGER'S DISCUSSION AND ANALYSIS



Dr. Huang Dazhan

Chairman of the Board of China Merchants China Investment Management Limited, the Investment Manager

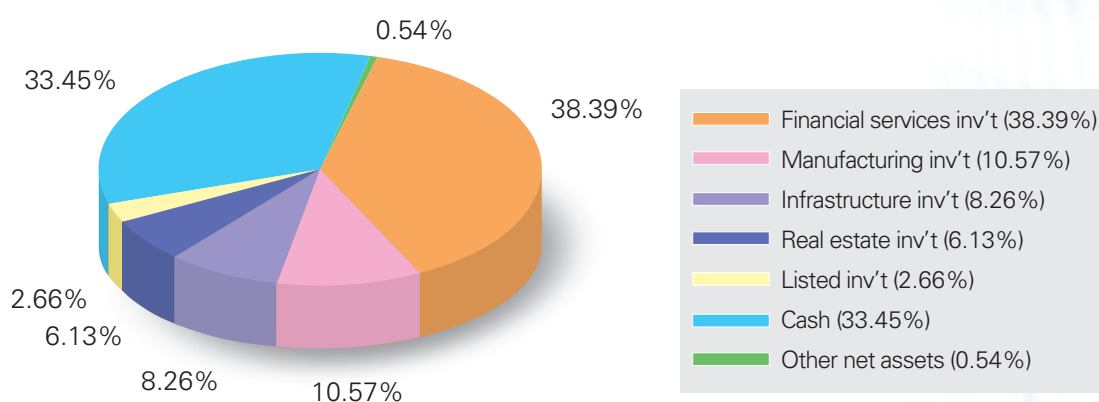
INVESTMENT MANAGER'S DISCUSSION AND ANALYSIS

For the year ended 31 December 2000, the turnover of China Merchants China Direct Investments Limited and its subsidiaries (the "Fund") was US\$6.18 million, representing a 23% decrease against 1999. The Fund achieved profit attributable to shareholders of US\$3.65 million for the year 2000, representing a 49% increase over 1999. The earnings per share were US\$0.027. The drop in turnover was mainly due to the decline of incomes from contractual joint venture investments. The increase of profit was mainly due to the appreciation in the value of the Fund's financial services investments. As at 31 December 2000, the net assets of the Fund were US\$121.12 million, representing a 1.6% increase over 1999. The net asset value per share was US\$0.883.

At the end of 2000, the Fund had total investments of approximately US\$80.55 million, of which US\$77.33 million was in unlisted investments and US\$3.22 million in listed investments. The major unlisted investment projects are spread through the sectors of financial services (accounting for 38.39% of the Fund's net assets); manufacturing (10.57%); infrastructure (8.26%); and real estate (6.13%). Additionally, the Fund had cash and bank balances of US\$40.52 million, accounting for 33.45% of the Fund's net assets.

NET ASSET DISTRIBUTION

As at 31 December 2000



*I*NVESTMENT MANAGER'S DISCUSSION AND ANALYSIS



Mr. Zhang Yun Kun

Managing Director of China Merchants China Investment Management Limited, the Investment Manager

REVIEW OF UNLISTED INVESTMENTS

The following table shows the major unlisted investment projects held by the Fund as at 31 December 2000:

Name of Projects	Location	Business Nature	Net Book Value US\$ million	Percentage of Net Assets
Financial Services:				
1. China Merchants Bank	Shenzhen, Guangdong	Banking	30.28	25.00
2. Fujian Industrial Bank	Fuzhou, Fujian	Banking	14.88	12.29
3. Industrial Securities Co. Ltd.	Fuzhou, Fujian	Securities	1.33	1.10
		Sub-total	<u>46.49</u>	<u>38.39</u>
Manufacturing:				
4. Zhaoyuan Jinbao Electronics Co. Ltd.	Zhaoyuan, Shandong	Copper foil & laminates	8.85	7.30
5. Chengde Wanli Steel Tubes Co. Ltd.	Chengde, Hebei	Steel tubes	3.96	3.27
6. Tangshan Kintil Ceramics Co. Ltd.	Tangshan, Hebei	Ceramic tiles	—*	—
		Sub-total	<u>12.81</u>	<u>10.57</u>
Infrastructure:				
7. Maoming Tongfa Highway Co. Ltd.	Maoming, Guangdong	Toll road	10.00	8.26
8. Weifang Yin Yuan Aviation Industry Co. Ltd.	Weifang, Shandong	Airport terminal	—*	—
		Sub-total	<u>10.00</u>	<u>8.26</u>
Real Estate:				
9. China Merchants Plaza (Shanghai) Property Co. Ltd.	Shanghai	Office & Commercial	—*	—
10. Beijing Longbao Mansion	Beijing	Office & Apartments	4.98	4.11
11. Shenzhen Man Kam Square	Shenzhen, Guangdong	Retail shops	2.45	2.02
12. Weifang Zhaoyin Real Estate Development Ltd.	Weifang, Shandong	Low-cost housing	—*	—
		Sub-total	<u>7.43</u>	<u>6.13</u>
		Total	<u>76.73</u>	<u>63.35</u>

