Report of the Directors

The Directors are pleased to submit their report together with the audited financial statements for the year ended 31st December 2001 to the shareholders.

Review of operations

Results

Under the financial statements prepared in accordance with PRC accounting standards for the year ended 31st December 2001, the principal operating income of the Company and its subsidiaries ("the Group") amounted to RMB2,076,603,000, representing a decrease of 6.55% over that of last year. The consolidated net profit after taxation and minority interest amounted to RMB8,978,000, representing a significant improvement over its loss position of RMB725,869,600 in 2000. The earnings per share was RMB0.018. Under the financial statements prepared in accordance with accounting principles generally accepted in Hong Kong for the year ended 31st December 2001, the turnover of the Group amounted to RMB2,076,603,000, representing a decrease of 6.55% over that of last year. The loss attributable to shareholders amounted to RMB5,160,000, representing a significant decrease in loss of RMB729,042,000 in 2000. The loss per share was RMB0.0104.

In 2001, the reduction in turnover of the group was attributable to the significant decrease in operation of container business. Furthermore, the Group's recovery from the previous year's loss position to a profitable position (a significant decrease in loss under accounting principles generally accepted in Hong Kong) can be attributed to its effective operation on budgetary and cost management and additional provision for the trust deposits with non-banking financial institutions was not considered necessary. This was largely due to the effective operation.

Roof of Guangzhou Gymnasium

Report of the Directors

Principal operations

Shipbuilding

In the 2001 year, the Group completed and delivered five vessels including three 35,000dwt product oil tankers for a Danish customer, one 40,000dwt product oil tanker and one 28,000dwt multipurpose vessel for domestic customers. The total completed tonnage of 173,000dwt was ranked sixth in the China Shipbuilding Industry (note) in 2001. The Group commenced construction work on nine vessels, six of which were launched in 2001. These vessels included a 38,000dwt product oil tanker for a Malta customer, a 35,000dwt product oil tanker for a Danish customer, a 1600 Ro/PAX vessel for a Swedish customer, a 40,000dwt product oil tanker and one 18,000dwt semi-submarine vessel for domestic customers. The construction of the1600 Ro/PAX vessel for a Swedish customer and 18,000dwt semi-submarine vessel for a domestic customer was considered as the most technologically advanced vessels within the shipbuilding industry in China. The progress of these two vessels were slow due to construction and cost controls were relatively difficult. Demands for technology and quality were high which reduced the income recognised and lowered the profit. The turnover from shipbuilding amounted to RMB1,407,794,000 and gross profit before taxation amounted to RMB 32,452,000 which represented a decrease of 5.53% and 38.33%, respectively over that of last year. The turnover attributable to shipbuilding represents 67.79% of the Group's turnover. Furthermore, the Group secured new orders for 11 vessels of which the total tonnage is 352,000dwt. This includes three 38,000dwt product oil tankers for a Malta customer, two 35,000wt product oil tanker for a Danish customer, four 42,000dwt product oil tanker and two auxiliary ships for domestic customers, with total contract value of RMB2,322,000,000. As at 31 December 2001, the Group has secured orders for 22 vessels with a total tonnage of 688,900dwt and a total contract value of RMB3,849,000,000.

1600 LM RO/RO passenger ships

Note: The information is extracted from the Secretariat of the Shipbuilding Industry Society.

Container manufacturing


Containers storing Yard

As demand in the international market has been diminishing, the manufacturing of containers by the Group was under production capacity during the year. The production of containers was occasionally stopped in the second half of the year which caused a significant decrease in production volume over that of last year. During the year, various containers with a total of 32,324TEU were manufactured by the Group and 32,378TEU were sold, representing a decrease of 44.05% and 36.23% over that of last year. The turnover from the manufacturing of containers amounted to RMB333,600,000 and gross profit before taxation amounted to RMB14,950,000. This represents a decrease of 35.91% and 53.71% respectively over that of last year. The turnover attributable to the container business represents 16.06% of the Group's turnover.

