



Chapter VII Directors' Report

Section 1. Operation of the Company

1. Scope of Principal Activities and Operation Review of the Company

The Company is one of the largest textile machinery manufacturers in the PRC. It is principally engaged in the manufacture and sale of textile machinery and components and special parts.

In 2001, amid the intense competition in the PRC market, the Company made use of its competitive edge and the prevailing opportunity to boost its business development.

As stated in the financial report prepared in accordance with the HK GAAP for the year ended 31st December 2001, turnover and profit attributable to shareholders of the Group amounted to RMB2,215,239,000 and RMB82,694,000 respectively, representing an increase of 22.52% and a decrease of 38.23% over the previous year respectively. As at 31st December 2001, bank and cash balances, short-term bank loans and overdrafts and long-term bank loans of the Group amounted to RMB1,329,574,000, RMB693,970,000 and RMB122,663,000 respectively. The gearing ratio (total long-term loans/net assets) of the Group as at 31st December 2001 was 5.5%.

As stated in the financial report prepared in accordance with the PRC GAAP for the year ended 31st December 2001, revenue from principal activities of the Group amounted to RMB2,215,239,000, representing an increase of 22.52% over the previous year. Profit from the principal activities was RMB434,459,000, representing an increase of 19.88% over the previous year.

Including:

Revenue from principal activities of the parent company was RMB857,234,000, representing an increase of 7.41% over the previous year while its profit from principal activities was RMB173,519,000 representing an increase of 14.57% over previous year.

Subsidiaries: Revenue from principal activities of Zhengzhou New Hongda Textile Machinery Company Limited was RMB320,626,000 while profit from principal activities was RMB53,980,000.

Revenue from principal activities of Qingdao Hongda Textile Machinery Company Limited was RMB571,424,000 while profit from principal activities was RMB101,455,000.

Revenue from principal activities of Shenyang Hongda Textile Machinery Company Limited was RMB115,617,000 while profit from principal activities was RMB31,666,000.

Revenue from principal activities of Tianjin Hongda Textile Machinery Company Limited was RMB235,404,000 while profit from principal activities was RMB44,894,000.

Section 1. Operation of the Company (continued)**2. An analysis of the turnover and contributions to operating profit prepared in accordance with the HK GAAP**

	Turnover <i>RMB'000</i>	Contributions to operating profit <i>RMB'000</i>
Manufacture and sales		
Natural fibre textile machinery	1,701,982	
Chemical fibre textile machinery	129,249	
Textile machinery series	46,932	
Textile machinery components, special parts and other products	337,076	
	<u>2,215,239</u>	440,875
Other revenues		6,743
Distribution expenses		(67,140)
Administrative expenses		(222,174)
Net interest expenses		(3,852)
Other operating expenses, net		(51,125)
Share of profits of associated companies		1,174
Profit from ordinary activities		<u>104,501</u>
Major markets		
The People's Republic of China	1,921,409	383,880
Africa	38,307	7,328
Asia	200,813	38,857
Others	54,710	10,810
	<u>2,215,239</u>	<u>440,875</u>

**Section 1. Operation of the Company (continued)****3. Major subsidiaries and their operating status**

As at 31st December 2001, the Group's subsidiaries were as follows:-

Name of enterprise	Principal activities	Registered capital (RMB '000)	Equity interest held by the Company %	Net assets (RMB '000)	Net profit (RMB '000)
Zhengzhou New Hongda Textile Machinery Company Limited	Development and manufacture of textile machinery and related components and equipment	24,696.5	98	44,653	10,643
Qingdao Hongda Textile Machinery Company Limited	Manufacture, sale, repairing and leasing of textile machinery and related components and equipment	45,508.5	98	83,941	22,336
Shenyang Hongda Textile Machinery Company Limited	Development and manufacture of textile machinery and related components; providing technical consultation	33,097.8	98	43,141	1,799
Tianjin Hongda Textile Machinery Company Limited	Provision for technical consulting and sale of photocopiers and agriculture processing machinery, as well as related components	30,349.2	98	45,725	13,500
Beijing Jingwei Textile Machinery New Technology Company Limited (Note 1)	Technical development, sale of textile machinery and computer hardware and software, sale of agricultural machinery instruments and meters as well as automobile components	100,000	98.4	102,646	(111)
Shanghai Jingwei Dongxing Blowing-Carding Machinery Company Limited	Production and sale of combing machine and related products	50,000	88	54,277	4,277

4. Major customers and suppliers

The percentage of the Group's purchases for the year ended 31st December 2001 attributable to the five largest suppliers of the Group was 5.49%.

