

CHAIRMAN'S STATEMENT AND REVIEW OF OPERATIONS AND RESULTS

On behalf of the Board of Directors, I present the Interim Report of China Resources Logic Limited (the "Company") and its subsidiaries (together the "Group") for the six months ended 30th June, 2001 to the shareholders.

Results

The Group's unaudited consolidated turnover for the six months ended 30th June, 2001 amounted to \$620 million, representing an increase of 7.5 times as compared to the six months period ended 30th September, 2000. The Group's gross profit margin is 37%, a significant increase over the gross profit margin of 21% for the six months period ended 30th September, 2000. The Group's operating profit for the period ended 30th June, 2001 was HK\$141.5 million representing a margin of 23%. The Group's profit attributable to shareholders and basic earnings per share for the period was HK\$65.2 million and HK\$4.32 cents respectively whilst for the comparative six months period ended 30th September, 2000, the Group recorded a loss of HK\$11.6 million. Apart from improved Office Furniture Business, the turnaround of the results of the Group was mainly due to the completion of the acquisition of the Compressor, Semiconductor and Information Technology Businesses during the period.

	Unaudited	
	Six months ended	
	30th June, 2001	30th September, 2000
	HK\$'000	HK\$'000
Turnover	<u>619,906</u>	<u>83,213</u>
Operating profit/(loss)	141,546	(9,875)
Finance costs	(20,983)	(1,508)
Share of loss of an associate	<u>—</u>	<u>(201)</u>
Profit/(loss) before taxation	120,563	(11,584)
Taxation	<u>(11,135)</u>	<u>—</u>
Profit/(loss) after taxation	109,428	(11,584)
Minority interests	<u>(44,258)</u>	<u>—</u>
Profit/(loss) attributable to shareholders	<u>65,170</u>	<u>(11,584)</u>
Basic Earnings (loss) per share	<u>4.32 cents</u>	<u>(0.79) cents</u>

Interim Dividend

The Directors do not recommend the payment of dividend and there was no dividend paid during either periods.

Business Review

Upon shareholders' approval on 22nd January, 2001, the Group has successfully completed its restructuring by acquisition (the "Acquisition") of (i) the Compressor Business; (ii) the Semiconductor Business and (iii) the Information Technology Business from China Resources (Holdings) Company Limited ("CRH"). The total consideration of the Acquisition was HK\$851.7 million and satisfied by the issue of Convertible Bond of similar amount by the Company to CRH. Upon shareholders approval, the name of the Company has changed from Logic International Holdings Limited to China Resources Logic Limited with effect from 23rd January, 2001. New directors of the Company have also been appointed to manage and develop the above-acquired businesses.

Compressor Business

The Group's Compressor Business is one of the leading suppliers of air-conditioner compressors in mainland China with a market share of about 10%. Residential air-conditioner has a penetration rate of only 25% in urban household in mainland China. With the growth of upper and middle class population in mainland China, more people are able to afford air-conditioners. Furthermore, air-conditioners normally need to be replaced after 7 to 8 years of usage (otherwise the energy efficiency ratio decreases which leads to increase in electricity consumption). This therefore represents huge potential demand for air-conditioner. Since the Group's Compressor Business is a key supplier to the few leading air-conditioner manufacturers in mainland China, the Group will benefit from such increase in demand for air-conditioners.

In April 2001, the construction of the Phase III production line for expansion of the Compressor Business's production capacity was completed and production commenced in May 2001. It has been introduced in the Phase III expansion the most current and internationally advanced air-conditioner compressor technology using DC rotary compressor technology and new refrigerants (which conforms to the international standards for environmental protection; and yet to be developed and utilised in mainland China). This provides room for long term development growth for the Compressor Business and a solid foundation for the Group's steady growth in profit. The production capacity of the Compressor Business of the Group has thus been increased from an annual production of 1,400,000 units of air-conditioner compressors to 2,200,000 units. Notwithstanding the keen competition in the air-conditioner industry in mainland China, the selling price of air-conditioner compressor was relatively stable because the demand for domestic air-conditioner compressors remained strong during the period because of limited supply.

For the period from February to June 2001, a record sales volume of 970,000 units were achieved. Turnover amounted to HK\$438 million. The Compressor Business has made a significant contribution to the Group's operating profit with good return. Such good return, apart from the buoyant air-conditioner compressor market, was mainly brought about by successful material localisation program and tight cost control measures. This provides a solid foundation for further development of the Compressor Business. The Compressor Business achieved an operating profit of HK\$133 million for the six months ended 30th June, 2001.