* Full provision was made. Please refer to the project's review listed below for the amount of provision.

FINANCIAL SERVICES INVESTMENTS

The financial services sector is one of the core investment areas of the Fund. The investment projects not only generated a stable cash inflow, but also contributed significant capital appreciation to the Fund.

China Merchants Bank ("CMB")

CMB, the first joint-stock bank established by mainland enterprises, is the second largest commercial bank in the PRC, with over 230 offices distributed throughout the country. CMB's All-in-One Card (ATM card) and All-in-One Net (Internet banking services) are pioneering services in PRC's electronic banking industry and received popular support in the market.

The Fund invested US\$13.77 million to own a 1.62% stake in CMB. CMB recorded a profit before taxation of RMB1.6 billion for 2000, representing a 6.6% increase over 1999. In 2000, the Fund received distribution of US\$1.227 million from CMB.

CMB has applied to the relevant government authorities of the PRC for the listing of "A" shares on one of the domestic stock markets. At the end of 2000, the Fund's investment in CMB was valued at US\$30.28 million, representing a 30% increase over 1999.

Fujian Industrial Bank Company, Limited ("FIB")

FIB is a joint-stock commercial bank with 14 branches, 67 sub-branches, 2 representative offices, 82 offices and 71 deposit counters, totalling 237 business points in major cities such as Beijing, Shanghai, Shenzhen, Changsha, Hangzhou and Xiamen.

In 1998, the Fund invested US\$12.75 million and owned a 3.2% stake in FIB. In order to cope with increasing competition after the PRC's entry into the World Trade Organization, FIB enlarged its capital base by issuance of new shares in mid 2000. The Fund's shareholding was diluted to 2.13% after the completion of the new share placement.

FIB recorded a RMB500 million profit before taxation for 2000, representing a 14% increase over 1999. The Fund received a dividend of US\$0.928 million.

The Board of Directors of FIB is actively studying the feasibility of listing the FIB shares on domestic and foreign stock exchanges. At the end of 2000, the Fund's investment in FIB was valued at US\$14.88 million, representing an 8.3% increase over 1999.

On 12 April 2001, the Fund signed a conditional agreement with an existing shareholder of FIB to acquire 20 million shares of FIB at a total consideration of US\$4.84 million. The agreement is conditional upon the approval of the relevant authorities in the PRC. Upon the completion of the transaction, the Fund will own 84 million shares of FIB, representing a 2.8% interest in the bank.

Industrial Securities Company, Limited ("ISCL")

ISCL is a comprehensive securities company registered in the PRC, with paid-up capital of RMB900 million. ISCL was formerly the securities department of FIB. In 1994, it was restructured as Fujian Industrial Securities Corporation, a wholly owned subsidiary of FIB. However, at the end of 1999 ISCL separated from FIB. ISCL's range of business includes securities underwriting, broking, house trading and investment advice. It has 16 offices in major cities such as Beijing, Shanghai, Shenzhen, Wuhan, Fuzhou and Xiamen.

The Fund invested US\$1.03 million for 6.72 million shares or a 0.74% stake of ISCL.

At the end of 2000, the total and net assets of ISCL were RMB7.38 billion and RMB1.49 billion respectively. ISCL recorded a profit after taxation of RMB200 million for the year 2000. At the end of 2000, the Fund's investment in ISCL was valued at US\$1.33 million, representing a 29% increase over 1999.

