

AUDITORS' REPORT

Xian Xigema Certified Public Accountants Firm Limited

Xi Hui Shen Zi Audit Report (2003) No.318

We were engaged to audit the balance sheet and the consolidated balance sheet of Jiaoda Kunji High-Tech Company Limited as at 31st December, 2002, the statement of income for 2002, the statements of income appropriation and consolidated income statement, income appropriation statement and cash flows statement and consolidated cash flows statement for 2002. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Independent Auditing Standards for Chinese Certified Public Accountants. Our audit included such tests of the accounting records and such other auditing procedures as we considered necessary in the practical circumstances of the Company.

In our opinion, such financial statements are prepared in conformity with "Accounting Standards for Business Enterprises" and "Accounting System for Business Enterprises" and, in all material respects, present fairly the financial position of the Company as at 31st December, 2002 and the results of its operations and cash flows for the year then ended. The accounting policies adopted follow the consistency principle.

Enclosures: 1. Balance Sheet
 2. Income Statement, Income Appropriation Statement and Consolidated Income Statement and Income Appropriation Statement
 3. Cash Flows Statement
 4. Notes to the Financial Statements

Xian Xigema Certified Public
Accountants Firm Limited
Xian, the PRC
Project Manager: Liu Bin
Auditor: Gao Hong
Signatory: Fan Min Hua

6th April, 2003

BALANCE SHEET

Unit: RMB

ASSETS	Notes	31st December, 2002 The Group	The Company	31st December, 2001 The Group	The Company
CURRENT ASSETS:					
Bank balances cash	5.1	202,607,334	161,859,776	153,538,588	151,877,168
Short-term investments	5.2	13,500	13,500	42,129,951	42,129,951
Bills receivable		1,820,000	—	1,908,000	—
Dividends receivable		—	—	—	—
Interest receivable		—	—	—	—
Accounts receivable	5.3	56,122,279	36,228,059	41,252,568	37,670,112
Other receivables	5.4	15,588,696	31,198,992	18,178,945	16,720,412
Prepayments	5.5	11,024,018	748,803	5,631,055	1,438,587
Subsidies receivable		—	—	—	—
Inventories	5.6	195,479,030	169,384,078	162,261,021	153,351,208
Prepaid expenses	5.7	270,578	—	399,554	126
Loss on deferrend current assets, net		—	—	—	—
Long-term debt investment due within one year		—	—	—	—
TOTAL CURRENT ASSETS		482,925,435	399,433,208	425,299,682	403,187,564
LONG-TERM INVESTMENTS:					
Long-term equity investments	5.8	13,813,775	71,149,477	15,070,862	22,843,069
Of which: consolidated difference in value		13,563,775	—	—	—
Of which: difference in equity investments		13,563,775	—	—	—
Long-term debt investment		—	—	—	—
Total long-term investments		13,813,775	71,149,477	15,070,862	22,843,069
FIXED ASSETS:					
Fixed assets at cost	5.9	366,513,174	330,375,455	346,219,439	322,695,527
Less: Accumulated depreciation		127,055,068	116,899,690	109,100,355	104,516,466
FIXED ASSETS, NET BOOK VALUE		239,458,106	213,475,765	237,119,084	218,179,061
Less: Provision for impairment loss		2,592,053	2,592,053	2,722,991	2,722,991
FIXED ASSETS, NET REALISABLE VALUE		236,866,053	210,883,712	234,396,093	215,456,070
Project materials		—	—	—	—
CONSTRUCTION IN PROGRESS, NET REALISABLE VALUE					
Unsettled disposal of fixed assets	5.10	43,545,559	39,139,163	35,073,817	35,031,717
Loss on deferred fixed assets, net		—	—	164,172	164,172
TOTAL FIXED ASSETS		280,411,612	250,022,875	269,634,082	250,651,959
INTANGIBLE AND OTHER ASSETS					
Intangible assets	5.11	60,969,335	40,770,394	66,102,919	66,102,919
Long-term deferred expenditures	5.12	1,349,054	691,260	—	—
Other long-term investments		—	—	—	—
TOTAL INTANGIBLE AND OTHER ASSETS		62,318,389	41,461,654	66,102,919	66,102,919
DEFERRED TAXATION:					
Deffered taxation		—	—	—	—
TOTAL ASSETS		839,469,211	762,067,214	776,107,545	742,785,511

Company's Representative: Yue Huafeng
Financial Controller: Liu Jian
Prepared by: Zhao Qiongfen

BALANCE SHEET

Unit: RMB

LIABILITIES AND SHAREHOLDERS' EQUITY	Notes	31st December, 2002 The Group	The Company	31st December, 2001 The Group	The Company
CURRENT LIABILITIES:					
Short-term loans	5.13	159,000,000	159,000,000	120,200,000	120,000,000
Bills payable		—	—	—	—
Accounts payable	5.14	18,879,494	6,405,614	10,165,500	7,766,799
Advances from customers	5.15	55,070,306	28,309,205	28,519,829	17,355,298
Payroll payable	5.16	75,774	—	3,416,690	3,416,690
Accrued welfare		2,064,733	465,424	1,328,734	563,742
Dividends payable		1,060,761	—	—	—
Taxes payable	5.17	8,927,275	5,793,232	14,253,232	12,895,557
Other taxes payable	5.18	119,224	—	—	—
Other payables	5.19	9,771,281	1,278,891	30,111,143	15,463,576
Accrued expenses	5.20	4,097,327	3,250,000	2,154,690	1,540,560
Estimated liabilities		—	—	—	—
Long-term loans due within one year	5.21	30,013,210	30,013,210	10,552,523	10,552,523
Other current liabilities		—	—	—	—
TOTAL CURRENT LIABILITIES		289,079,385	234,515,576	220,702,341	189,554,745
LONG-TERM LIABILITIES:					
Long-term loans	5.22	6,000,000	3,000,000	34,102,437	34,102,437
Long-term payable	5.23	11,037,762	3,837,762	4,050,971	4,050,971
Specific project payable	5.24	2,490,406	2,490,406	2,065,806	2,065,806
Deferred gain	5.25	11,445,425	11,445,425	12,310,986	12,310,986
TOTAL LONG-TERM LIABILITIES		30,973,593	20,773,593	52,530,200	52,530,200
DEFERRED TAXATION:					
Deferred taxation		—	—	—	—
TOTAL LIABILITIES		320,052,978	255,289,169	273,232,541	242,084,945
MINORITY INTEREST		12,638,188	—	2,174,438	—
SHAREHOLDERS' EQUITY:					
Share capital	5.26	245,007,400	245,007,400	245,007,400	245,007,400
Less: Returned on investment		—	—	—	—
Share capital, net		245,007,400	245,007,400	245,007,400	245,007,400
Capital reserves	5.27	305,280,480	305,280,480	305,280,480	305,280,480
Surplus reserve	5.28	16,812,656	16,812,656	16,812,656	16,812,656
Including: Statutory public welfare fund		8,406,328	8,406,328	8,406,328	8,406,328
Unappropriated profits	5.29	(60,322,491)	(60,322,491)	(66,399,970)	(66,399,970)
TOTAL SHAREHOLDERS' EQUITY		506,778,045	506,778,045	500,700,566	500,700,566
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		839,469,211	762,067,214	776,107,545	742,785,511

Company's Representative: Yue Huafeng

Financial Controller: Liu Jian

Prepared by: Zhao Qiongfeng

STATEMENT OF INCOME AND APPROPRIATION

Unit: RMB

ITEMS	Notes	2002		2001	
		The Group	The Company	The Group	The Company
1. Principal operating income	5.30	179,628,485	146,248,123	102,493,975	102,493,975
Less: Principal operating cost		120,047,698	94,861,386	77,526,169	77,526,169
Direct operating expenses	5.31	235,954	88,076	—	—
2. Principal operating profit		59,344,833	51,298,661	24,967,806	24,967,806
Add: Income from other operations	5.32	2,840,696	2,733,696	599,645	599,645
Less: Selling expenses		11,520,949	9,908,747	5,522,625	5,522,625
Administrative expenses		37,381,994	37,205,388	17,533,853	17,533,853
Financial expenses	5.33	7,805,693	6,888,030	4,872,072	4,872,072
3. Operating profit		5,476,893	30,192	(2,361,099)	(2,361,099)
Add: Investment income	5.34	1,013,989	5,127,483	3,273,201	3,273,201
Subsidy income	5.35	1,322,691	1,322,691	1,700,000	1,700,000
Non-operating income	5.36	299,834	166,250	14,646,831	14,646,831
Less: Non-operating expenses	5.37	379,343	375,843	15,207,812	15,207,812
4. Profit before income tax		7,734,064	6,270,773	2,051,121	2,051,121
Less: Income tax	5.38	722,835	193,294	—	—
Minority interest		933,750	—	—	—
5. Net profit for the period		6,077,479	6,077,479	2,051,121	2,051,121
Add: Accumulated losses at beginning of the year		(66,399,970)	(66,399,970)	(68,451,091)	(68,451,091)
6. Profit for distribution		(60,322,491)	(60,322,491)	(66,399,970)	(66,399,970)
Less: Statutory surplus reserve		—	—	—	—
Statutory public welfare fund		—	—	—	—
Employee welfare and bonus		—	—	—	—
Reserve fund		—	—	—	—
Corporate development fund		—	—	—	—
Return on investment		—	—	—	—
7. Profit available for distribution to shareholders		(60,322,491)	(60,322,491)	(66,399,970)	(66,399,970)
Less: Preference shares dividend paid		—	—	—	—
Surplus reserve		—	—	—	—
Ordinary share dividend paid		—	—	—	—
Convertible share dividend		—	—	—	—
8. Unappropriated profit		(60,322,491)	(60,322,491)	(66,399,970)	(66,399,970)

Company's Representative: Yue Huafeng

Financial Controller: Liu Jian

Prepared by: Zhao Qiongfen

CASH FLOW STATEMENT

		Unit: Rmb	
Item	Notes	The Group	The Company
1. Cash flows from operating activities:			
Cash received from sales of goods or rendering of services		230,370,549	191,347,353
Refund of taxes and surcharges received other cash received relating to operating activities		1,322,691	1,322,691
Sub-total of cash inflows		231,693,240	192,670,044
Cash paid for goods and services		125,662,103	105,101,281
Cash paid to and on behalf of employees		44,181,682	40,624,660
Taxes and surcharges paid		21,712,124	19,337,906
Other cash paid relating to operating activities	5.39	44,618,651	62,899,931
Sub-total of cash outflows		236,174,561	227,963,778
Net cash flows from operating activities		(4,481,320)	(35,293,733)
2. Cash flow from investing activities:			
Cash received from refund of investment		46,737,226	46,737,226
Cash received for investment income		—	—
Net cash received from disposal of fixed assets, intangible assets and other long term assets		743,716	610,863
Other cash received relating to investing activities		—	—
Sub-total of cash inflows		47,480,942	47,348,089
Cash paid to acquire fixed assets, intangible assets and long term assets		30,466,284	13,943,693
Cash paid for investment		3,613,000	5,240,365
Other cash paid relating to investing activities		—	—
Sub-total of cash outflows		34,079,284	19,184,058
Net cash flows from investing activities		13,401,658	28,164,031
3. Cash flows from financing activities			
Cash from proceeds for use of investment		9,530,000	—
Including: Cash from proceeds arising from minority fund		9,530,000	—
Cash from borrowings		37,569,641	27,569,641
Other cash received relating to financing activities		—	—
Sub-total of cash inflows		47,099,641	27,569,641
Cash repayments of borrowings		8,214,533	8,357,631
Cash payments for distribution of dividends or profits and payments of interest expenses		—	—
Including: dividend paid by subsidiaries to minority shareholders		—	—
Other cash paid relating to financing activities		—	—
Sub-total of cash outflows		8,214,533	8,357,631
Net cash flows from financing activities		38,885,108	19,212,010
4. Effect of foreign exchange rate changes on cash		—	—
5. Net increase in cash and cash equivalents		47,805,446	12,082,308