Shiprepairing

In 2001, the shiprepairing operation of the Group was growing steadily through the reorganisation of the ship repairing division as well as continuous development in high technology and complicated ship repairing projects. During the year, the repairing services for 36 vessels with various types were completed. The turnover from the ship repairing operation amounted to RMB23,479,000 and gross profit before taxation amounted to RMB3,059,000 which represent an increase of 11. 46% and 46.46%, respectively over that of last year. The turnover attributable to the ship repairing operation represents 1.13% of the Group's turnover.


Repairing dock

Steel structure

Although the steel structure operation of the Group encountered strong market competition, it has recovered from its loss position in last year. This recovery was mainly attributable to the enhancement of management as well as the continuous market development. The turnover contributed from the steel structure operation amounted to RMB68,473,000 and the contribution to gross profit before taxation amounted to RMB19,115,000. The major projects completed in 2001 included Macau Electricity Factory, Bei Lao Bridge, Guangdong Shun De Chen Chun Flower Center and Nan Hai Citizen Plaza. The turnover attributable to the steel structure operation represents 3.30% of the Group's turnover.

Nanhai CItizen Square

Greenhouse of Tropical plants in Beijing Botanical Garden

Centary Altar for the 9th National Games

Mechanical and electrical equipment and other operations

The mechanical and electrical equipment operations of the Group have achieved comparatively large growth despite deterioration in market conditions. The major projects completed in 2001 included container crane machine for Hong Kong Inside River Harbour and the building of the opening ceremony platform for the Ninth National. The turnover from the mechanical and electrical equipment and other operations amounted to RMB243,257,000 and gross profit before taxation amounted to RMB 22,970,000, representing an increase of 114.22% and 5% respectively over that of last year. The turnover attributable to mechanical and electrical and other operations represents 11.72% of the Group's turnover.

NC hydraulic bending machine

Geographical analysis of turnover

The countries/regions which contributed to more than 10% of the Group's annual consolidated turnover are listed as follows:

	Year ended 31 December	
Countries/Regions	**2001**	2000
	%	%
Mainland China	**26.89**	33.32
Sweden	**27.02**	2.25
Denmark	**11.93**	35.79
United States	**3.50**	8.10
The Netherlands	**1.13**	10.09
Others	**29.53**	10.45

Turnover from export operation

During the year, the Group's turnover attributable to exports amounted to US$170,771,300 (2000: US$178,994,900).

Major customers and suppliers

The turnover derived from the Group's five largest customers accounted for 67.79% of the turnover of the Group in 2001. The largest customer of the Group accounted for 27.02% of the turnover of the Group in 2001.

The purchase of raw materials and equipment from the Group's five largest suppliers accounted for 23.25% of the total purchases of the Group in 2001. The largest supplier of the Group accounted for 6.62% of the total purchases of the Group in 2001.

None of the Directors, Supervisors and their respective associates had any interests in the major customers and suppliers noted above, nor had any of the Company's shareholders disclosed to the Company that he or she had an interest in the above mentioned major customers or suppliers.

Major subsidiaries

The operation conditions of the Company's major subsidiaries, with 51% or more interest held, during the year are summarised as follows:

No	Company Name	Principal Activities	Registered Capital *RMB'000*	Interest Attributable to the Company *(%)*	Assets *RMB'000*	Net profit (loss) *RMB'000*
1.	Kwangchow Shipyard Container Factory	Container manufacturing	44,925	100	210,813	4,907
2.	Guangdong Guangzhou Shipyard International Elevator Company Limited	Elevator production and sales	21,000	95	24,135	1,059
3.	Guangzhou Jinfan Advertisement and Decoration Company	Advertising	1,400	90	-1,442	(261)
4.	Guangzhou Hongfan Information Technique Company Limited	Development ofcomputer software, system integration and sales of hardware	5,000	90	9,524	338
5.	Guangzhou Xinsun Shipping Service Company Limited	Welding and coating of ships	600	83	15,581	1,058
6.	Masterwood Company Limited	Furniture manufacturing	3,315	75	9,174	396
7.	Guangzhou Guanglian Container Transportation Company Limited	Container transportation	20,000	75	20,418	34
8.	Xinhui City Nanyang Shipping Industrial Company	Ship dismantling	15,000	70	31,602	–
9.	Guangzhou Sanlong Industrial Trading Development Co., Ltd.	Municipal construction project	1,500	67	3,651	(1,830)
10.	Guangzhou Haizhu District Guanghua Machinery Factory	Machine manufacturing	1,438	65	3,422	344
11.	United Steel Structures Limited	Large-sized steel structure	73,573	51	80,450	2545
12.	Guangzhou Shipyard Machinery Equipment Engineering Co. Ltd.	Mechanical & electrical product manufacturing and equipment maintenance	1,000	60	1,567	21
13.	Guangzhou Henghe Construction Co. Ltd.	Services, wholesale and retail	2,750	75.9	30,531	792