MANUFACTURING INVESTMENTS

The Fund's investments in the manufacturing sector include electronics, steel tubes and ceramic tiles. The investment return on these projects varied. The electronics project generated satisfactory returns to the Fund, but the steel tubes and ceramic tiles projects did not perform to our expectation. The Fund will gradually decrease investment in this sector.

Zhaoyuan Jinbao Electronics Company Limited ("Jinbao")

The Fund, BOC China Fund and Shandong Zhaoyuan Electronic Materials Factory set up Jinbao in December 1993, to engage in the manufacture and sale of electronic materials, namely, copper foils and copper-clad laminates. Jinbao recorded a profit before taxation of RMB18.39 million for the year 2000, a slight decline over the previous year. The decrease in profit was mainly attributable to stock clearance. In 2000, the Fund received a total of US\$1.15 million from profit distribution and shareholder loan interest. The new 2,500-ton copper foil production line was scheduled to begin operation in the second half of 2001, and is expected to become a new source of profit.

Chengde Wanli Steel Tubes Company Limited ("Wanli")

Established in 1996, Wanli is a Sino-foreign cooperative joint venture engaged in the production and sale of seamless-like steel tubes. The Fund invested US\$5 million, to own a stake of 35%. After a prolonged trial period, the production line still fails to meet the pre-designated expectations. High production costs due to a high ratio of sub-standard products have resulted in

a lack of profit at Wanli. Since 1999, the Chinese party has decelerated its pace on return payment. The Fund therefore suspended recording predetermined return from Wanli as from the beginning of 2000. To date, the Chinese party has made the Fund a return payment US\$3.23 million in total, representing approximately 75% of the investment principal, though only 39% of the fourth payment of US\$1.25 million, due in March 2000, was actually made. Aside from already demanding an early settlement of due payments, we are in contact with the Chinese party for disposal of interest in the project, and both parties are currently working on the details of disposal agreement.

As the fourth payment has been due for a year, the Fund made a provision of US\$0.45 million against the outstanding receivable amount which was booked in 1999.

Tangshan Kintil Ceramics Company Limited ("Kintil")

In 1993, the Fund, together with Tangshan Victory Group (now combined with Tangshan Ceramics Group), Tangshan Hi-Tech Industries Development Zone Group and BOC China Fund, formed Kintil, to engage in the production and sale of glazed mosaics and homogenous tiles. The Fund invested US\$2.21 million, to own an interest of 15%. In the light of a continuing weak construction-material market, and due to huge recorded losses, Kintil terminated its production in 1999. Regarding the disposal of the Fund's interest in the project, the Fund has maintained constant contact with the Chinese party. As opinion from shareholders has so far not been consolidated, a final agreement has not yet been reached.

The Fund made a provision of US\$2 million in 1999. As the disposal agreement is unlikely to be concluded soon, a further provision of US\$0.21 million was made against the balance of the investment cost.

INFRASTRUCTURE INVESTMENTS

Infrastructure investments continued to generate cash income to the Fund. The Fund will continue to explore investment opportunities and invest in those projects that promise a high return.

Maoming Tongfa Highway Co. Ltd. ("Tongfa")

Tongfa is a contractual joint venture with total investment and paid up capital of US\$28.8 million and US\$10 million respectively. The contractual period is 24 years. Tongfa is engaged in the construction and operation of the Provincial Highway No. 1987 linking Maoming City and Huazhou City.

The Fund invested US\$10 million and owned a 34.7% stake in Tongfa. In 2000, the Fund received return payment of US\$1.5 million in accordance with the joint-venture agreement.

Weifang Yin Yuan Aviation Industry Company Limited ("Yin Yuan")

Yin Yuan was established in 1994, with the aim of developing Weifang city's civil airport. The Fund invested 2.875 million, representing a 31.3% stake in the project. By the end of 1998, the Chinese party had fully repaid the Fund's investment principal. However, the termination of the Transportation Construction Fund collection by the Weifang Government has put the Chinese party under financial pressure. The Chinese party therefore proposed to cease cooperation following on partial settlement of the fifth guaranteed return. We have not agreed with this proposal and is conducting meetings with the Chinese party on the issue.

A provision of US\$0.998 million was made in 1999. As the fifth return payment has been outstanding for over one year, the Fund decided to make a full provision of US\$0.6 million against this payment.

REAL ESTATE INVESTMENTS

Investment returns in the real estate sector have not been satisfactory, so we will adopt a more conservative attitude towards property projects in future.