Company's Representative: Yue Huafeng

Financial Controller: Liu Jian

Prepared by: Zhao Qiongfen

CASH FLOW STATEMENT

		Unit: Rmb	
Item	Notes	The Group	The Company
1.	Reconciliation of profit to cash flows from operating activities:		
	Net profit	6,077,478	6,077,478
	Add: Gain or loss of minority shareholders	933,750	—
	Provision for diminution in value of assets	(11,102,086)	(12,358,231)
	Amortization of deferred income	(865,561)	(865,561)
	Depreciation of fixed assets	18,438,630	15,171,011
	Amortization of intangible assets	5,622,805	4,896,813
	Amortization of long term deferred expenses	553,590	—
	Decrease in deferred expenses (less: increase)	128,976	126
	Increase in accruals (less: decrease)	1,942,637	1,709,440
	Loss on disposal of fixed assets, intangible assets and other long term assets (less: income)	264,171	397,025
	Loss on deserted fixed assets	—	—
	Financial expenses	7,805,693	6,888,030
	Investment loss (less: income)	4,712,810	599,316
	Credit on deferred tax (less: borrowing)	—	—
	Decrease in inventory (less: increase)	(30,744,126)	(33,279,289)
	Decrease in operating receivables (less: increase)	(15,240,098)	(9,320,597)
	Increase in operating payables (less: decrease)	7,112,957	(15,209,295)
	Others	—	—
	Net cash flows from operating activities	(4,358,373)	(35,293,733)
2.	Financing and investing activities not involved in cash:		
	Debts capitalized	—	—
	Convertible bond due within one year	—	—
	Fixed assets under financial lease	—	—
3.	Net increase in cash and cash equivalents:		
	Cash and bank balances at the end of the period	162,101,834	124,717,276
	Less: cash and bank balances at the beginning of the period	114,296,388	112,634,968
	Add: cash equivalents at the end of the period	—	—
	Less: cash equivalents at the beginning of the period	—	—
	Net increase in cash and cash equivalents	47,805,446	12,082,308

Company's Representative: Yue Huafeng

Financial Controller: Liu Jian

Prepared by: Zhao Qiongfeng

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

1. GENERAL

Jiaoda Kunji High-Tech Company Limited (formerly known as Kunming Machine Tool Company Limited) (“the Company”) was established in the Mainland People’s Republic of China as a sino-foreign joint stock limited company as part of the reorganization of a state-owned enterprise known as Kunming Machine Tool Plant (“KMT Plant”). Pursuant to the reorganization, the operations, assets and liabilities of KMT Plant were divided between the Company and Kunming Kun Ji Group Company (“Kun Ji Group Company”). The Company was established on 19th October, 1993. The Company’s A shares and H shares have been listed on the Shanghai Securities Exchange in Shanghai and the Stock Exchange of Hong Kong Limited in Hong Kong respectively. The Company is engaged principally in the design, development, production and sale of machine tool, precision measuring equipment and precision transducers.

On 25th December, 2000, Xian Jiaotong University Industrial (Group) Incorporation (“Jiaotong Group”) entered into an agreement with Yunnan Provincial People’s Government (“Yunnan Government”), the Company’s former controlling shareholder whereby Yunnan Government would transfer a 29% interest of 71,052,146 state-owned shares in the Company to Jiaotong Group. The Ministry of Finance Signed Approval of State-owned shares transfer of Jiaoda Kunji High-tech Company Limited (Cao Qi [2001] No. 283), and approved the share transfer. Upon completion of share transfer procedure on 5th June, 2001, Jiaotong Group became substantial shareholder of the Company.

Pursuant to extraordinary general meeting of the Company held on 31st December, 2001. After the assets restructuring, the Company changed from a traditional machinery manufacturing company which focused on production of machine tools to a high-tech and diversified production company.

With effective from 29th March, 2002, the Company uses the name “Jiaoda Kunji High Tech Company Limited”. The amount of registered capital RMB245,007,400. The place of registration is 23 Ciba Road, Kunming City, Yunnan Province. The business registration number is Qi Gu Dian Zong Zi No. 000682.

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS

1. Accounting Standards and Accounting System

The financial statements have been prepared in accordance with “Accounting Standards for Business Enterprises”, “Accounting System for Business Enterprises” and the complementary regulation.

2. Accounting Fiscal Year

The accounting year of the Company commences on 1st January and ends on 31st December each year.

3. Reporting Currency

The reporting currency of the Company is Renminbi (“RMB”)

4. Recording Principles and Accounting Basis

The Company adopts the accrual basis as the basis of accounting and the historical cost as the principle of valuation.

5. Foreign Currency Translation

Transactions in foreign currencies are translated at the market exchange rates (middle rate), ruling on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are re-translated into RMB at the market exchange rates (middle rate), ruling on the balance sheet date. Profits and losses arising on exchange are included in financial expenses apart from those relating to the construction in progress.

6. Recognition Criteria for Cash equivalents

Cash equivalents included in the cash-flow statement are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are within three months of maturity and subject to limited risk on changes in value.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS *(Continued)*

7. Accounting for Bad Debts

(1) Recognition criteria for bad debt

1. The irrecoverable amount of a debtor who has gone bankrupt or has died and has insufficient asset or estate to repay;
2. The irrecoverable amount, demonstrated by sufficient evidence, of a debtor who does not comply with his/her repayment obligation after the debt fall due.

The irrecoverable amount stated above is cancelled as bad debt after hierarchical approval ratified by the Board of Directors.

(2) Accounting for bad debt

The cost of bad debts is calculated on the provision method. Provision for bad debts is made using the provision method based on aging analysis.

The provision percentage is reasonably estimated based on the past experiences of management of the Company, the financial position and cash flows condition of the relevant debtor, as well as other relevant information.

The estimated bad debt loss percentage excluding special provision is as follows: The estimated provision percentage is 5% when the accounts receivable age is within 1 year; The estimated provision percentage is 50% when the accounts receivable age is 1 to 2 years; The estimated provision percentage is 100% when the accounts receivable age is over 2 years.

8. Accounting for Inventories

- (1) Inventory category: Inventories include merchandise inventory, self-made semi-finished goods, raw materials, low value consumables and packaging materials.
- (2) Valuation method of inventories. Buying-in of raw materials, packaging materials and low value consumables are stated at cost incurred. Inventory issued and inventory shipped are recorded based on the weighted average cost method.
- (3) Amortization of low value consumables: Low value consumables are fully charged to cost when they are issued.
- (4) Inventories are recorded at the lower of cost and net realizable value and provision for loss on realization of inventories is recognized using the single-item comparison method.

Net realizable value represents the estimated selling price less the estimated cost of completion and the estimated costs to be incurred in marketing, selling and distribution in general operation.

9. Accounting for Short-term Investment

- (1) Short-term investment is stated at the historical cost. Gain on an investment is recognized when the investment is transferred or repaid on maturity.
- (2) Short-term investment is recorded at the lower of cost and market value at the end of each period. Provision for impairment on short-term investment should be recognized according to the investment collectively.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS *(Continued)*

10. Accounting for long-term investment

(1) Long-term bond investment

Long-term bond investment is recorded at its initial cost on acquisition. Premium and discount are amortized during the period when bonds are held using the straight-line method. Accrual interest is made at the period end.

(2) Long-term equity investment

The cost method is adopted when the amount of the investment is below 20 percent of the amount of registered capital of the investee enterprise; The equity method is adopted when the amount of the investment is above 20 percent of the amount of registered capital of the investee enterprise; The equity method is adopted and the financial statements are consolidated when the amount of the investment is above 50 percent of the amount of registered capital of the investee enterprises.

(3) Equity investment difference are amortized evenly over 10 years and recognized in the income statement accordingly.

(4) If the recoverable amount of any long-term equity investment is lower than the carrying amount of that investment as a result of a continuing decline in market value or changes in operating conditions of investee enterprises and the reduced value can not be recovered in the foreseeable future period, provision should be made for the difference between the recoverable amount and the carrying amount of the investment.

11. Accounting for and Depreciation of Fixed Assets

(1) Fixed assets are stated at initial cost.

(2) Recognition Criteria for Fixed Assets: Fixed assets include buildings, plant, machinery and equipment, transportation equipment and other equipment, tools having useful lives over one year and used in production and operation. Other major equipment which is not used in production or operation but with unit value over RMB2,000 and having useful lives over two years are recognized as fixed assets.

(3) Depreciation of Fixed Assets: Depreciation is provided using the straight-line method at the following rates per annum:

Category of fixed assets	Estimated useful lives	Residual value rate (%)	Annual depreciation rate(%)
Buildings	40	4	2.5
Plant and machinery	12-50	4	2-8
Furniture, fixture and equipment	10-14	4	6-10
Motor vehicles	10-14	4	6-10

The depreciation policy for assets held under finance bases are consistent with that for owned assets. If there is reasonable certainty that the lease will obtain ownership at the end of lease, the asset should be depreciated over the shorter of the lease term and the life of the asset.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS *(Continued)*

11. Accounting for and Depreciation of Fixed Assets *(Continued)*

(4) Provision on impairment loss on fixed assets

The Company recognizes an impairment loss on fixed assets when realizable value fall lower than book value as a result of a continuing decline in market value, lagging behind in technology, damage and long-term idling. Provision on impairment loss on fixed assets is provided according to total amount of fixed assets if there exists:

1. Fixed assets have been idled in the long-term and will not be reused in the foreseeable future. They have no transfer value as well;
2. Fixed assets cannot be utilized because of their obsolete technology;
3. Large quantity of unqualified products are produced when fixed assets are used;
4. Fixed assets have been damaged and have no usage value and transfer value;
5. Fixed assets in substance cannot produce economic benefits for the Company.

12. Accounting for Construction in progress

Construction in progress is stated at initial cost. Costs on completed construction works are transferred to other categories of fixed assets. Interest incurred before the construction works are ready for their intended use is capitalized as part of the engineered cost. Interest incurred after the construction works are ready for their intended use is provided in the income statement.

Provision on impairment loss on construction in progress

At the period end, based on the investigation on each construction in progress, if there exists

1. construction in progress has been ceased for construction for a long period of time and no re-commencement of work is expected in the future 3 years;
2. construction in progress was technically and physically obsolete and its economics benefits to the Company are uncertain;
3. other evidences can prove the existence of the circumstance of the decline in value on construction in progress,

the difference of the recoverable amount and the carrying amount of construction in progress can be made as provision on impairment loss on construction in progress.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS *(Continued)*

13. Intangible Assets

(1) Amortisation of Intangible Assets

1. If the contract stipulates the benefiting period and the law does not prescribe the effective period, intangible assets are amortized over the effective period.
2. If the contract does not stipulate the benefiting period and the law prescribes the effective period, intangible assets are amortized over the effective period.
3. If the contract stipulates the benefiting period and the law prescribes the effective period, intangible assets are amortized over the shorter of the benefiting period and the effective period.
4. If the contract does not stipulate the benefiting period and the law does not prescribe the effective period, intangible assets are amortized over 10 years except for land use right which are amortized evenly over the terms of the contract from the date the Company obtains the certificate of land occupancy rights and usage right to staff quarter which is amortized evenly during its benefiting period.

(2) Provision on impairment loss on intangible assets

At the period end, based on investigation on the intangible assets and estimation of their ability of producing economic benefits, provision should be made for the difference between realizable value and book value, when

1. one term of intangible assets has been replaced by other new technology and its ability of producing economic benefits has been affected significantly;
2. the market value of one item of intangible assets drops sharply in the current period and estimatedly cannot be recovered in the rest of the year.
3. one item of intangible assets unprotected by the law still has usage value.
4. other evidence indicates the loss on value of intangible assets.

14. Amortization of Initial Expenses and Long-term deferred expenditures

1. Initial cost is fully charged to income in the current month when operations begin.
2. Long-term deferred expenditures are evenly amortized during the benefiting period.

15. Borrowing Costs

Interest except for those incurred in connection with specific borrowings for the purchase of fixed assets should be recognized as financial expenses and recorded in the income statement in the current period accordingly.

Interest incurred in connection with specific borrowings for the purchase of fixed assets is capitalized before the relevant fixed asset being acquired or constructed is ready for its intended use. If acquisition and construction of one item of fixed assets are abnormally discontinued for 3 months, interest is temporarily ceased to be capitalized and the interest incurred in this period is recognized as a financial expense. Interest incurred after the construction work is ready for its intended use is made as financial expenses.