The above subsidiaries, which are established and operated in Mainland China, in the opinion of the Directors, represent those principally affected the Group's results of the year or formed a substantial portion of the net assets of the Group. In the opinion of the Directors, a full listing of the operating conditions for all subsidiaries will result in excessive length.

Status of the company's investments

During the year, the Company invested RMB116,171,000 in relation to technical improvement. The completed projects transferred to fixed assets during the year amounted to RMB63,248,000. The major projects included steel panel production line, conversion of the on production line for pipeline processing, conversion of the on second slipway and the extension on third crane production line.

According to the resolution of the Fifteenth Meeting of the third term Board of the Directors, the Company invested fixed assets amounted RMB17,500,000 as additional capital to Guangzhou Henghe Construction Company Limited. The registered capital has increased from RMB10,000,000 to RMB27,500,000 and the Company's shareholding has increased from 33.8% to 75.9%. Guangzhou Henghe Construction Company Limited is set up by the Company together with Shenzhen Shipbuilding Enterprise and China Machinery Installation Company and is engaged in steel structure construction.

Financial position of the Group

According to PRC accounting standards, the fluctuations in total assets, long-term liabilities, shareholders' equity, profit from principal operations, and net profit of the year as compared to last year are as follows:

(1) *In accordance with PRC accounting standard:*

Indicator	**2001**	**2000**	**Increase/ (decrease)**	**Main reason**
	RMB'000	*RMB'000*	*(%)*	
Total assets	**2,510,263**	2,396,910	4.72	Amonts received from oustomers and increase in loans
Long-term liabilities	**418,706**	282,474	48.23	Increase in bank loans
Shareholders' equity	**617,730**	608,663	1.49	Profit of the year
Principal operating profit	**90,319**	104,328	-13.43	Affected by sales volume
Net profit/(loss)	**8,978**	(739,770)	101.21	Specific provision for doubtful debts in last year

Prospects for the coming year

During 2001, the Group was facing the challenge of recovering the losses incurred in 2000. Although the Group encountered difficulties in controlling the costs associated with new and high technology ship construction as well as facing a significant decrease in the turnover of container manufacturing, the Group has managed to recover from its significant loss position in 2000 to a profitable position (a significant decrease in loss under accounting principls generally acepted in Hong Kong. This recovery can be attributed to the significant efforts contributed by the Group's employees, who will continue to strengthen the Group's development in 2002.

In 2002, the Group shall mobilise all staff again to exercise detailed management techniques moving the Group into the future. One major goal of the Group is to overcome difficulties associated with high technology ship construction. After the completion of the present construction of the first Ro/PAX vessel and semi-submarine vessel, the Group shall to fully utilise and expand the existing capacity in order to improve economic performance. The Group is contemplating to reloacte the container factory to cope with environmental protection requirements. In addition the Group will establish new sales and production systems to further develop of its major products. Moreover, the Group will continue to focus on the importance of people in order to enhance the internal incentive scheme, improve budgetary management, increase efficiency through cost saving, and ultimately to ensure improvements in the Group's performance.

Report of the Daily Operations of the Board of Directors

Meetings of the Board of Directors

During the year, the Board of Directors held eight meetings. The major points and resolutions arising from each of these meetings are as follows:

1. The Tenth Meeting of the third term of the Board of the Company was held on 10th January 2001. All 11 Directors voted by means of written resolution for the approval of the Company's subsidiary – "Xinhui City Nanyang Shipping Industrial Company" to change its name to "Xinhui City Guangzhou Shipyard International Nanyang Shipping Industrial Limited".