China Merchants Plaza (Shanghai) Property Company Limited ("CM Plaza")

CM Plaza is an office/commercial complex located at 333 Cheng Du Road in Shanghai, with a site area of 9,642 sq.m. Its gross floor area and saleable area are 70,805.95 sq.m. and 60,086 sq.m. respectively.

Through a 22% holding in Daily On Property Limited, the Group invested US\$7.682 million to develop CM Plaza. Leasing and sales started following its completion in 1998. However, the leasing and sales have been sluggish and CM Plaza's operating income was insufficient to cover its interest expenses, resulting in a lack of profit to the shareholders.

Because of the oversupply of office space in Shanghai and because no great improvement on leasing or sales is likely in the near future, the Fund provided in full the balance of the investment cost of US\$3.78 million, following collection of the shareholder's loan of US\$1.997 million in 2000.

Beijing Longbao Mansion ("Longbao")

Longbao is situated near the Third East Ring of Chaoyang District in Beijing. It comprises two blocks of 17-storey apartments and a podium, which is earmarked for office use. In 1997, the Fund invested US\$4.98 million and signed an agreement with the developer to jointly manage the Longbao rental space for three years. The Fund owned a 35% interest.

According to a joint-management agreement, the developer should pay a fixed investment return semi-annually to the Fund within the 3-year contractual period. However, the developer failed to pay further return after making the first year's return payment. We are examining various options in order to speed up recovery of capital. According to an independent surveyor's report, the market value of the property as at the end of 2000 was higher than its investment cost.

The Fund now owns 5,016 sq.m. of the property, of which the Fund has let 1,095 sq.m. The rental yield for this portion is about 10%. In view of the considerable time needed for the disposal of the property, a full provision of US\$0.78 million was made in 2000 against the previously recorded return payment.

Shenzhen Man Kam Square ("Man Kam")

Through a 35% holding in Hansen Enterprises Limited ("Hansen"), the Fund invested US\$4.3 million to purchase the whole of the retail space on level 3, totalling 5,262 sq.m. of Man Kam in 1994.

Man Kam is a 33-storey office/commercial complex in Wen Jin North Road of Shenzhen. At the outset, Hansen signed a pre-sale contract with the developer and made a down payment of 90% of the whole transaction. According to the pre-sale contract, the delivery date was originally scheduled for 30 June 1995. However, as the relevant floor was still not completed at the end of 1996, the developer failed to deliver the property on time.

Accordingly, in 1997, Hansen instituted legal proceedings requiring the developer to terminate the pre-sale contract, and to refund the deposit and make compensation as well. Hansen obtained a favorable judgement against the developer in both Shenzhen Intermediate Court and Guangdong Provincial High Court respectively. However, in the course of enforcing the judgements, the developer complained to the Beijing Supreme Court, which finally ordered Guangdong Provincial High Court to re-examine the case in July 1999. In November 2000, Guangdong Provincial Court made a judgment that both Hansen and the developer were required to honor the obligations of the pre-sale contract, whereby the developer compensate Hansen 10% of the contract sum for the delay. Hansen is now in the process of taking possession of the property.

Given the legal expenses incurred over the past few years and the decline in the Shenzhen real estate market, the investment's book value decreased by US\$1.85 million by the end of 2000. The Fund's share of loss of the project company and the provision for the project totalled US\$0.67 million for 2000.

Weifang Zhaoyin Real Estate Development Limited ("Zhaoyin")

Zhaoyin is a Sino-foreign cooperative joint venture set up in 1994 in the High & New Technology Industrial Development Zone in Weifang, Shandong Province for the development of the "Comfort Housing Program" in the zone. The Fund invested US\$4 million, to own an 18% interest in Zhaoyin. Other partners are Weifang Hi-Tech Industries Development Zone Group, BOC Investment Limited and China Merchants Investment Limited. Because of financial problems since 1997, the Chinese party stopped paying returns according to the contracted schedule. To date, the Fund has received return payments US\$2.18 million in total, representing 54.5% of the original investment. We, together with other foreign parties, are negotiating closely with the Chinese party, hoping that a new repayment schedule can soon be finalized.

Anticipating that return payment rescheduling would take a while, the Fund therefore decided to make a full provision of US\$1.91 million against the remaining investment cost.