The percentage of the Group's turnover for the year ended 31st December 2001 attributable to the five largest customers of the Group was 13.96%.

Except as disclosed above, as at 31st December, 2001, none of the directors and supervisors of the Company or any of their associates (as defined by the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited) or any shareholders (which, to the best knowledge of the directors owns 5% or more of the Company's issued share capital) had any beneficial interest in the Group's five largest customers or five largest suppliers.

5. Difficulties encountered in operations and solutions

The year of 2001 saw a downward pricing trend in the textile machinery market while the new investment projects of the Company were still in their infancy period. Accordingly, the Company was operating under pressure. However, the Company was actively involved in the development of new products and enhancement of product performance and quality with a view to increasing its competitiveness. The Company also made extra efforts in market access and adjustments in its product portfolio. For best-selling models, production was expanded and internal management was strengthened to reduce operating costs. These measures proved to be significantly effective.

Section 2. Investments of the Company

(1) Use of proceeds from the issue of shares

In May 2000, the Company issued 180,000,000 A Shares and the net proceeds arising therefrom, after deduction of related listing expenses, were RMB1,234,800,000. During the reporting period, the proceeds had been used for the following purposes in accordance with the prospectus.

- (i) new cotton yarn equipment project with investment of RMB116,470,000;
- (ii) high-end series of machines for non-woven fabric and finishing with investment of RMB20,000,000;
- (iii) establishment of technological development centre project with investment of RMB63,060,000
- (iv) development of new model of shuttleless loom with investment of RMB16,390,000;
- (v) national project of localizing the production of major technical equipment with investment of RMB22,000,000
- (vi) commercialization of new and high technology with investment of RMB45,000,000;
- (vii) establishment of an information centre and a CIMS system with investment of RMB11,660,000; and
- (viii) replenishment for working capital of RMB113,780,000

The above projects had utilized a total of RMB408,360,000 in addition to the amount utilized in 2000 of RMB298,670,000. As at 31st December 2001, funds not yet utilised and deposited in banks amounted to RMB527,770,000. In order to make the best use of the proceeds, the Company will invest the rest of the proceeds in phases according to project progress and actual circumstances.

(2) Other investments

On 10th October 2001, the Company entered into a supplemental agreement to the Sales and Purchase Contract of Real Estate with Beijing City Development Group Company Limited (北京城市開發集團有限公司) ("BCD Group") and Beijing Hualian Composite Supermarket Company Limited (北京華聯綜合超市有限公司) ("Hualian") in Beijing, pursuant to which a property in the "Aiancun" section of the Commercial Service Centre at "WWUJU District" (五路居地區) Chaoyang District, Beijing, the PRC, which was owned by BCD Group and comprising a basement and three storeys of a building with the relevant land use right for construction with gross floor area of 24,887.64 sq.m., was transferred to the Company at a selling price of RMB12,950 per sq. m., which amounted to an aggregate price of RMB322.2949 million. The purchase of the "Aiancun" property was for a long-term commercial lease to Hualian. The purchase itself was not related to the Company's issue of additional shares in 2000 and was to be fully settled by cash. As at 31st December 2001, the purchase price was fully settled and the documentation of the relevant title certificate is currently in progress. The related announcement was published in the China Securities Post, Securities Times, Hong Kong Wen Wei Po and Hong Kong iMail on 11th October 2001.

**Section 3. Financial Position of the Group****Under PRC GAAP**

Item	2001 RMB'000	2000 (restated) RMB'000	2000 RMB'000	Percentage of change (%)	Reasons for change
Total assets	4,012,056	3,634,027	3,673,565	+10.40	– increase in borrowings and realization of profit during the year
Long term liabilities	93,075	71,290	71,290	+30.56	– increase in borrowings
Shareholders' equity	2,175,492	2,088,777	2,128,315	+4.15	– realization of profit during the year
Profit from principal activities	434,459	362,410	362,410	+19.88	– increase in sales revenue
Net profit	122,888	127,341	133,933	-3.50	– expiry of tax exemption for subsidiaries

Section 4. Business plan for 2002

In 2002, the Company will continue to pursue the strategy with textile as its focus complemented by diversified development. Its strategic targets are to perfect its core business and to become an industry leader and a strong enterprise. The Company is committed to establishing itself as a diversified, internationalized and modernized conglomerate with international competitiveness.