2. The Eleventh Meeting of the third term of the Board of the Company was held on 9th February 2001. 11 Directors presented and voted by written resolution for approval of an announcement of expected loss for 2000.

3. The Twelfth Meeting of the third term of the Board of the Company was held on 10th January 2001. The 10 Directors present voted by written resolution for the approval of provision for non-recovery of overdue trust deposits with non-banking financial institutions during 2000. They also approved to provide for the foreseeable losses associated with certain shipbuilding products.

4. The Thirteenth Meeting of the third term of the Board of the Company was held on 20th April 2001 with attendance by 11 Directors (including 1 valid proxy). 11 Directors voted for approval of the Company's Annual Report of 2000; approved the recommendation to reappoint Yangcheng Certified Public Accountants Company Limited and PricewaterhouseCoopers as the auditors for 2001; approved the resignation of Mr. He Suxia, Deputy General Manager of the Company; approved the resignation of Mr. Tao Quan, Deputy General Manager and Chief Accountant of the Company from the position of Chief Accountant; approved the financial budget for 2001; approved the total payment to workers in 2001; approved the tentative plan of production plant relocation of the Company's subsidiary – Kwangchow Shipyard Container Factory and Machinery Division, and agreed for management to prepare an executive plan; approved the resolution of recovering the trust deposits with Guangzhou International Trust and Investment Company; approved the amendment of the resolution of the Ninth Meeting of the third term Board of the Company to accept Guangzhou Foreign Economic and Trading International Trust and Investment Company to settle its overdue trust deposits through its interests in real estate in Changchun and Guangzhou; approved the housing subsidy policy of the Company; approved the resolution to close the following three branches: Transportation Team, Oxygen Producing Factory and Machinery Factory.

5. The Fourteenth Meeting of the third term of the Board of the Company was held on 22nd June. 11 Directors attended and voted by written resolution for approval of the amount of payment to be paid to the auditors for 2000, including an audit fee of RMB400,000 paid to Yangcheng Certified Public Accountants Company Limited, an Interim financial report review fee of HKD250,000 and annual audit fee HKD1,100,000 paid to PricewaterhouseCoopers; approved to authorize management to review the provision of shipbuilding products on a monthly basis.

6. The Fifteenth Meeting of the third term Board of the Company was held on 10th August 2001 with attendance by 10 Directors (including two valid proxies). 10 Directors all voted to approve the 2001 interim report, and propose that no distribution be made from interim profits; approved the executive plan of the Container factory's relocation; approved to invest fixed assets as additional capital to Guangzhou Henghe Construction Company Limited, which increased the shares held by the Company from 33.8% to 75.9% after the investment; approved the proposal of technical transformation applied to the 1600wt Ro/PAX shipbuilding project; approved Mr. Li Guanghui's resignation from Deputy General Manager; approved Mr. Chen Miaogen's resignation from Deputy General Manager; appointed Mr. Zhong Jian, Mr. Wang Yi and Mr. Han Guangde to the position of Deputy General Manager of the Company; approved the payment of HKD 250,000 to PricewaterhouseCoopers for fees relating to the review of the interim financial statements.

7. The Sixteenth Meeting of the third term of the Board of the Company was held on 21st September 2001, with attendance by 10 Directors. One Director opposed and 9 Directors voted by written resolution for approval of the debt transfer agreement reached between the Company's management and Guangzhou Hongli Investment Consulting Company Limited. Of the 10 directors who voted, five Directors voted against the resolution to authorize the Company's management to accept recovery rate of no less than 30% of the trust deposits due from Guangzhou Economic and Technology Development Zone International Trust and Investment Company and was therefore not approved.

8. The Seventeenth Meeting of the third term of the Board of the Company was held on 21st November, with attendance by 10 Directors. 10 Directors voted by written resolution for approval of the capital withdrawal from South China Marine and Industrial Special Coating Limited after the expiry of the period of co-operation; entitled the management of the Company to deal with the change in the equity of the US shareholder of United Steel Structures Limited.

The execution by the Board of Directors in respect of the resolution passed in the annual general meeting

During the year, the Board of Directors had executed all the resolutions passed in the 2000 annual general meeting.