The Group intends to enlarge its market share in mainland China and increase export through expanding its production facilities and introducing new products. It is anticipated that after such measures are taken, the Group will be able to satisfy local demand as well as for export. Meanwhile, from the point of view of long term strategic development, the Group will strengthen its relationship and form strategic partnerships with leading air-conditioner manufacturers in mainland China. The Group's Compressor Business would also enhance its product research and development through co-operation with its Japanese partner so as to keep up with the latest cooling technology to increase its competitiveness.

Semiconductor Business

The Group's 4-inch wafer operations are mainly engaged in the production of consumer integrated circuits ("IC") and special semiconductor devices for use in watches, clocks, toys, telecommunication and other consumer products. Even though global demand for IC's has decreased this year, there is still a growing demand of IC's in mainland China. The profit margins of 4-inch wafer products are lower than those for 8-inch and 12-inch wafers but are less price sensitive. It is relatively immune to the recent price volatility in the global semiconductor market. Turnover of the consumer IC's produced by the Group's Semiconductor Business amounted to HK\$85 million. Despite the downward pressure on selling price, the gross profit margin achieved by the Semiconductor Business was at a respectable 30% because of stringent cost control measures and relative low depreciation of 4-inch wafer production line. The Semiconductor Business achieved an operating profit of HK\$15 million for the six months ended 30th June, 2001.

At present, the domestic semiconductor industry only supplies less than 20% of the total demand in mainland China. With this ample room for growth and the continuous expansion of this market, the Group's Semiconductor Business has good potential. To realise this potential, the Group has in March, 2001, established in mainland China a wholly owned subsidiary for IC development and marketing. The Group intends to expand its market share in this area and will explore opportunities to expand both its production facilities, enhance its design capability and form strategic partnerships with both overseas and Chinese enterprises. In addition, the Group will also consider acquiring additional production facilities from enterprises in mainland China.

Information Technology ("IT") Business

Resources Link Network Limited ("Resolink"), a wholly owned subsidiary of the Company, provides IT services which include, amongst others, the provision of business solutions to assist customers to achieve the most effective use of hardware and software resources, and the provision of IT consultancy services. Resolink is also engaged in the development of software and the related consulting services. At present, the major customers of Resolink are members of the CRH group. The IT services rendered to them provide Resolink with a solid customer base and steady income. Turnover for the Group's IT Business amounted to HK\$21 million for the six months ended 30th June, 2001. The IT Business achieved an operating profit of HK\$1.9 million in the period.

The Group intends to expand and build upon the foundation of its IT services to CRH group. As the Directors anticipate growth in the IT business, Resolink is exploring opportunities to expand its services to third parties both in Hong Kong and in mainland China. Particularly in mainland China, Resolink is positioning itself to become a major IT service provider specialising in IT related business/application consultancy, technical solution service, IT infrastructure management and IT product distribution. To achieve this, the Group considers (i) the forming of strategic partnership with local players and (ii) the development of enterprise application services for the local retail and distribution industry. The Group is also exploring forming strategic partnership with overseas entities on research and development to exploit latest IT technology for commercial use.

Office Furniture Business

The Group is one of the top quality office furniture manufacturers and suppliers in mainland China and its brand name has been firmly established. The Group's furniture business will continue to grow as the demand for high quality office furniture will increase with China's economic growth and the increase in the number of foreign entities investing in mainland China.

The Group has streamlined its operation after reorganised its Hong Kong sales operation into distributorship and completing the consolidation of the production factories in mainland China. This includes the relocation of the factory in Guangzhou to Zhuhai. Production is now centralised in Zhuhai, making it more cost-effective and efficient in production resulting from saving in materials and labour costs as well as the shortening of production lead time.

The Group's business for the provision of quality office furniture in mainland China benefits from the latter's continual growth of its overall economy particularly that of the major cities such as Beijing and Shanghai. The performance of the Office Furniture Business has significantly improved. Turnover is HK\$75.4 million for the six months ended 30th June, 2001. An operating profit of HK\$4.9 million was achieved compared to operating loss of HK\$9.9 million in the six months period ended 30th September, 2000.

Prospects

With the successful restructuring and acquisition of the Compressor, Semiconductor and IT Businesses, the continuous support from CRH, steady growth and positive contributions from all its operating businesses, the Group is now well positioned to embark upon its expansion plan via organic and acquisition growth.

The Group intends to live up to its billing as the technology flagship of CRH group by leveraging and capitalising on (i) its existing core manufacturing and IT services competency; (ii) the vast and talented human resources pool available in mainland China; (iii) the competitiveness of manufacturing bases in mainland China and (iv) the steadily growing market in mainland China.

Over the next few years, it is expected that the Group will grow rapidly by organic expansion as well as external acquisitions of promising technology based enterprises in high growth industries in mainland China.