16. Accounting for Bonds Payables

Bonds payables are stated at initial cost. Premiums and discounts are amortized during the existent period of bonds using the straight-line method.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS *(Continued)*

17. Recognition Criteria for Revenue

- (1) Sales of goods: Revenue from sales of goods is recognized when the Company has transferred to the buyers the risk and ownership of the goods and received the relevant revenue or obtained the evidence proving the sales proceeds and the cost relating to sale of goods can be measured reliably.
- (2) Provision of services: When the provision of services is started and completed within the same accounting year, revenue is recognized at the time of completion of the services. When the provision of services is started and completed in different accounting years and the outcome of a transaction involving the rendering of services can be estimated reliably, the Company recognizes the service revenue at the balance sheet date by the use of the percentage of completion method.
- (3) Revenue from assets used by other parties: Interest revenue is calculated based on the length of time for which other parties use cash of the Company and the applicable interest rate; Occupancy expense revenue is calculated by the length of time and the method as stipulated in the contract.

Fund occupancy expense is provided to write off the financial expenses in the current period when fund occupancy expenses which relevant parties pay to the Company can be recognized as revenue and the Company received them. If the amount of fund occupancy expenses received exceed the amount of interest calculated at the rate of one-year- deposit placed with banks, the amount equivalent to that of the latter writes off the amount of the financial expense in the current period and the difference between the former and the latter is provided in capital surplus.

(4) Revenue from Finance Leases and Operating Leases

1. Rents from operation leases are recognized as revenue in each period using the straight-line method;
2. Revenue from finance leases in the current period is recognized adopting the real interest rate method. Unrecognized revenue from finance leases is allocated to each period over the lease term in accordance with the straight-line method. Rents the Company has not received after one period of rent payment should not been recognized as revenue from finance leases. If recognized, recognized revenue should be offset. Revenue from finance leases included in rents is recognized as revenue in the current period when actual receipts incur.

For the two items of finance leases stated above, the initial cost which is incurred in the course of negotiation and contracting and can be attributed directly to items of leases should be recognized as current cost. Contingent rents incurred should be recognized as revenue in the current period.

(4) Revenue from Finance Leases and Operating Leases *(continued)*

3. Sale and Leaseback Transactions. For finance leases resulting from sale and leaseback transactions, any difference between the sales proceeds and the original carrying amount of the assets involved are deferred and amortized as an adjustment to depreciation according to the depreciation pattern of the leased asset. For operating leases resulting from sale and leaseback transactions, any difference between the sales proceeds and the original carrying amount of the assets involved are deferred and amortized according to the proportion of the lease payments during the lease term.

18. Accounting for Income Taxes

Income taxes are calculated using the taxes receivable method.

19. Tax Refund

Tax refund is recorded in current year's profit when actual receipts incur.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS *(Continued)*

20. Basis of Consolidation

The consolidated financial statements incorporate the financial statements of the Company and investee enterprises in which the Company holds more than half of the equity or where the Company controls the operation of the investee enterprises.

If there exists some difference between the accounting policies used by subsidiaries included in the consolidation and that used by the Company, the financial statements of subsidiaries are adjusted in accordance to the accounting policies used by the Company.

Pursuant to Cai Kuai Zi (1995) No. 11 "Notice on issuing 'Provisional Regulation on Consolidation of Financial Statements'", the financial statements of the Company and subsidiaries included in the consolidation and relevant materials, the amount of each item in the financial statements is consolidated and the following items are eliminated on consolidation:

- (1) equity investment of the Company and relevant parts of ownership interests of subsidiaries in the scope of consolidation.
- (2) all significant intercompany transactions and balances between the Company and subsidiaries in the scope of consolidation.

3. TAXATION

1. Value Added Tax

Output value added tax is calculated at 17% of the revenue. Input value added tax rate for industrial products is 17%. Input value added tax rate for agricultural and subsidiary products is 13%. The amount of taxes payable is recorded after deducting input value added tax in the current period from output value added tax in the current period. If the amount of output value added tax in the current period is less than the amount of input value added tax in the current period, balance due is carried down to the next period.

2. Income Tax

According to the notice of Cai Shui Zi (1994) No.017 jointly issued by the Ministry of Finance and the State Administration of Taxation, the applicable income tax rate of the Company is 15%.

Shannxi Hengtong Intelligent Machine Company Limited, Xian Jiaoda Resources Intelligent Machine Company Limited and Kunming Jiaoda Kunji Automatic Machine Company Limited, subsidiaries of the Company, are all high-tech companies. The applicable income tax rate for them is 15%. The income tax rate for Xian Ser Turbo Machinery Equipment Company Limited is 33%.

3. Business Tax

Business tax is calculated and paid at 5% of operating income.

4. Other Taxes

Other tax is calculated and paid according to the Law of Taxation.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

4. SUBSIDIARIES AND JOINT VENTURES

(1) General of the Company's Subsidiaries and Joint Ventures

Name of subsidiaries and joint ventures	Place of Registration	Scope of Business	Registered Capital (thousand dollars)	Investment Proportion (%)	Economic Nature	Date of Investment
Xian Ser Turbo Machinery Company Limited ("Xian Ser")	Xian City	Design, develop and sales of turbo-machinery	200.00	80.00%	Limited liability	December 2001
Shannxi Hengtong Intelligent Machine Company Limited (Shannxi Hengtong)	Xian City	Develop and sale of manufacturing moulds, machinery, equipment, electronic products, software and hardware	60.00	90.00%	Limited liability	December 2001
西安交大思源智慧電器有限公司	Xian City	Develop, manufacture and Sale of electronic products, electronic machine and products of electronic power; Provide technology services	3,500.00	78.03%	Limited liability	December 2002
昆明交大昆機自動機器有限公司	Kunming City	Develop, apply and integrate hardware and software; Retail, wholesale, purchase on behalf of others and consign electronic products, machinery and electronic machine.	2,023.00	90.91%	Limited liability	November 2002
西安通大思源電器有限公司	Xian City	Develop, manufacture, and installation of Mechatronis products; Permanent magnets.	100.00	25.00%	Limited liability	September 2002

- (2) The subsidiaries stated above except for Xian Jiaoda Resources Electronic Machine Company Limited have been included in the consolidation. 昆明交大昆機自動機器有限公司, 昆明交大昆機自動機器有限公司 established in the current year have been included in the consolidation since the date the subsidiaries were established.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB)

1. Bank Balances and Cash

Items	At 31st December, 2002		At 1st January, 2002	
	Foreign currency	RMB	Foreign currency	RMB
Cash on hand				
RMB		840,606		472,574
HKD	29,935	32,351	21,219	22,505
USD	13,891	114,927	6,384	52,840
DEM	7,633	42,134	7,633	42,134
Bank				
RMB		81,250,018		102,238,453
Including: time deposit		3,363,000		
HKD	193,610	205,460	3,772,385	4,000,992
USD	39,153			
		324,062	39,103	323,640
	35,000,000	37,142,000	37,000,000	39,242,200
Time deposit in HKD		82,655,776		7,143,250
Other currency				
Total		202,607,334		153,538,588

Note:

(1) Time deposit of HK dollar amounting to HKD 35,000,000 (equals to RMB37,142,500) has been pledged to secure short-term loan. Time deposit of RMB3,363,000 has been pledged to secure long-term loan.

(2) Other currency are deposits in stock companies.

2. Short-term investment

Category	At 31st December, 2002		At 1st January, 2002	
	Capital	Provision for impairment	Capital	Provision for impairment
Stock and fund investment	13,500	—	47,856,750	5,726,799

Provision on impairment loss on short-term investment is not provided because short-term investment includes marketable shares amounting to RMB13,500 equal to year end market values.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

3. Accounts receivable

Age	At 31st December, 2002			At 1st January, 2002		
	Amount	Proportion (%)	Bad debt provision	Amount	Proportion (%)	Bad debt provision
Within 1 year	49,266,767	70	1,895,425	38,774,514	63	6,127,498
1-2 years	10,492,945	15	4,561,473	14,527,988	23	7,514,498
2-3 years	4,335,858	6	4,335,858	448,584	1	391,081
Over 3 years	6,498,949	9	3,679,484	8,033,507	13	6,498,948
Total	70,594,519	100	14,472,240	61,784,593	100	20,532,025

Note:

- (1) There is no balance due from shareholders whose shares exceed 5%(including 5%) of the total shares of the Company.
- (2) The total amount of the 5 largest debtors is RMB13,953,370, constituting 19.77% of the total amount of accounts receivable.

4. Other Receivables

Age	At 31st December, 2002			At 1st January, 2002		
	Amount	Proportion (%)	Bad debt provision	Amount	Proportion (%)	Bad debt provision
Within 1 year	13,590,038	70	679,502	16,000,757	87	—
1-2 years	4,020,417	21	1,918,208	1,507,498	8	98,261
2-3 years	1,262,778	8	686,827	124,541	1	43,961
Over 3 years	167,003	1	167,003	688,371	4	—
Total	19,040,236	100	3,451,540	18,321,167	100	142,222

Note:

- (1) The balance due from shareholders whose shares exceed 5%(including 5%) of the total shares of the Company is disclosed in Note 7 "Relevant Party Relationship and Transactions".
- (2) The total amount of other receivables from the 5 largest debtors is RMB4,950,470, constituting 26% of the total amount of accounts receivable.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

5. Prepayments

Age	At 31st December, 2002		At 1st January, 2002	
	Amount	Proportion (%)	Amount	Proportion (%)
Within 1 year	9,659,197	88	5,631,055	100
1-2 years	1,364,821	12	—	—
Total	11,024,018	100	5,631,055	100

Note:

(1) There is no prepayments to shareholders whose shares exceed 5% (including 5%) of the total shares of the Company.

(2) As at 31st December, 2002, the amount of prepayments increased by 95.77% over that at the end of last year, mainly because the increase of orders in Xian Ser, one of subsidiary of the Company has made the amount of prepayments for raw materials increase.

6. Inventories

Items	At 31st December, 2002		At 1st January, 2002	
	Amount	Provision for loss on realization	Amount	Provision for loss on realization
Finished goods	71,747,269	19,874,957	52,751,888	16,463,176
Raw materials	22,757,246	595,586	20,297,212	6,053,437
Low value consumables	4,271,246	—	4,289,321	82,781
Work in progress	132,515,987	24,225,426	126,038,001	24,570,458
Materials on consignment for future processing	1,307,093	—	—	—
Materials purchased	7,140,017	—	—	—
Goods in transit	—	—	6,054,451	—
Merchandise on consignment sales	424,383	—	—	—
Packaging materials	11,758	—	—	—
Total	240,174,999	44,695,969	209,430,873	47,169,852

7. Prepaid Expenses

Items	At 1st January, 2002	Addition In the current period	Amortization in the current period	At 31st December, 2002
Office buildings reconstruction	299,002	—	299,002	—
Appraisal expenses	100,552	150,000	100,552	150,000
Rentals	—	30,312	—	30,312
Others	—	158,012	67,746	90,266
Total	399,554	338,324	467,300	270,578

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

8. Long-term Equity Investment

(1) General of investee enterprises

Name of Investee	Initial investment cost	Investment proportion	Investment period	Accounting
Xian Ser Turbo Machinery Company Limited	16,734,463	80.00%	N/A	Equity method
Shannxi Hengtong Intelligent Machine Company Limited	6,108,606	90.00%	N/A	Equity method
西安交大思源智慧電器有限公司	27,310,000	78.03%	N/A	Equity method
昆明交大昆機自動機器有限公司	18,390,000	90.91%	N/A	Equity Method
Yunan Cheng Jiang Copper Products Plant	2,000,000	40.00%	N/A	Cost method

(2) Changes in Long-term Equity Investment

Name of Investee	At 1 st January, 2002	Changes in the current period		Changes in accumulated equity		At 31st December, 2002
		Investment cost	Equity adjustment	Investment Cost	Equity adjustment	
Yunan Cheng Jiang Copper Products Plant	2,000,000	—	—	—	—	2,000,000
西安通大思源電器有限公司	—	250,000	—	—	—	250,000
Consolidated price difference	15,070,862	—	1,507,087	—	—	13,563,775
	17,070,862	250,000	(1,507,087)	—	—	15,813,775
	2,000,000					2,000,000
	15,070,862	250,000	(1,507,087)	—	—	13,813,775