Equity interests of Directors and Supervisors

Except for the disclosure under "Directors, Supervisors, senior management and staff", at no time during the year, had the Company been notified that the Directors and Supervisors (including their spouses and children under 18 years of age) had any interest in, or had been granted, or exercised, any rights to subscribe for shares or debentures of the Company and its associated corporations (within the meaning of the Securities (Disclosure of Interests) Ordinance ("SDI Ordinance")).

Service contracts of Directors and Supervisors

None of the Directors and Supervisors who were elected in the 1998 annual general meeting had entered into any service contract with the Company with payment of compensation for early termination of the service contract or non re-election upon the expiration of the service contract.

Interests of Directors and Supervisors in contracts

During the year, no contracts of significance in relation to the Company's business, to which the Company and its subsidiaries were a party to, and in which a Director and Supervisor of the Company had a material interest, whether directly or indirectly, were in existence.

The highest paid individuals

The five highest paid individuals are either Directors, Supervisors or senior management whose emoluments have been disclosed in "Directors, Supervisors, senior management and staff" noted above.

Profit forecast

The Company did not prepare any profit forecast for the period covered by this report.

Profit distributon forthe year 2001

As the Company has a profit of RMB8,978,000 in the financial statements prepared in accordance with the PRC accounting standards and a loss of RMB5,160,000 in the financial statements prepared in accordance with the accounting principles generally accepted in Hong Kong in 2001, spacing the Directors do not recommend any profit distribution or capital increment. This proposal will be submitted to 2001 annual general meeting for approval.

Financial summary

Summaries of the results and of the assets and liabilities of the Group for the last five financial years in accordance with the PRC accounting standards and accounting principles generally accepted in Hong Kong are set out on page 5 and page 6, respectively.

Results and profit distribution

The results and profit distribution of the Group for the year ended 31st December 2001 prepared under PRC accounting standards and the accounting principles generally accepted in Hong Kong are set out in the profit and loss statement on page 37 and consolidated profit and loss account on page 79.

Dividend

The Directors do not recommend the payment of dividend.

Reserves

The movements in the reserves of the Group which are prepared under PRC accounting standards and the accounting principles generally accepted in Hong Kong are set out in note 19 to the financial statements on page 65 and 40 and note 23 on page 107 to 110, respectively.

Fixed assets

Details of movements in fixed assets (including properties and other tangible assets) of the Group which are prepared under PRC accounting standards and the accounting principles generally accepted in Hong Kong are set out in note 7(1) to the financial statements on page 59 and 60 and note 10 on page 98 and 99, respectively.

Properties held for development or sale

The Group has no property held for development or sale, which represents over 15% of the value of net tangible assets, or where contribution derived from these properties exceeded 15% of pre-tax operating profit.

Share capital

Details of the share capital of the Company are set out in "Share capital structure" on page 10.

Pre-emptive rights

As there is no provision for pre-emptive rights under the Company's Articles of Association, the Company had not arranged any scheme for such right during the year.

Warrants and others

During the year, neither the Company nor its subsidiaries have issued any warrants, convertible securities, options or other securities with similar rights, nor had any person exercised any right noted above.

Purchase, sale or redemption of the Company's securities

Neither the Company nor its subsidiaries made any purchase, sale or redemption of the Company's securities during the year.

Bank loans, overdraft and other borrowings

Details of bank loans, overdraft and other borrowings of the Group are set out in note 12 and 17 to the financial statements on page 61 and 65 and note 24 on page 111, respectively.

Interest capitalisation

Details of interest capitalisation of the Group during the year are set out in note 9 to the financial statement on page 60.

Application of Statutory Public Welfare Fund

During the year, the Company utilised its statutory public welfare fund for the purchase of medical facilities for the welfare of the Company's employees. The amount transferred to fixed assets was RMB710,000.