1. More efficient use of the operating capital, accelerate the regrouping of factors of production, optimize resources allocation and accelerate the structural adjustments in the product and business portfolios.
2. Further strengthening of internal management, tighter control over cost, upgrading of product quality and enhancing the competitiveness.
3. Strengthening of market analysis, research and forecast, rationalization of corporate marketing network, enhancing market development and increase efforts to capture more market share.
4. Accelerate the digitalization of corporate information, stepping up of the CIMS project and upgrading the modernization in corporate management.
5. Deepening of corporate reform, change of business operation mechanism, more efforts in the training of talents and advancement of corporate culture construction.

A board meeting of the Company was held on 5th February 2002 to propose the following investments:

Acquisition of 95% equity interests of Changde Textile Machinery Company Limited and 64.38% of Yichang Textile Machinery Company held by the ultimate holding company at RMB40,232,000 and RMB41,207,600 respectively;

The Company's acquisition of the fixed assets held by the Jingwei Group at RMB20,927,800 and the acquisition of the fixed assets held by Qingdao Textile Machinery Factory by Qingdao Hongda at RMB17,472,800; Zhengzhou Hongda's acquisition of the fixed assets held by Zhengzhou Textile Machinery Factory at RMB12,103,700; Tianjin Hongda's acquisition of the fixed assets held by Tianjin Textile Machinery Factory at RMB12,075,100; and Shenyang Hongda's acquisition of the fixed assets held by Shenyang Textile Machinery Factory at RMB9,710,100;

Establishment by the Company and the ultimate holding company of two companies, namely Wuxi Textile Technology Testing Company Limited and Hongda Non-woven Fabric Engineering Technology Company Limited; and

Sale by the Company to the ultimate holding company of the operating assets in respect of the manufacture of chemical fibre textile machinery production line. Total assets and total liabilities were RMB131,011,700 and RMB101,785,500 respectively. Net assets were RMB29,226,200.

Section 5. Report on the work of the Directors

1. Board meetings held during the period of this report and contents of resolutions passed

- (1) On 9th April 2001, the ninth meeting of the second term of the Board of Directors was held in Beijing and the following resolutions were considered and passed:
 1. the annual report of the Company for 2000 and its summary;
 2. the profit distribution proposal of the Company for 2000: the Company realised net profit of RMB133,311,000, 10% of which, i.e. RMB13,331,000 will be appropriated to each of the statutory reserve and the statutory public welfare fund pursuant to the Articles of Association of the Company. The remaining balance of RMB106,649,000, when combined with the undistributed profit of RMB127,120,000 brought forward at the beginning of the year, resulted in a total profit of RMB233,769,000 available for distribution to the shareholders. A final dividend of RMB0.11 per share amounting to a total of RMB66,418,000 was proposed;
 3. The 2001 profit distribution proposal for the Company comprises:
 - (1) Dividend distribution for 2001 will be made once;
 - (2) The percentage of the net profit available for distribution for 2001 will be at least 10%;
 - (3) The percentage of the undistributed profit available for distribution at the end of 2000 will not be less than 20%; and
 - (4) The dividend distribution in respect of 2001 will be in the form of cash. The Board of the Company reserves its rights to adjust the dividend distribution policy subject to the actual circumstances then;
 4. Mr. Lu Chengye ceased to be a director of the Company and that Mr. Liu Haitao be nominated as a candidate of director; and
 5. The content of Article 15 of the constitution which reads “The scope of operations of the Company includes: ... development and sales of computer softwares; sale of the Company’s products domestically and externally; engaging in import and export trade; technological and economic information enquiry services related to the Company’s products.” be amended as “The scope of operations of the Company includes: ... development and sales of computer softwares; sale of the Company’s products domestically and externally; engaging in import and export trade; technological and economic information enquiry services related to the Company’s product; also involving in the operation of aluminium, wood, metal and chemical products, non-ferrous metals, daily necessities, household electrical appliances, decorations, conferences, leasing activities and sales and purchase agency etc.”

The press announcement in respect of the resolutions considered and passed was published on 10th April 2001 in the China Securities Post and the Securities Times in the PRC and in the Wen Wei Po and the Hong Kong iMail in Hong Kong.