Note:

- (1) Provision for impairment on long-term investment is provided on the basis of the total amount of investment the Company has made to Yunnan Cheng Jiang Copper Products Plant, Because the plant has lost of the ability of sustainable operation.
- (2) Consolidated price difference is the difference of the amount of equity investment. Concrete information on consolidated price difference is disclosed in Note 6 " Notes to the Financial Statements of the Company".
- (3) There is no significant difference between the accounting policies used by the investee enterprises and that used by the Company. There is no significant restrictions to realization of investment and investment income outflow as foreign currency.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

9. Fixed Assets and Accumulated Depreciation

Category	at 1st January, 2002	Increase this year	Decrease this year	at 31st December, 2002
Buildings	110,090,421	10,001,456	215,095	119,876,782
Furniture, fixture and equipment	27,480,525	2,237,086	1,201,409	28,516,202
Plant and machinery	200,665,100	10,075,624	2,467,867	208,272,857
Motor vehicles	7,983,393	2,319,444	455,504	9,847,333
Sub-total	346,219,439	24,633,610	4,339,875	366,513,174
ACCUMULATED DEPRECIATION:				
Buildings	17,155,817	2,830,034	31,852	19,953,999
Furniture, fixture and equipment	14,009,644	2,814,745	560,071	16,264,318
Plant and machinery	74,965,244	14,587,270	2,131,444	87,421,070
Motor vehicles	2,969,650	643,304	197,273	3,415,681
Sub-total	109,100,355	20,875,353	2,920,640	127,055,068
Net realizable value	237,119,084			239,458,106
PROVISION FOR IMPAIRMENT:				
Buildings	—	—	—	—
Plant and machinery	2,229,794	—	127,239	2,102,555
Plant and machinery	493,197	—	3,699	489,498
Sub-total	2,722,991	—	130,938	2,592,053
NET REALIZABLE VALUE	234,396,093			236,866,053

Note:

- (1) Provision on impairment is recognized because the book value is higher than the net realizable value.
- (2) Buildings and motor vehicles amounting to RMB106,511,449 in original cost and RMB73,132,832 in net realizable value have been pledged to secure loans amounting to RMB44,000,000.
- (3) The original book value of fixed assets from finance leases is RMB4,264,181. The amount of accumulated depreciation is RMB656,175 and the net realizable value is RMB3,608,006 accordingly.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

10. Construction in progress

Construction name	At 1st January 2002	Additions this year	Transfer to fixed assets	Other transfer out	At 31st December 2002	Source of funds
Engineering of heat-treatment workshop	6,905,493	23,013	6,928,506		—	Listing proceeds
95 Technical improvement projects	23,440,476	9,987,305	20,000		33,407,781	Loans
including Capitalised interest	1,951,510	1,469,601	—		3,421,111	
Resources Office Building	—	4,207,968	—		4,207,968	Funds owned
Others	5,399,445	3,255,451	1,463,489	610,000	6,581,407	Listing proceeds
Total	35,745,414	17,473,737	8,411,995	610,000	44,197,156	
Less: provision on impairment loss on construction in progress	671,597			20,000	651,597	
Net realizable value	35,073,817				43,545,559	

Note:

Payment of capitalized interest in construction in progress in the current accounting year is RMB1,469,601. Capitalized interest rate is 6%.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

11. Intangible Assets

Items	Acquired method	Original cost	At 1st January, 2002	Addition this year	Transfer out this year	Amortization this year	At 31st December 2002	Amortization Period left
Good-Will (Note 1)	Acquisition of business	5,638,632	5,638,632	—	—	563,863	5,074,769	10.00
Goodwill (Note 2)	Acquisition of business	3,720,569	3,720,569	—	—	372,057	3,348,512	10.00
The All Over Controlled Vortex Technology		11,630,000	11,630,000	—	—	1,163,000	10,467,000	9.00
Technical know-how Of fast moulding		14,730,000	14,730,000	—	—	1,473,000	13,257,000	9.00
Intelligent know -how		9,044,400	9,044,400	8,139,960	8,139,960	904,440	8,139,960	10.00
Technical know-how of embroidery machine		4,039,667	4,039,667	3,736,692	3,736,692	403,967	3,635,700	9.75
Land use right (Note 2)	Contributed	17,568,198	13,374,411	—	—	320,349	13,054,062	40.75
Usage right to staff quarter	Acquisition of business	4,485,988	3,925,240	—	—	93,458	3,831,782	41.00
Financial software	Acquisition of business	129,200	—	129,200	—	5,383	123,817	9.58
Company website development expenses	Acquisition of business	38,000	—	38,000	—	1,267	36,733	4.83
Total		71,024,654	66,102,919	12,043,852	11,876,652	5,300,784	60,969,335	

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

11. Intangible Assets (Continued)

Note:

- (1) Goodwill is made for the difference between the transaction price and the book value when Xian Jiaotong University Industrial Group acquired two subsidiaries from Jiaoda Resources, Intelligent Electronic Machine and Automatic Machine, in December 2001 during the course of the assets restructuring. The company made the investment of the assets in the two subsidiaries and relevant goodwill stated above and established Xian Jiaoda Resources Intelligent Electronic Machine Company Limited and Kunming Jiaoda Automatic Machine Company Limited in this year. These two items of goodwill are amortized over 10 years.
- (2) Technical know-how is that the Company acquired from Xian Jiaotong University Industrial Group in December 2001 during the course of the assets restructuring. The Company made the investment of "Intelligent Technical Know-how" and "Embroidery Machine Technical Know-how" and established Xian Jiaoda Resources Intelligent Electronic Machine Company Limited and Kunming Jiaoda Automatic Machine Company Limited. Addition to these two items of technical know-how is recorded at the carrying amount of intangible assets when the subsidiaries accept them. Transfer out is recorded for the carrying amount of intangible assets when the Company made the investment of intangible assets.
- (3) Land use right was contributed by Yunnan Government as capital.

12. Long-term Deferred Expenditures

Items	Original costs	Addition this year	Amortization this year	Accumulated amortization	At 31st December, 2002	Remaining amortization period left
Office buildings reconstruction	298,876	298,876	60,787	60,787	238,088	4.00
Workshop reconstruction	91,674	91,674	52,342	52,342	39,332	0.75
Old united workshop Repairs expenses	691,259	691,259	—	—	691,259	3.00
Plant fitment	594,875	594,875	214,500	214,500	380,375	1.75
Total	1,676,684	1,676,684	327,629	327,629	1,349,054	

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

13. Short-term Loans

Category	At 31st December, 2002		At 1st January, 2002	
	Amount	Exchange rate currency	Amount	Exchange rate currency
Guaranteed loans	10,000,000	RMB	—	
Secured loans	44,000,000	RMB	20,000,000	RMB
Pledge loans	35,000,000	RMB	30,000,000	RMB
Credit Loans	70,000,000	RMB	70,200,000	RMB
Total	159,000,000		120,200,000	

Note:

- (1) All the secured loans are secured by buildings in possession of the Company.
- (2) All the pledge loans are pledged by Hong Kong dollar time deposit.
- (3) All the guaranteed loans are guaranteed by Xian Jiaoda Resources High-Tech Company Limited.

14. Accounts payables

As at 31st December, 2002 and at 31st December, 2001, the balance of accounts payables amounts to RMB18,879,494 and RMB10,165,500 respectively. The balance of accounts payables do not contain any amounts due to shareholders whose shares exceed 5% (including 5%) of total shares of the Company.

15. Advances from customers

- (1) As at 31st December 2002, the balance of advances from customers increases by 93.09% over that at 31st December, 2001 amounting to RMB28,519,829, which results from the increase of sale orders of Xian Ser, one of subsidiaries of the Company.
- (2) No advances from shareholders whose shares exceed 5% (including 5%) of total shares of the Company.

16. Payroll Payables

Payroll payable is made for the payroll due to the employees of the Company. As at 31st December, 2002 and at 31st December, 2001, the balance of payroll payables totals up to RMB75,774 and RMB3,416,690 respectively.

17. Taxes payables

Items	At 31st December,2002	At 1st January, 2002
Value added tax	7,371,929	10,007,928
Business tax	229,152	3,420,775
City construction tax	90,584	—
Income tax	1,206,106	711,583
Building taxes	—	—
Others	29,504	112,946
Total	8,927,275	14,253,232

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

18. Other payables

Items	At 31st December, 2002	At 1st January, 2002
Additional educational fee	38,822	—
Flood-controlling funds	80,402	—
Total	119,224	—

19. Other payables

As at 31st December, 2002 and at 31st December, 2001, the balance contains RMB9,771,281 and RMB30,111,143 respectively. The details of the balance due to shareholders whose shares exceed 5% (including 5%) of total shares of the Company are disclosed in Note 5 "Connected Party Relationship and Transaction".

20. Accrued Expenses

Items	At 31st December, 2002	At 1st January, 2002
Accrued rental	514,011	50,000
Accrued audit fee	1,600,000	1,280,000
Accrued engineered cost	328,876	824,690
Accrued consulting fee, accrued lawyer fee etc.	1,650,000	—
Others	4,440	—
Total	4,097,327	2,154,690

21. Long-term Loans Due Within One Year

Items	At 31st December, 2002	At 1st January, 2002
Long-term loans due within 1 Year	29,800,000	10,339,313
Obligation under finance leases due within on 1 year	213,210	213,210
Total	30,013,210	10,552,523

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

22. Long-term loans

Category	At 31st December, 2002		At 1st January, 2002	
	Amount	Currency	Amount	Currency
Guaranteed loans				
Secured loans	29,800,000	RMB	40,441,750	RMB
Pledge loans	3,000,000			
Credit loans	3,000,000	RMB	4,000,000	RMB
Total	35,800,000		44,441,750	
Less: amount due within 1 year	29,800,000		10,339,313	
Amount due after 1 year	6,000,000		34,102,437	

All secured loans are secured by buildings in possession of the Company.

All pledged loans are pledged by time deposit of Xian Ser.

23. Long-term payable

Category	Period	Original amount	Amount at 1st January, 2002	Increase this year	Decrease this year	Amount at 31st December, 2002
Obligation under Finance lease	20 years	6,843,378	6,843,378	—	342,169	6,501,209
Less: future finance charge		2,579,197	2,579,197	—	128,960	2,450,237
Less: amount due for settlement within one year			213,210			213,210
Sub-total		4,264,181	4,050,971	—	213,209	3,837,762
Add: infrastructure construction appropriation from the Office of Finance of Shannxi Province		—	—	200,000	—	200,000
Appropriation for intelligent electronic machine technology and equipment technology industrialization exemplary projects		—	—	7,000,000	—	7,000,000
Total		4,264,181	4,050,971	7,200,000	213,209	11,037,762

Note:

- (1) The difference between the present value of minimum lease payment amounting to RMB6,843,378 and the net book value of assets held under finance leases amounting to RMB4,264,181 is made as future finance charge and is amortized over 20 years using the straight-line method.
- (2) Appropriation for intelligent electronic machine technology and equipment technology industrialization exemplary projects represents appropriation for the projects based on Approval of Feasibility of Intelligent Electronic Machine Technology and Equipment Technology Industrialization Exemplary Projects signed by the State Development Plan Committee (Kuai Qi Gao Ji (2000) No. 1883.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

24. Specific Project Payable

Items	At 31st December, 2002	At 1st January, 2002
Specific project appropriation from the Science and Technology Committee of Yunnan province	2,490,406	2,065,806

25. Deferred Gain

Items	Original amount	Amount at 1st January, 2002	Addition this year	Provided for the year	Accumulated amortization	Amount at 31st December, 2002	Amortization period left
Buildings	4,023,642	4,023,642	—	451,196	451,196	3,572,446	19
Including:							
Operating Lease	1,758,331	1,758,331	—	87,917	87,917	1,670,414	19
Finance lease	2,265,311	2,265,311	—	363,279	363,234	1,902,077	5-20
Land use right	8,287,344	8,287,344	—	414,365	414,365	7,872,979	19
Including:							
Operating Lease	8,287,344	8,287,344	—	414,365	414,365	8,286,930	19
Finance lease							
Total	12,310,986	12,310,986	—	865,561	865,561	11,445,425	

Note:

The Company leased back a portion of land use right and premise use right which had been disposed to Yunnan Government in December 2001 when the Company implemented the assets restructuring. The lease term is 20 years. The selling price of these assets is RMB28,438,361 and the book value of these assets is RMB16,127,375. The gain due from the transaction is to be deferred. For operating lease, deferred gain is to be allocated through the lease period according to rental expense; For finance lease, deferred gain is to be allocated to adjust depreciation expense according to depreciation rate.