Connected transactions

The connected transactions made between the Group and the associated enterprises under the control of CSSC or associated companies of the Group included sales of goods amounting to RMB7,520,000 and purchases of raw materials and other expenses amounting to RMB102,720,000. Those connected transactions are audited by the Company's independent directors, and confirmed by its non-executive independent directors, Mr. David Hon To YU and Mr. Philip Pat Yiu YUEN, that they were carried out in the ordinary course of business and had been entered into accordance with the terms of the agreement covering such transactions or (where there is no such agreement) on terms no less favourable than terms available to third parties. The Group did not receive any extra-ordinary benefit from such transactions, which are considered as reasonable to the Group's shareholders. Details of such transactions are set out in note vi to the financial statements prepared under PRC accounting standards on page 72 to 77.

The above transactions, which also constitute related party transactions under the listing rules of the Stock Exchange of Hong Kong Limited ("Listing Rules"), require disclosure in accordance with Chapter 14 of the Listing Rules. Details are set out in note 28 to the financial statements prepared under the Hong Kong generally accepted accounting principles on page 114.

Application of proceeds from share offering

The Company had not raised funds during the year and the proceeds previously raised had been fully utilised.

Employees' pension scheme

The Company and certain subsidiaries have joined the defined contribution retirement scheme operated by the provincial government of Guangdong Province since 1st January 1994. Under the scheme, the relevant group companies are required to make contributions at 18% of the standard salaries. Upon retirement, the retirees will receive monthly payments from the Social Insurance Bureau of Guangdong Province. Contributions made by the Group for the year ended 31st December 2001 was RMB21,861,000 (2000: RMB20,090,091). In addition, the Company has operated a supplemental defined contribution retirement scheme since 1st March 1995. Under this scheme, the relevant group companies and the employees are required to make contributions at 10% and 5% of a specified amount of the employees' monthly salaries respectively. The staff will receive both contributions plus interest upon retirement. Contributions made by the Group for the year ended 31st December 2001 was RMB2,618,886 (2000: RMB2,315,397). Contributions by the Group forfeited as a result of resignation of the employees before retirement totalling RMB206,778 (2000: RMB169,256) are utilised for the welfare of retirees. In addition, during the year the Group had made payments of RMB636,453 (2000: RMB643,824) as subsidies to retirees.

Purchase of staff quarters by employees

Guangzhou Shipyard owns staff quarters occupied by employees of the Company. Accordingly, the staff quarters provided to the Company's employees by Guangzhou Shipyard are in accordance with the State and Guangzhou City's housing reform policy and the Company was not involved in the selling of staff quarters to the employees.

Publications for disclosure

The Publications used for disclosing information of the Company during the year 2001 are "Shanghai Securities News", "Hong Kong Commercial Daily" and "Hong Kong iMail".

Code of Best Practice

The Board of Directors have not established an audit committee (the "Audit Committee") to review and supervise the Company's financial reporting procedures and internal controls pursuant to paragraph 14 of Code of Best Practice set out in Appendix 14 of the Listing Rules (the "Code of Best Practice"). However, the Company's organisational structure includes a supervisory committee (the "Supervisory Committee") which carries out functions similar to that of an Audit Committee. The differences being that the representatives of the Supervisory Committee (one of which shall be the representative of the Company's employees) are elected and removed by shareholders in general meeting, and the Supervisong Committe is responsible to report to shareholders in general meeting of shareholders instead of the Board of Directors, whereas the Listing Rules require the Audit Committee comprise of independent non-executive Directors of the listed company. Apart from this, none of the Directors is aware of any information that would reasonably indicate that the Company is not, or was not at any time during the year, in compliance with the Code of Best Practice.

Significant litigation

Details of significant litigation of the Group during the year are set out in note 1 in "Significant Events" on page 32.

Auditors

The financial statements for the year ended 31st December 2001 prepared under PRC accounting standards and the accounting principles generally accepted in Hong Kong have been audited by Yangcheng Certified Public Accountants Company Limited and PricewaterhouseCoopers, respectively. They shall respectively resign and, being eligible, offer themselves for re-appointment.

Acknowledgment

The Board of Directors would like to extend its sincere gratitude to various customers for their trust in the Company, and to the shareholders for their valuable support to the Company, and to the staff for their efforts and dedication to the Company's development.

On behalf of the Board
Chairman
Hu Guoliang

Guangzhou, 19th, April 2002