Section 5. Report on the work of the Directors (continued)

1. Board meetings held during the period of this report and contents of resolutions passed (continued)

- (2) On 28th June 2001, the tenth meeting of the second term of the Board of Directors was held in Beijing and resolutions in respect of the following were considered and passed:

1. Article 121 of the constitution, which reads “The supervisory committee shall be composed of five supervisors, one of whom as the chairman of the committee. The appointment and removal of the chairman of the supervisory committee shall be subject to more than two thirds of the affirmative votes by supervisors.”, be amended as “The supervisory committee shall be composed of seven supervisors, one of whom as the chairman of the committee and another as the vice-chairman. A supervisor shall be appointed for a term of three years and may be reelected. The appointment and removal of the chairman of the supervisory committee shall be subject to more than two thirds of the affirmative votes by supervisors.” and Article 122 of the constitution, which reads “Three of the supervisors shall be represented by shareholders and by staff members. Shareholders’ representatives shall be elected or removed by general meetings and staff representatives shall be elected or removed among staff members.” be amended as “Four of the supervisors shall be represented by shareholders and by staff members. Shareholders’ representatives shall be elected or removed by general meetings and staff representatives shall be elected or removed among staff members.”; and
2. election of next term of the members of the board of directors and the supervisory committee and the remunerations for directors and supervisors.

The press announcement in respect of the resolutions considered and passed was published on 29 June 2001 in the China Securities Post and the Securities Times in the PRC and in the Wen Wei Po and the Hong Kong iMail in Hong Kong.

- (3) On 15th August 2001, the first meeting of the third term of the Board of Directors was held in Beijing and the following resolutions were considered and passed:

- 1 the election of Mr. Lu Yunliang as Chairman of the Company; and
- 2 the election of Mr. Fan Xinmin as Vice-chairman of the Company.

The press announcement in respect of the resolutions considered and passed was published on 16th August 2001 in the China Securities Post and the Securities Times in the PRC and in the Wen Wei Po and the Hong Kong iMail in Hong Kong.

- (4) On 17th August 2001, the second meeting of the third term of the Board of directors was held in Beijing and resolutions in respect of the following were considered and passed:-

1. the interim report of the Company for 2001 and its summary; and
2. the proposal of not making any profit distribution nor increase in share capital by means of transfers from capital reserve for the interim report of 2001.

The press announcement in respect of the resolutions considered and passed was published on 20th August 2001 in the China Securities Post and the Securities Times in the PRC and in the Wen Wei po and the Hong Kong iMail in Hong Kong.

- (5) On 10th October 2001, the third meeting of the third term of the Board of Directors was held in Beijing and resolutions in respect of the following were considered and passed:

It was decided that an amount of RMB322,294,900 would be used to acquire a property in Qian Village, Beijing, comprising the basement and three storeys of a building, with gross floor area of approximately 24,887.64 sq. m. (actual area subject to the building ownership certificate), plus the relevant land use right for construction purposes.

The press announcement in respect of the resolutions considered and passed was published on 20th October 2001 in the China Securities Post and the Securities Times in the PRC and in the Wen Wei Po and the Hong Kong iMail in Hong Kong.

2. Implementation of resolutions passed during the shareholders’ meeting

During the year, the Directors of the Company had implemented all the resolutions and had distributed dividends to shareholders of A shares and H shares accordingly.

Section 6. Profit distribution proposal and capitalisation of surplus reserve

1. Profit distribution proposal for 2001

In 2001, the parent company of the Company realized a net profit of RMB122,204,000, 10% of which amounting to RMB12,220,000 will be appropriated to each of the statutory surplus reserve and statutory public welfare fund in accordance with the Articles of Association of the Company. The balance of the current year's profit of RMB97,764,000 available for distribution, when combined with the undistributed profit of RMB135,721,000 at the beginning of the year, amounted to RMB233,485,000 which was available for distribution to the shareholders. A final dividend of RMB0.06 (inclusive of tax) per share is proposed, totalling RMB36,228,000. The balance of the undistributed profit of RMB197,257,000 will be carried forward to the following year.

2. Forecast of profit distribution policy for 2002

- (1) Dividend distribution for 2002 will be made once ;
- (2) The percentage of the net profit available for distribution for 2002 will be at least 10 %;
- (3) The percentage of the undistributed profit available for distribution as at the end of 2001 will not be less than 20%; and
- (4) The dividend distribution in respect of 2002 will be in the form of cash. The Board of Directors reserves its rights to adjust the dividend distribution policy subject to the actual circumstances then.