REVIEW OF LISTED INVESTMENTS

While leading worldwide stock exchange indexes declined in 2000, the hi-tech stock suffered a even greater drop. Over this period, the H-share and red-chip indexes in Hong Kong dropped 18% and 17% respectively. Despite this, the Shenzhen and Shanghai B-share indexes recorded 63% and 136% increases. The gains from the Fund's B share investments offset part of the investment losses from other listed stocks. Over the whole year, the Fund realized a profit of US\$1.31 million from the disposal of listed investments. The dividends received were US\$0.19 million. The unrealized holding loss was US\$2.03 million. The Guangdong Enterprises' bond previously held by the Fund was exchanged into assets of Guangdong Enterprises following its restructuring. The aggregate value of these assets was approximately the carrying value of the bond. At the end of 2000, the Fund had listed shares valued at US\$3.22 million.

INVESTMENT MANAGER'S DISCUSSION AND ANALYSIS

Particulars of the Group's listed investment portfolio at 31 December 2000 are as follows:

Name of Securities	Principal Activities	Cost US\$	Market Value US\$	Percentage of Net Assets
Angang New Steel Co., Ltd. "H" share	Production and sale of steel products	127,870	91,359	0.08
Beijing Datang Power Generation Co., Ltd. "H" share	Operate coal-fired electric power plants	45,543	44,818	0.04
Beijing North Star Co., Ltd. "H" share	Property investment and development in Beijing, PRC	271,240	200,733	0.17
Beijing Yanhua Petrochemical Co., Ltd. "H" share	Manufacturing and sales of petrochemical products	492,498	200,733	0.17
China Mobile (Hong Kong) Ltd.	Provision of cellular telecommunications services	750,206	548,158	0.45
China Overseas Land & Investment Ltd.	Property development	403,059	259,924	0.21
China Shipping Development Co., Ltd. "H" share	Provision of cargo shipping services in PRC	200,201	151,837	0.13
CITIC Pacific Ltd.	Aviation, trading, property investment and development	542,514	355,787	0.29
Guangdong Development Fund Ltd. *	China direct investments	24,256	17,200	0.01

Name of Securities	Principal Activities	Cost US\$	Market Value US\$	Percentage of Net Assets
Guangdong Investment Ltd.	Infrastructure, property development and investment	15,483	15,483	0.01
Guangshen Railway Co., Ltd. "H" share	Operation of railroad between Guangzhou and Shenzhen	769,791	374,445	0.31
Harbin Power Equipment Co., Ltd. "H" share	Manufacturing thermal and hydro power equipment	357,709	133,179	0.11
I-Wood International Holdings Ltd.	Design and manufacture of wooden furniture products	103,984	38,603	0.03
Pacific Century Cyberworks Ltd.	Provision of telecommunication services	936,311	282,667	0.23
Phoenix Satellite Television Holdings Ltd.	Operating satellite television	280,927	273,435	0.23
Shenyang Public Utility Holdings Ltd. "H" share	Public utility development and operations	209,731	133,822	0.11
Skyworth Digital Holdings Ltd.	Manufacture and sale of Colour TV sets in the PRC	698,127	97,793	0.08
Total		6,229,450	3,219,976	2.66

* Securities traded overseas

PROSPECTS

Since the investment strategy of the Fund focuses on the sectors of financial services, infrastructure and hi-tech industries, we will actively seek investment opportunities in the above sectors and recommend the Fund for further investments if appropriate. We believe that hi-tech industries will represent the highest growth area. Valuation of hi-tech projects has come down to a reasonable level after the major consolidation in 2000, rendering more investment opportunities for the Fund.

Meanwhile, we will try to decrease the investment weighting of the Fund in both manufacturing and property sectors and put more effort into the collection of return payments and on the realization of some non-core investment projects. We will also continue to strengthen our management efforts on the existing projects so as to bring a higher return to the Fund.

Zhang Yun Kun

Managing Director

China Merchants China

Investment Management Limited

Hong Kong, 20 April 2001

I NVESTMENT MANAGER'S DISCUSSION AND ANALYSIS



Directors of China Merchants China Investment Management Limited, the Investment Manager, from right, Dr. Huang Dazhan, Ms. Kan Ka Yee, Elizabeth and Mr. Zhang Yun Kun; from upper right, Mr. Wu Hui Feng and Mr. Tse Yue Kit.