26. Share Capital

Items	Amount at 1st January, 2002	Increase this year	Decrease this year	Amount at 31 st December, 2002
1. Non-trading shares	120,007,400	—	—	120,007,400
Promoters shares	31,345,554	—	—	31,345,554
Including: State-Owned shares	31,345,554	—	—	31,345,554
Legal person shares	88,661,846	—	—	88,661,846
2. Trading shares	125,000,000	—	—	125,000,000
Including: A shares	60,000,000	—	—	60,000,000
H shares	65,000,000	—	—	65,000,000
Total shares	245,007,400	—	—	245,007,400

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

27. Capital Reserves

Items	Amount at 31st December, 2002	Amount at 1st January, 2002
Share premium	293,744,338	293,744,338
Revaluation surplus	11,536,142	11,536,142
Total reserves	305,280,480	305,280,480

28. Surplus Reserves

Items	Amount at 1st January, 2002	Increase this year	Decrease this year	Amount at 31st December, 2002
Statutory surplus reserve	8,406,328	—	—	8,406,328
Statutory public reserve	8,406,328	—	—	8,406,328
Total	16,812,656	—	—	16,812,656

29. Retained Profit

Items	2002
Retained profit at the beginning of the period	(66,399,970)
Add: net profit this year	6,077,478
Less: statutory surplus reserve	—
Statutory public reserve	—
Retained profit at the period end	(60,322,492)

30. Principal Operation Tax and Addition

Items	Accumulated amount		Accumulated amount	
	this year Revenue	last year Cost	Revenue	Cost
Revenue from sales and processing	179,628,485	120,047,698	102,493,975	77,526,169

Note:

Total sales of the 5 largest customers total up to RMB22,662,484 which constitutes 12.62% of total sales of the Company.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

31. Principal Operation Tax and Addition

Items	Accumulated amount this year	Accumulated amount last year
Business tax	14,551	—
City construction tax	154,925	—
Education fee addition	66,478	—
Total	235,954	—

Note:

City construction tax and education fee addition are calculated and paid at 7% of value added tax and 3% of business tax.

32. Profit from Other Operations

Items	Income	Cost	Profit
Materials sold	663,057	760,319	(97,262)
Materials disposed	433,026	—	433,026
Income from consulting	2,625,000	131,250	2,493,750
Others	15,304	4,122	11,182
Total	3,736,387	895,691	2,840,696

33. Financial Expenses

Items	Accumulated amount this year	Accumulated amount last year
Interest expenses	8,517,229	7,300,644
Less: interest income	892,885	2,507,812
Exchange (loss) gain	(21,780)	(4,077)
Bank's processing fee	70,747	83,317
Others	132,382	—
Total	7,805,693	4,872,072

34. Investment Income

Items	Accumulated amount this year	Accumulated amount last year
Reversal provision for diminution in value of short-term investment	5,726,798	(5,726,799)
Amortization of Equity investment difference	(1,507,086)	—
Income from short-term investment	(3,205,723)	9,000,000
Total	1,013,989	3,273,201

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

35. Subsidies

Items	Accumulated amount this year	Accumulated amount last year
Income tax refunded	1,322,691	1,700,000

36. Non-operating Income

Items	Accumulated amount this year	Accumulated amount last year
Gain on disposal of premises to Yunnan Government	—	48,056
Gain on disposal of land use right to Yunnan Government	—	14,493,349
Gain on disposal of fixed assets	247,137	—
Income from provision of training	46,910	—
Others	5,787	105,426
Total	299,834	14,646,831

37. Non-operating Expenses

Items	Accumulated amount this year	Accumulated amount last year
Loss on disposal of inventory to Yunnan Government	—	14,971,758
Loss on disposal of fixed assets	397,074	175,417
Contribution expenses	23,000	—
Provision on impairment loss on fixed assets	(130,938)	—
Provision on impairment loss on Construction in progress	(20,000)	—
Others	110,207	60,637
Total	379,343	15,207,812

38. Income Taxes

Income taxes represent income taxes paid by subsidiaries included in the consolidation.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

39. Other Cash paid relating to Operating Activities

Payment of other cash paid relating to operating activities amounting to RMB44,618,651 is as follows.

Items	Amount
Traveling expense	4,373,381
Office expense	3,286,190
Business entertainment expense	1,240,399
Administrative expense for stock exchange	4,544,667
Warrant expense	1,662,458
Audit fee	2,034,758
Taxes including building tax	1,032,853
Research & development expense	3,819,017
Gardening expense	1,120,909
Consulting fee	1,273,855
Total	24,388,487

40. Cash and cash equivalent

Items	At 31st December, 2002		At 1st January, 2002	
	Consolidated amount	Amount for the Company	Consolidated amount	Amount for the Company
Cash	202,607,334	161,859,778	153,538,588	151,877,168
Less: time deposit	40,505,500	37,142,500	39,242,200	39,242,200
Cash and cash equivalents	162,101,834	124,717,278	114,296,388	112,634,968

6. NOTES TO THE FINANCIAL STATEMENTS OF THE COMPANY

1. Accounts Receivable

Age	At 31st December, 2002			At 1st January, 2002		
	Amount	Proportion (%)	Provision on bad debt	Amount	Proportion (%)	Provision on bad debt
Within 1 Year	28,754,410	60	925,807	33,664,862	63	3,717,303
1-2 years	9,127,037	19	3,547,045	11,261,326	21	5,110,836
2-3 years	3,602,141	8	3,602,141	182,736	1	145,232
Over 3 years	6,293,100	13	3,473,636	8,033,507	15	6,498,948
Total	47,776,688	100	11,548,629	53,142,431	100	15,472,319

Note:

(1) No balance due from shareholders whose shares exceed 5%(including 5%) of the total shares of the Company.

(2) Total amount of the 5 largest debtors is RMB11,580,885, constituting 23.96% of total amount of accounts receivable.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

6. NOTES TO THE FINANCIAL STATEMENTS OF THE COMPANY (Continued)

2. Other Receivables

Age	At 31st December, 2002			At 1st January, 2002		
	Amount	Proportion (%)	Provision on bad debt	Amount	Proportion (%)	Provision on bad debt
Within 1 Year	26,506,186	83	141,421	15,451,361	92	
1-2 years	4,832,552	15	574,276	598,361	3	98,261
2-3 years	589,751	2	13,800	124,541	1	43,961
Over 3 years	97,703	—	97,703	688,371	4	
Total	32,026,192	100	827,200	16,862,634	100	142,222

Note:

- (1) The balances due from shareholders whose shares exceed 5% (including 5%) of the total shares of the Company are disclosed in Note 7 "Relevant Party Relationship and Transaction".
- (2) Total amount of the 5 largest debtors is RMB30,926,800, which constitutes 96.57% of the total amount of other receivables.
- (3) As at 31 st December, 2002, the amount of other receivables increases by 87.66% over that at the end of last year, mainly because loans the Company lent Xian Ser and Shannxi Hengtong, subsidiaries of the Company, increased in this year.

3. Prepayments

Age	At 31st December, 2002		At 1st January, 2002	
	Amount	Proportion (%)	Amount	Proportion (%)
Within 1 year	518,803	69	1,438,587	100
1-2 years	230,000	31	—	—
Total	748,803	100	1,438,587	100

Note:

There is no prepayments to shareholders whose shares exceed 5% (including 5%) of the total shares of the Company.

4. Long-term Equity Investment

- (1) General of Investee enterprises

Name of investee	Original cost	Investment proportion	Investment period	Accounting
Xian Ser Turbo Machinery Company Limited	16,734,463	80.00%	N/A	Equity method
Shannxi Hengtong Intelligent Machine Company Limited	6,108,606	90.00%	N/A	Equity method
西安交大思源智能電器有限公司	27,310,000	78.03%	N/A	Equity method
昆明交大昆機自動機器有限公司	18,390,000	90.91%	N/A	Equity method
Yunnan Cheng Jiang Copper Products Plant	2,000,000	40.00%		Cost method

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

6. NOTES TO THE FINANCIAL STATEMENTS OF THE COMPANY (Continued)

4. Long-term Equity Investment (Continued)

(2) Changes in Long-term Equity Investment

Name of investee	Amount at 1st January, 2002	Increase(decrease) in equity this year		Increase(decrease) in accumulated equity		Amount at 31st December, 2002
		Investment cost	Adjusted equity	Investment cost	Adjusted equity	
Xian Ser Turbo Machinery Company Limited	16,734,463	—	2,753,715	—	2,753,715	19,488,178
Shannxi Hengtong Intelligent Machine Company Limited	6,108,606	—	(789,640)	—	(789,640)	5,318,966
西安交大思源智能電器有限公司	—	27,310,000	—	—	—	27,310,000
昆明交大昆機自動機器有限公司	—	18,390,000	642,333	—	642,333	19,032,333
Yunnan Cheng Jiang Copper Products	2,000,000	—	—	—	—	2,000,000
Sub-total	24,843,069	45,700,000	2,606,408	—	2,606,408	73,149,477
Less: Provision	2,000,000	—	—	—	—	2,000,000
Total	22,843,069					71,149,477

(3) Equity Investment Difference

Items	Original cost	Amount at 1st January, 2002	Addition this year	Amortization this year	Accumulated amortization	Amount at 31st December, 2002	Amortization period left
Xian Ser Turbo Machinery Company Limited	7,296,277	7,296,277	—	729,628	729,628	6,566,649	108 months
Shannxi Hengtong Intelligent Machine Company Limited	7,774,585	7,774,585	—	777,459	777,459	6,997,126	108 months
Total	15,070,862	15,070,862	—	1,507,087	1,507,087	13,563,775	

(1) Provision on impairment loss on long-term investment amounting to RMB2,000,000 is stated as a result of the carrying amount of the long-term investment lower than its recoverable amount.

(2) Pursuant to the Board of Directors, the Company established Kunming Jiaoda Kunji Automatic Machine Company Limited in which part of the assets in the Embroidery Machine Subsidiary and Sensor Apparatus Sub-factory were invested in November 2002. In December 2002, the Company established Xian Resources Intelligent Electronic Machine Company Limited in which all the assets in the Intelligent Electronic Machine subsidiary were invested.