Financial Review

Cash Flow

The Acquisition completed during the period had a fundamental effect on the Group's cash flow position. Net cash flow from operating activities was HK\$148 million and the contribution from newly acquired businesses accounted for over 100% of this. Net cash inflow from investing activities in the period mainly comprised of HK\$273 million of net cash brought in through the Acquisition, while the payment made during the period for the construction of the Phase III air-conditioner compressor production line had reduced the amount of cash by HK\$188 million. Net cash outflow from financing activities was mainly as a result of the net partial repayment of the short term bank loan in the Compressor Business which amounted to HK\$46.8 million. Overall, the Group had cash and cash equivalent of HK\$362 million as at 30th June, 2001, representing an increase of HK\$170 million since the beginning of the period.

By contrast, in the six months period ended 30th September, 2000, the major source of cash inflow comes from (i) issuance of new shares by the Group to CRH and China Resources Enterprise, Limited in April 2000, which raised HK\$350 million and (ii) the disposal of one of the Group's properties in Hong Kong with net proceeds of HK\$62 million.

Liquidity and Financial Resources

As at 30th June, 2001, the Group had total interest bearing debts of HK\$1,037 million and cash balance of HK\$362 million, with a gearing ratio (calculated as ratio of net debt : shareholders' funds plus minority interests) of 1 : 1. The increase in the Group's gearing was mainly due to the issuance of Convertible Bond of HK\$851.7 million on 1st February, 2001 as consideration for the acquisition of the three new businesses from CRH group. The Convertible Bond with a coupon rate of 2% p.a., is

redeemable by 1st February, 2004, (i.e. the Maturity Date) and with an option to the bond holder to convert into shares of the Company any time between 1st February, 2001, to 1st February, 2004 (both days inclusive) at the conversion price of HK\$0.9108 per share. The rest of the borrowing was for financing of working capital of the Group. The interest cover of the Group for the period was at a healthy level of 6.6 times. Apart from this, the Group has pledged HK\$8 million bank deposit against an equivalent amount of short-term Chinese Renminbi bank facilities.

The Group has no other committed borrowing facilities. For day-to-day liquidity management and maintaining flexibility in funding, the Group has access to sufficient uncommitted short-term facilities provided by its bankers. There are, however, no present needs for borrowings of any material amount.

Financial Management and Treasury Policy

The financial risk management of the Group is the responsibility of the Group's treasury function at the head office based in Hong Kong. Barring any possible devaluation of the Chinese Renminbi, currently the Group does not expect any significant foreign exchange exposure.

Capital Structure

As at 30th June, 2001, the gearing ratio (calculated as ratio of net debt : shareholders' funds plus minority interests) of the Group was 1 : 1, which is relatively high. This is mainly due to the issuance of Convertible Bonds. Since the Maturity Date of the Convertible Bonds is about 2¹/₂ years from now, thus the Group has no intention to change the mix of its equity and debt structure for the foreseeable short-term period.

The outstanding debts are mainly denominated in Hong Kong dollars and Renminbi, the Group does not expect significant exposure to foreign exchange fluctuations in this regard. Details of the loans outstanding are as depicted in Note 12 to the accounts.

Significant Investments, Acquisitions and Disposals

During the period under review the Group had successfully completed a restructuring exercise with a view to positioning the Group as the listed technology arm of the CRH group. The core of the restructuring exercise consisted of the acquisition of (i) the Compressor Business (ii) the Semiconductor Business and (iii) the IT Business from the CRH group.

The acquisitions were approved by the shareholders in the Special General Meeting held on 22nd January, 2001 and were completed officially on 1st February, 2001. The aggregate consideration for the acquisitions which amounted to approximately HK\$851.7 million was satisfied in full by the issuance of Convertible Bonds of equivalent value on 1st February, 2001.

During the period, the Group has incurred a total capital expenditure (including technical know-how) of HK\$188 million in the construction of its Compressor Business's Phase III expansion. The said amount of HK\$188 million represented 95% of the Group's total capital expenditure up to 30th June, 2001. This investment has achieved the aim of enhancing the production capacity of the Group's Compressor Business.

Except the above acquisitions and investment, there were no significant investments and material changes in the composition of the Group during the period under review.

Going Concern

On the basis of current financial projections and facilities available, the Group has adequate financial resources to continue its operation for the foreseeable future. For this reason, the going concern basis continues to be adopted in preparing the financial statements.

Reward for Employees

As at 30th June, 2001, the Group employs approximately 2,900 employees in Hong Kong and mainland China. The Group values human resources and recognises the importance of attracting and retaining quality staff for its continuous success. Staff bonus and incentives are awarded basing on individual performance and share options are granted by the Board of Directors to certain employees as the Board considers appropriate.