(3) There is no significant difference between the accounting policies used by the investee enterprises and that used by the Company. There is no significant restrictions to investment realization and investment gain outflow in foreign currency.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

6. NOTES TO THE FINANCIAL STATEMENTS OF THE COMPANY *(Continued)*

4. Long-term Equity Investment *(Continued)*

(4) Principal Operation Revenue/ Cost

Items	Accumulated amount this year		Accumulated amount Last year	
	Revenue	Cost	Revenue	Cost
Revenue from sale and processing	146,248,123	94,861,386	102,493,975	77,526,169

(5) Investment Income

Items	Accumulated amount this year	Accumulated amount last year
Provision for diminution in value of short-term investment	5,726,799	(5,726,799)
Income from investment in subsidiaries	4,113,494	—
Amortization of equity investment difference	(1,507,086)	—
Income from short-term investment	(3,205,724)	9,000,000
Total	5,127,483	3,273,201

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

7. RELATED PARTY RELATIONSHIP AND TRANSACTIONS

1. Details of Related Parties with Control Relationship

(1) Related Parties with Control Relationship

Name	Relationship with the company	Economic Nature	Place of registration	Scope of Business	Legal Representative
Jiaotong Group	substantial shareholders	state-owned	Xian city	Develop, manufacture, sales of electronic products, chemical products, equipment, building materials, telecommunication products, environmental protection products and biological products; assume domestic commerce and material trade; Import technology, raw materials, machinery, equipment, instrument and accessories necessary to research and production; Process with materials provided; And export technological products and technology produced by enterprises owned by the university.	Yue Huafeng
Xian Ser Turbo Machinery Company Limited (Xian Ser)	subsidiary	Limited reliability	Xian city	Design, develop and sales of turbo-machinery	Wang Shangjin
Shannxi Hengtong Intelligent Machine Company Limited (Shannxi Hengtong)	subsidiary	Limited reliability	Xian city	Develop and sale of manufacturing moulds, machinery, equipment, electronic products, software and hardware	Lu Bingheng
西安交大思源智能電器有限公司	subsidiary	Limited reliability	Xian city	Develop, manufacture and Sales of electronic products, electronic machinery and products of electronic power; Provide technology services	Zhang Hanrong
昆明交大昆機自動機器有限公司	subsidiary	Limited reliability	Kunming city	Develop, apply and integrate hardware and software; Retail, wholesale, purchase on behalf of others and consign electronic products, machinery and electronic machinery.	Zhang Hanrong

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

7. RELATED PARTY RELATIONSHIP AND TRANSACTIONS (Continued)

1. Details of Related Parties with Control Relationship (Continued)

(2) Registered Capital of Related Parties with Controlling Relationship

Name	Amount at 1st January, 2002	Increase this year	Decrease this year	Amount at 31st December, 2002
Jiaotong Group	30,000,000	—	—	30,000,000
Xian Ser Turbo Machinery Company Limited (Xian Ser)	2,000,000	—	—	2,000,000
Shannxi Hengtong Intelligent Machine Company Limited (Shannxi Hengtong)	600,000	—	—	600,000
西安交大思源智能電器有限公司		35,000,000	—	35,000,000
昆明交大昆機自動機器有限公司		20,230,000	—	20,230,000

(3) Shares and equity held by related parties with controlling relationship

Name	Amount at 1st January, 2002		Increase this year	Decrease this year	Amount at 31st December, 2002	
	Amount	Proportion (%)			Amount	Proportion (%)
Jiaotong Group	71,052,146	29%	—	—	71,052,146	29%
Xian Ser Turbo Machinery Company Limited	1,600,000	80%	—	—	1,600,000	80.00%
Shannxi Hengtong Intelligent Machine Company Limited	540,000	90%	—	—	540,000	90.00%
西安交大思源智能電器有限公司	—	—	27,310,000	—	27,310,000	78.03%
昆明交大昆機自動機器有限公司	—	—	18,390,000	—	18,390,000	90.91%

2. Related Parties with non-controlling Relationship

Name	Relationship with the Company
Kunji Group Company	Second-largest shareholders designated to manage equity
Yunnan Government	Promoter's shareholders
Jiaoda Resources	Subsidiary of substantial shareholder of the Company

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

7. RELATED PARTY RELATIONSHIP AND TRANSACTIONS *(Continued)*

3. Related Party Transactions

(1) Sales of goods

The Company sold goods amounting to RMB1,113,504 to related parties in 2002. The Company sold goods amounting to RMB2,000,000 to related parties in 2001. The details of sales are as follows:

Name	Sales incurred this year	Sales incurred last year
Kunji Group Company	573,504	1,003,419
Xian Ser	—	996,581
Total	<u>573,504</u>	<u>2,000,000</u>

The Company signed with Kunji Group a future sale contract involving RMB250,000.

The selling price of machine tools is decided at the market price.

(2) Provision and Receipts of Service

On 15 th November 1993, the Company entered into an agreement with Kunji Group Company relating to the provision of certain services to each other after the reorganization. Pursuant to this agreement, the Company agreed to provide certain public utility services available to the Company such as water and electricity to Kunji Group Company, while Kunji Group Company agreed to provide certain services to the Company including gardening service and transportation service. Service fee is reviewed by both parties on an annual basis and is determined by reference first to the standards set by the relevant government department for that particular service. If there are no applicable State standards, the Company and Kunji Group Company will determine the service fees based on market prices or transacted price at arm's length negotiations.

The connected transactions between the Company and the Kunji Group Company are as follows:

Transaction events	Amount incurred this year	Amount incurred last year
Utility service fees received from Kun Ji Group Company	611,417	191,630
Transportation service fees paid to Kun Ji Group Company	—	317,856
The provision of medical service from Kun Ji Group Company to the Company's employees	1,343,125	1,712,786
The provision of social and education services from Kun Ji Group Company to the Company's employees	570,000	1,904,061
Gardening expense paid to Kun Ji Group Company.	<u>1,044,434</u>	<u>—</u>
Total	<u>3,568,976</u>	<u>4,126,333</u>

(3) Leases

In December 2001, the Company leased back portion of premise and land use right at annual rent of RMB607,760 and RMB407,520 respectively after reorganization. The lease term is 20 years.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

7. RELATED PARTY RELATIONSHIP AND TRANSACTIONS (Continued)

3. Related Party Transactions (Continued)

(4) Other Transactions

- (1) Loans of the Company amounted to RMB10,000,000 are guaranteed by Xian Jiaoda Resources in this year.
- (2) The Company had the following transactions with Kunji Group Company or companies under its control.

Transaction events	Amount incurred this year	Amount incurred last year
Sales commission	—	58,700
Sales of raw materials	—	67,782
Sub-contracting fees received	—	126,671
Sub-contracting fees paid	—	95,159
Construction costs paid	857,191	329,600
Sales of accounts receivable	—	11,398,114
Total	857,191	12,076,026

- (3) The Company had the following transactions with Jiaoda Industrial Group Company or companies under its control:

Transaction events	Amount incurred this year	Amount incurred last year
Water and electricity service		
Fees paid to Jiaoda Industrial Group	557,790	—
Interest expense paid to Jiaoda Resources	408,000	—
Total	965,790	—

- (4) Transactions between the Company and Xian Jiaotong University, investor of Jiaoda Industrial Group are as follows:

Transaction events	Amount incurred this year	Amount incurred last year
Sales of goods to Xian Jiaotong University	177,300	—
Research expense paid to Xian Jiaotong University	550,000	—
Total	727,300	—

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

7. RELATED PARTY RELATIONSHIP AND TRANSACTIONS *(Continued)*

4. Balances of Connected Transactions

(1) Other receivables

Items	Amount at the year end	Amount at the beginning
Jiaoda Industrial Group	488,338	4,761,979
Kunji Group	593,332	1,204,749
Jiaoda Resources	109,803	
Total	<u>1,191,473</u>	<u>5,966,728</u>

(2) Prepayments

Items	Amount at the year end	Amount at the beginning
Kunji Group	500,000	—

Prepayment represents service fees in 2003 prepaid to Kunji Group.

(3) Payables

Items	Amount at the year end	Amount at the beginning
Jiaoda Group	125,000	—

(4) Other Payables

Items	Amount at the year end	Amount at the beginning
Jiaoda Industrial Group	3,340,000	7,837,126
Kunji Group Company	1,065,808	3,101,936
Jiaoda Resources	—	4,963,003
Total	<u>4,405,808</u>	<u>15,902,065</u>

(5) Long-term payables due within 1 year

Items	Amount at the year end	Amount at the beginning
Yunnan Government	342,169	342,169

(6) Long-term payables

Items	Amount at the year end	Amount at the beginning
Yunnan Government	6,159,040	6,501,209

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

8. CONTINGENT EVENTS

The Company has no contingent events.

9. COMMITMENTS

Lease commitments

The Company was obliged to pay the minimum rental payables as follows:

Accounting fiscal year	Amount
2003	342,169
2004	342,169
2005	342,169
After 3 years	5,474,702
Total	6,501,209

10. POST BALANCE SHEET EVENT

The Company has no significant post balance sheet events.

11. DEBT RESTRUCTURING EVENTS

The Company has no debt restructuring events.

12. OTHER SIGNIFICANT EVENTS

Difference between PRC GAAP and Hong Kong GAAP:

These financial statements are prepared according to PRC GAAP, which are different from those prepared according to HK GAAP.

At balance sheet day, The amount of net profit and net assets are RMB6,077,477 and RMB506,778,046 respectively according to PRC GAAP. These figures can be reconciled to that under HK GAAP as follows:

Items	Net profit	Net assets
In accordance to the PRC GAAP	6,077,479	506,778,045
Interest subsidy from the PRC government	1,311,520	—
Amortisation on deferred gain on sale and lease back transaction	(664,425)	—
Gain on sale and lease back transaction deferred and amortised	—	7,622,920
In accordance to the HK GAAP	6,724,574	514,400,965

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**Deloitte
Touche
Tohmatsu**

TO THE SHAREHOLDERS OF JIAODA KUNJI HIGH-TECH COMPANY LIMITED

交大昆機科技股份有限公司

(a sino-foreign joint stock limited company established in the People's Republic of China with limited liability)

We have audited the financial statements on pages 68 to 101 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Company's Directors are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently.

It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

BASIS OF OPINION

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the circumstances of the Company and the Group, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

OPINION

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31st December, 2002 and of the profit and cash flows of the Group for the year then ended and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

DELOITTE TOUCHE TOHMATSU
Certified Public Accountants
Hong Kong
6th April, 2003

CONSOLIDATED INCOME STATEMENT

FOR THE YEAR ENDED 31ST DECEMBER, 2002

	NOTES	2002 RMB'000	2001 RMB'000
Turnover	5	179,628	102,494
Cost of sales		(120,283)	(77,526)
Gross profit		59,345	24,968
Other operating income	6	10,196	15,601
Net gain arising from assets restructuring	30	—	7,858
Administrative expenses		(40,865)	(21,131)
Distribution costs		(11,519)	(5,523)
Unrealised holding losses of other investments		(94)	(6,003)
Profit from operations	7	17,063	15,770
Finance costs	8	(8,592)	(7,297)
Non-operating expenses		(89)	(237)
Profit before taxation		8,382	8,236
Taxation	9	(723)	—
Profit after taxation		7,659	8,236
Minority interest		(933)	—
Net profit for the year	10	6,726	8,236
Earnings per share	12	2.7 cents	3.4 cents

CONSOLIDATED BALANCE SHEET

AT 31ST DECEMBER, 2002

	NOTES	2002 RMB'000	2001 RMB'000
Non-current assets			
Property, plant and equipment	13	294,453	283,008
Goodwill	15	21,987	24,430
Intangible assets	16	35,499	39,444
Investment in an associate	17	250	—
Deferred costs	18	3,832	3,926
		<u>356,021</u>	<u>350,808</u>
Current assets			
Inventories	19	195,479	162,261
Trade receivables	20	56,122	41,253
Other receivables		24,353	21,356
Amount due from an associate	36	400	—
Amount due from a related company	36	28	—
Other investments	21	13	42,130
Deposits placed with securities company		82,656	7,143
Taxation recoverable		16	142
Pledged cash deposits	34	40,505	31,818
Bank balances and cash	22	79,446	106,205
		<u>479,018</u>	<u>412,308</u>
Current liabilities			
Trade payables	23	19,026	10,165
Other payables		77,524	61,163
Amounts due to related companies	36	197	8,038
Taxation payable		1,379	969
Obligations under finance leases - due within one year	24	213	468
Bank borrowings - due within one year	25	188,800	130,200
		<u>287,139</u>	<u>211,003</u>
Net current assets		<u>191,879</u>	<u>201,305</u>
		<u>547,900</u>	<u>552,113</u>

CONSOLIDATED BALANCE SHEET

AT 31ST DECEMBER, 2002

	NOTES	2002 RMB'000	2001 RMB'000
Capital and reserves			
Share capital	27	245,007	245,007
Reserves	28	269,395	262,669
		514,402	507,676
Minority interests		12,638	2,175
Non-current liabilities			
Obligations under finance leases - due after one year	24	3,838	4,439
Bank borrowings - due after one year	25	3,000	29,800
Deferred gain	26	3,822	4,023
Other long-term loans	29	10,200	4,000
		20,860	42,262
		547,900	552,113

The financial statements on pages 68 to 101 were approved and authorised for issue by the Board of Directors on 6th April, 2003 and are signed on its behalf by:

DIRECTOR
YUE HUA FENG

DIRECTOR
ZHANG HAN RONG

BALANCE SHEET

AT 31ST DECEMBER, 2002

	NOTES	2002 <i>RMB'000</i>	2001 <i>RMB'000</i>
Non-current assets			
Property, plant and equipment	13	263,929	264,027
Interests in subsidiaries	14	68,543	22,843
Amounts due from subsidiaries	14	25,654	—
Goodwill	15	—	9,359
Intangible assets	16	23,724	39,444
Deferred costs	18	3,832	3,926
		385,682	339,599
Current assets			
Inventories	19	169,384	153,351
Trade receivables		34,249	36,466
Other receivables		4,754	13,395
Trade receivables from subsidiaries		5,411	1,205
Amount due from a related company	36	28	4,605
Other investments	21	13	42,130
Deposits placed with securities company		82,656	7,143
Taxation recoverable		16	143
Pledged time deposits	34	37,142	31,818
Bank balances and cash	22	42,062	104,544
		375,715	394,800
Current liabilities			
Trade payables		6,406	7,767
Other payables		43,523	45,974
Taxation payables		—	252
Obligations under finance leases - due within one year	24	213	468
Bank borrowings - due within one year	25	188,800	130,000
		238,942	184,461
Net current assets		136,773	210,339
		522,455	549,938

BALANCE SHEET

AT 31ST DECEMBER, 2002

	NOTES	2002 RMB'000	2001 RMB'000
Capital and reserves			
Share capital	27	245,007	245,007
Reserves	28	266,788	262,669
		511,795	507,676
Non-current liabilities			
Obligations under finance leases - due after one year	24	3,838	4,439
Bank borrowings - due after one year	25	—	29,800
Deferred gain	26	3,822	4,023
Other long-term loan	29	3,000	4,000
		10,660	42,262
		522,455	549,938

DIRECTOR
YUE HUA FENG

DIRECTOR
ZHANG HAN RONG

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31ST DECEMBER, 2002

	Share capital RMB'000	Share premium RMB'000	Capital reserve RMB'000 (Note 28)	Statutory surplus reserve RMB'000 (Note 28)	Statutory public welfare fund RMB'000 (Note 28)	Accumulated losses RMB'000 (Note 28)	Total RMB'000
At 1st January, 2001	245,007	293,745	10,225	8,406	8,406	(66,349)	499,440
Net profit for the year	—	—	—	—	—	8,236	8,236
At 31st December, 2001	245,007	293,745	10,225	8,406	8,406	(58,113)	507,676
Net profit for the year	—	—	—	—	—	6,726	6,726
At 31st December, 2002	245,007	293,745	10,225	8,406	8,406	(51,387)	514,402

CONSOLIDATED CASH FLOW STATEMENT

FOR THE YEAR ENDED 31ST DECEMBER, 2002

	2002 RMB'000	2001 RMB'000
OPERATING ACTIVITIES		
Profit before taxation	8,382	8,236
Adjustments for:		
Interest income	(893)	(2,508)
Interest expenses	8,608	7,301
Interest subsidy from finance bureau	(1,312)	(1,688)
Investment income on other investments	(5,240)	(9,000)
Exchange gain	(16)	(4)
Amortisation of deferred income	(201)	—
Depreciation and amortisation of property, plant and equipment	21,263	16,003
Amortisation of goodwill	2,443	—
Amortisation of intangible assets	3,945	—
Amortisation of prepaid rental	94	93
Loss on disposal of property, plant and equipment	145	518
Unrealised holding losses on other investments	94	6,003
Net gain arising from assets restructuring	—	(7,858)
Impairment loss recognised in respect of property, plant and equipment	—	3,395
Loss on disposal of other investments	—	120
Operating cash flows before movements in working capital	37,312	20,611
Increase in inventories	(33,218)	(23,543)
Increase in trade receivables	(14,869)	(6,555)
Increase in other receivables	(2,997)	(14,927)
Increase in amount due from a related company	(28)	—
Increase (decrease) in trade payables	8,861	(674)
Increase in other payables	16,361	1,213
Decrease in amounts due to related companies	(7,841)	—
Cash from (used in) operations	3,581	(23,875)
Income taxes paid	(187)	—
Interest paid	(10,078)	(8,250)
Interest subsidy from finance bureau	1,312	1,688
NET CASH USED IN OPERATING ACTIVITIES	(5,372)	(30,437)

CONSOLIDATED CASH FLOW STATEMENT

FOR THE YEAR ENDED 31ST DECEMBER, 2002

	NOTES	2002 RMB'000	2001 RMB'000
INVESTING ACTIVITIES			
Deposits placed with securities company		(80,000)	(7,018)
Purchase of property, plant and equipment		(33,102)	(28,431)
(Increase) decrease in pledged time deposits		(8,687)	10,606
Advance to an associate		(400)	—
Investment in an associate		(250)	—
Refund of deposits placed with securities company		46,510	56,190
Withdrawal of time deposits		7,424	20,000
Investment income on other investments		5,240	9,000
Proceeds from disposal of property, plant and equipment		1,719	563
Interest received		893	2,508
Proceeds from disposal of other investments		—	5,810
Net cash inflow from assets restructuring	30	—	5,212
Purchase of other investments		—	(42,982)
Placement of time deposits		—	(7,424)
NET CASH (USED IN) GENERATED FROM INVESTING ACTIVITIES		(60,653)	24,034
CASH FLOWS FROM FINANCING ACTIVITIES			
New bank loans raised		156,000	90,000
Capital contributed by minority shareholder		9,530	—
Other borrowings raised		7,200	—
Repayment of bank loans		(124,200)	(50,200)
Repayment of other borrowings		(1,000)	—
Repayments of obligations under finance leases		(856)	—
NET CASH GENERATED FROM FINANCING ACTIVITIES		46,674	39,800
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS		(19,351)	33,397
CASH AND CASH EQUIVALENTS AT BEGINNING OF THE YEAR		98,781	65,380
EFFECT OF FOREIGN EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS		16	4
CASH AND CASH EQUIVALENTS AT END OF THE YEAR REPRESENTING			
Bank balances and cash	22	79,446	98,781

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

1. GENERAL

The Company is a sino-foreign joint stock limited company established in the Mainland People's Republic of China (the "PRC"). The Company acts as an investment holding company and it is also engaged in the design, development, manufacture and sale of machine tools, precision measuring equipment and precision transducers. The principal activities of its subsidiaries are set out in note 14.

2. ADOPTION OF STATEMENTS OF STANDARD ACCOUNTING PRACTICE

In the current year, the Group has adopted, for the first time, a number of new and revised Statements of Standard Accounting (SSAPs) issued by the Hong Kong Society of Accountants. The adoption of these Standards has resulted in a change in the format of presentation of the cash flow statement and the statement of changes in equity, but has had no material effect on the results for the current or prior accounting periods. Accordingly, no prior year adjustment has been required.

Cash Flow Statements

In the current year, the Group has adopted SSAP 15 (Revised) Cash Flow Statements. Under SSAP 15 (Revised), cash flows are classified under three headings - operating, investing and financing, rather than the previous five headings. Interest and dividends, which were previously presented under a separate heading, are classified as operating and investing cash flows. Cash flows arising from taxes on income are classified as operating activities, unless they can be separately identified with investing or financing activities.

In addition, the amounts presented for cash and cash equivalents have been amended to exclude cash balances held for investment purposes/short-term loans that are financing in nature.

Employee Benefits

In the current year, the Group has adopted SSAP 34 Employee Benefits, which introduces measurement rules for employee benefits, including retirement benefit plans. Because the Group's participates only in defined contribution retirement benefit schemes, the adoption of SSAP 34 has not had any material impact on the financial statements.

3. SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared under the historical cost convention in accordance with accounting principles generally accepted in Hong Kong. The principal accounting policies adopted are as follows:

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries made up to 31st December each year.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Revenue recognition

Sales of goods are recognised when goods are delivered and title has passed.

Service income is recognised when services are provided.

Interest income is accrued on a time basis by reference to the principal outstanding and at the interest rate applicable.

Interest subsidy from government is credited to income when the related interest expenses are incurred.

Dividend income from investments is recognised when the Group's rights to receive payment have been established.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Property, plant and equipment

Property, plant and equipment are stated at cost less depreciation, amortisation and accumulated impairment losses.

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sale proceeds and the carrying amount of the asset and is recognised in the income statement.

The cost of land use rights is amortised over the terms of the contract after obtaining the certificate of land occupancy rights.

Depreciation and amortisation are provided to write off the cost of property, plant and equipment, other than construction-in-progress, over their estimated useful lives, after taking into account their estimated residual value, using the straight line method at the following rates per annum:

Buildings	2.5%
Plant and machinery	2% - 8%
Furniture, fixtures and equipment	6% - 10%
Motor vehicles	6% - 10%

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets or, where shorter, the term of the relevant lease.

Construction-in-progress

Construction-in-progress is stated at cost which includes all development expenditure and other direct costs, including borrowing costs, attributable to such projects. The cost of completed construction work is transferred to the appropriate asset category.

Goodwill

Goodwill arising on consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary.

Goodwill is capitalised as a separate asset and amortised on a straight-line basis over its useful economic life.

Intangible assets

Intangible assets are stated at cost less accumulated amortisation and accumulated impairment losses.

The cost of technological knowhow is amortised on a straight line basis over its expected useful life of ten years.

Impairment

At each balance sheet date, the Group reviews the carrying amounts of its assets to determine whether there is any indication that those assets have suffered an impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. Impairment losses are recognised as an expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, such that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Investments in subsidiaries

Investments in subsidiaries are included in the Company's balance sheet at cost less any identified impairment loss.

Interests in associates

The consolidated income statement includes the Group's share of the post-acquisition results of its associates for the year. In the consolidated balance sheet, interests in associates are stated at the Group's share of the net assets of the associates, less any identified impairment loss.

Inventories

Inventories are stated at the lower of cost and net realisable value.

Cost is calculated using the weighted average cost method. Net realisable value represents the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Investments in securities

Investments in securities are recognised on a trade-date basis and are initially measured at cost.

Investments other than held-to-maturity debt securities are classified as investment securities and other investments.

Investment securities, which are securities held for an identified long-term strategic purpose, are measured at subsequent reporting dates at cost, as reduced by any impairment loss that is other than temporary.

Other investments are measured at fair value, with unrealised gains and losses included in net profit or loss for the year.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, are capitalised as part of the cost of those assets. Capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale.

All other borrowing costs are recognised as an expense in the period in which they are incurred.

Leased assets

Leases are classified as finance leases when the terms of the lease transfer substantially all the risks and rewards of ownership of the assets concerned to the Group. Assets held under finance leases are capitalised at their fair values at the date of acquisition. The corresponding liability to the lessor, net of interest charges, is included in the balance sheet as a finance lease obligation. Finance costs, which represent the difference between the total leasing commitments and the outstanding principal amount at the inception of the finance lease, are charged to the income statement over the period of the relevant lease so as to produce a constant periodic rate of charge on the remaining balance of the obligations for each accounting period.

All other leases are classified as operating leases and the annual rentals are charged to the income statement on a straight-line basis over the relevant lease term.

Where assets are sold to a lessor and leased back by the Group, and the transaction results in a finance lease, any excess of sales proceeds over the carrying amount of the assets is deferred and amortised over the appropriate lease term.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

Taxation

The charge for taxation is based on the results for the year as adjusted for items which are non-assessable or disallowed. Timing differences arise from the recognition for tax purposes of certain items of income and expense in a different accounting period from that in which they are recognised in the financial statements. The tax effect of timing differences, computed under the liability method, is recognised as deferred taxation in the financial statements to the extent that it is probable that a liability or an asset will crystallise in the foreseeable future.

Research and development expenditure

Expenditure on research activities is recognised as an expense in the period in which it is incurred.

An internally-generated intangible asset arising from development expenditure is recognised only if it is anticipated that the development costs incurred on a clearly defined project will be recovered through future commercial activity. The resultant asset is amortised on a straight-line basis over its estimated useful life.

Retirement scheme cost

The Group participates in state-managed retirement plans pursuant to which the Group pays a fixed percentage of its qualifying staff's wages as contribution to the plan. The contribution payable to the retirement plan in respect of the year is charged to the income statement.

Foreign currencies

The Group maintains its books and records in Renminbi.

Transactions in foreign currencies are translated at the rates ruling on the dates of the transactions quoted by the People's Bank of China. Monetary assets and liabilities denominated in foreign currencies are re-translated at the middle market rates ruling on the balance sheet date quoted by the People's Bank of China. Profits and losses arising on exchange are dealt with in the income statement.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

4. SEGMENT INFORMATION

In accordance with the Group's internal financial reporting, the Group has determined that business segment by products is its primary reporting segment.

Business segments

The Group reports its primary segment information by products, which are boring machines, computerised embroidery machines, intelligence electrical appliances, turbo machines and laser phototyping machines. Segment information about these products is presented below:

2002

	Boring machines RMB'000	Computerised embroidery machines RMB'000	Intelligence electrical appliances RMB'000	Turbo machines RMB'000	Laser phototyping machines RMB'000	Consolidated RMB'000
TURNOVER	134,931	3,071	8,250	28,726	4,650	179,628
SEGMENT RESULT	5,419	709	711	5,409	(425)	11,823
Investment income on other investments						5,240
Profit from operations						17,063
Finance costs						(8,592)
Unallocated corporate expense						(89)
Profit before taxation						8,382
Taxation						(723)
Profit after taxation						7,659
Minority interest						(933)
Net profit for the year						6,726

The following is an analysis of the carrying amount of segment assets and segment liabilities, analysed by products:

	Boring machines RMB'000	Computerised embroidery machines RMB'000	Intelligence electrical appliances RMB'000	Turbo machines RMB'000	Laser phototyping machines RMB'000	Eliminations RMB'000	Consolidated RMB'000
ASSETS							
Segment assets	706,365	26,431	47,197	74,221	8,481	(27,906)	834,789
Investment in an associate							250
Consolidated total assets							835,039
LIABILITIES							
Segment liabilities	(250,931)	(5,492)	(11,066)	(58,070)	(10,346)	27,906	(307,999)
OTHER INFORMATION							
Capital additions	30,883	9	275	3,235	170	—	34,572
Depreciation and amortisation of property, plant and equipment	19,167	10	161	1,346	579	—	21,263
Amortisation of goodwill	2,443	—	—	—	—	—	2,443
Amortisation of intangible assets	3,945	—	—	—	—	—	3,945
Loss on disposal of property, plant and equipment	—	—	—	—	145	—	145

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

4. SEGMENT INFORMATION (Continued)

Business segments (Continued)

2001

	Boring machines RMB'000	Computerised embroidery machines RMB'000	Intelligence electrical appliances RMB'000	Turbo machines RMB'000	Laser phototyping machines RMB'000	Consolidated RMB'000
TURNOVER	102,494	—	—	—	—	102,494
RESULT						
Segment result	6,770	—	—	—	—	6,770
Investment income on other investments						9,000
Profit from operations						15,770
Finance costs						(7,297)
Unallocated corporate expenses						(237)
Profit before taxation						8,236
Taxation						—
Net profit for the year						8,236

The following is an analysis of the carrying amount of segment assets and segment liabilities, analysed by products:

	Boring machines RMB'000	Computerised embroidery machines RMB'000	Intelligence electrical appliances RMB'000	Turbo machines RMB'000	Laser phototyping machines RMB'000	Eliminations RMB'000	Consolidated RMB'000
ASSETS							
Segment assets	726,967	3,860	3,589	28,952	953	(1,205)	763,116
LIABILITIES							
Segment liabilities	(227,311)	(3,860)	(3,589)	(17,154)	(2,556)	1,205	(253,265)
OTHER INFORMATION							
Capital additions	63,877	4,039	9,044	21,701	4,501	—	103,162
Depreciation and amortisation of property, plant and equipment	16,003	—	—	—	—	—	16,003
Loss on disposal of property, plant and equipment	518	—	—	—	—	—	518

More than 90% of the Group's turnover and operating results are derived from the PRC market. All assets and liabilities of the Company are located in the PRC as all operations are carried in the PRC and therefore no further analysis are presented.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

5. TURNOVER

Turnover represents the amounts received and receivable, which is net of value-added tax ("VAT"), business tax and returns, for goods sold and services rendered by the Group to outside customers during the year.

An analysis of the Group's turnover is as follows:

	2002 RMB'000	2001 RMB'000
Sales of goods	166,374	91,291
Services rendered	13,254	11,203
	<u>179,628</u>	<u>102,494</u>

6. OTHER OPERATING INCOME

	2002 RMB'000	2001 RMB'000
Other operating income comprises:		
Interest income on deposits with banks and other financial institutions	893	2,508
Investment income on other investments	5,240	9,000
VAT for new products refunded	1,323	1,700
Interest subsidy from finance bureau	1,312	1,688
Others	1,428	705
	<u>10,196</u>	<u>15,601</u>

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

7. PROFIT FROM OPERATIONS

	2002 RMB'000	2001 RMB'000
Profit from operations has been arrived at after charging:		
Staff costs including:		
Directors' and supervisors' remuneration		
- Fees		
Executive Directors and supervisors	92	70
Non-Executive Director	72	4
Independent Non-Executive Directors	108	35
- Other emoluments		
Executive Directors and Supervisors	427	455
Non-Executive Director	42	—
	<u>741</u>	<u>564</u>
Retirement schemes contributions	4,541	4,096
Other staff costs	<u>42,052</u>	<u>33,109</u>
	<u>47,334</u>	<u>37,769</u>
Auditors' remuneration		
- current year	2,046	1,280
- underprovision in prior years	83	35
	<u>2,129</u>	<u>1,315</u>
Amortisation of prepaid rental	94	93
Amortisation of goodwill included in administrative expenses	2,443	—
Amortisation of intangible assets included in administrative expenses	3,945	—
Depreciation and amortisation of property, plant and equipment		
- owned by the Group	21,224	16,003
- held under finance lease	39	—
	<u>27,745</u>	<u>16,096</u>
Loss on disposal of property, plant and equipment	145	518
Impairment loss recognised in respect of property, plant and equipment	—	3,395
Loss on disposal of other investments	—	120
Research and development costs	3,819	2,747
and after crediting:		
Amortisation of deferred income included in administrative expenses	<u>201</u>	<u>—</u>
Emoluments of Directors are within the following bands:		
	2002	2001
Nil to HK\$1,000,000	<u>15</u>	<u>19</u>

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

7. PROFIT FROM OPERATIONS *(Continued)*

The emoluments of the five highest paid employees are analysed as follows:

The five highest paid employees of the Group in the year included five (2001: three) Executive Directors of the Company, details of whose emoluments are set out above. The emoluments of the remaining two individuals for the year ended 31st December, 2001 were analysed as follows:

	2002 RMB'000	2001 RMB'000
Salaries	—	133
Contributions to retirement benefits schemes	—	6
	<u>—</u>	<u>139</u>

During the year, no emoluments were paid by the Group to the respective five highest paid individuals, including Directors, as an inducement to join or upon joining the Group or as compensation for loss of office. In addition, during the year, no Director waived any emoluments.

8. FINANCE COSTS

	2002 RMB'000	2001 RMB'000
Interest on:		
- bank borrowings wholly repayable within five years	9,949	8,250
- obligations under finance leases	129	—
Total borrowing costs	<u>10,078</u>	<u>8,250</u>
Less: amount capitalised in construction-in-progress	<u>(1,470)</u>	<u>(949)</u>
	8,608	7,301
Exchange gain	<u>(16)</u>	<u>(4)</u>
	<u>8,592</u>	<u>7,297</u>

9. TAXATION

Pursuant to a document issued by the PRC State Tax Bureau on 21st October, 1993 and confirmed by a notice issued by the Ministry of Finance and the State Tax Bureau on 18th April, 1994, the Company's profit is subject to income tax at a rate of 15% as from 1st January, 1993.

Pursuant to the relevant laws and regulations in the PRC, the Group's PRC subsidiaries are entitled to an exemption from PRC income tax for the two years starting from the first production year. The taxation charge for the year represents provision for PRC income tax for certain subsidiaries taking into account of these tax incentives.

No provision for PRC income tax of the Company has been made in the financial statements as the Company's assessable profit for the year was wholly absorbed by tax losses brought forward.

At 31st December, 2002, the Group had an unrecognised deferred tax asset of RMB1,647,000 (2001: RMB2,167,000), which represents the tax effect of timing differences arising as a result of tax losses available to set off against future profits. The deferred tax asset has not been recognised in the financial statements as it is not certain that the benefit will crystallise in the foreseeable future.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

10. PROFIT AFTER TAXATION BEFORE ALLOCATION TO STATUTORY RESERVES

In accordance with Article 177 of the PRC Company Law, profit after taxation is applied as follows:

- (1) making up prior year losses;
- (2) allocation to statutory surplus reserve;
- (3) allocation to statutory public welfare fund;
- (4) allocation to discretionary surplus reserve; and
- (5) payment of dividends in respect of ordinary shares.

The board of Directors has proposed that no appropriation be made for the year.

11. TRANSFER TO STATUTORY SURPLUS RESERVE AND STATUTORY PUBLIC WELFARE FUND

No transfer is proposed to be made to the statutory surplus reserve or the statutory public welfare fund as the Company has accumulated losses.

12. EARNINGS PER SHARE

The calculation of earnings per share is based on the net profit for the year of RMB6,726,000 (2001: RMB8,236,000) and the 245,007,400 (2001: 245,007,400) shares in issue throughout the year.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

13. PROPERTY, PLANT AND EQUIPMENT

	Land use rights RMB'000	Buildings under medium term lease in the PRC RMB'000	Plant and machinery RMB'000	Furniture, fixtures and equipment RMB'000	Motor vehicles RMB'000	Construction- in-progress RMB'000	Total RMB'000
THE GROUP							
COST							
At 1st January, 2002	17,568	110,092	200,665	27,480	7,982	35,910	399,697
Additions	—	3,840	8,723	2,839	1,861	17,309	34,572
Transfers	—	6,893	527	547	445	(8,412)	—
Disposals	—	(215)	(2,468)	(1,201)	(441)	(610)	(4,935)
At 31st December, 2002	17,568	120,610	207,447	29,665	9,847	44,197	429,334
DEPRECIATION AND AMORTISATION							
At 1st January, 2002	4,194	17,156	77,196	14,502	2,969	672	116,689
Provided for the year	320	2,829	15,606	1,868	640	—	21,263
Eliminated on disposals	—	(32)	(2,245)	(576)	(198)	(20)	(3,071)
At 31st December, 2002	4,514	19,953	90,557	15,794	3,411	652	134,881
NET BOOK VALUE							
At 31st December, 2002	13,054	100,657	116,890	13,871	6,436	43,545	294,453
At 31st December, 2001	13,374	92,936	123,469	12,978	5,013	35,238	283,008
THE COMPANY							
COST							
At 1st January, 2002	17,568	109,598	179,438	25,975	7,684	35,868	376,131
Additions	—	3,602	7,113	2,151	767	17,250	30,883
Transfers	—	6,893	527	547	445	(8,412)	—
Transferred to subsidiaries	—	(513)	(4,854)	(1,868)	(2,475)	(4,305)	(14,015)
Disposals	—	(215)	(2,468)	(671)	(441)	(610)	(4,405)
At 31st December, 2002	17,568	119,365	179,756	26,134	5,980	39,791	388,594
DEPRECIATION AND AMORTISATION							
At 1st January, 2002	4,194	17,143	73,249	14,027	2,819	672	112,104
Provided for the year	320	2,803	13,837	1,599	608	—	19,167
Transferred to subsidiaries	—	(68)	(2,726)	(414)	(460)	—	(3,668)
Eliminated on disposals	—	(32)	(2,245)	(443)	(198)	(20)	(2,938)
At 31st December, 2002	4,514	19,846	82,115	14,769	2,769	652	124,665
NET BOOK VALUE							
At 31st December, 2002	13,054	99,519	97,641	11,365	3,211	39,139	263,929
At 31st December, 2001	13,374	92,455	106,189	11,948	4,865	35,196	264,027

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

13. PROPERTY, PLANT AND EQUIPMENT *(Continued)*

The Group was granted the rights to use the land, on which its buildings are situated, by the relevant PRC authorities for a period of 50 years from October 1993 onwards.

At 31st December, 2002, the cumulative amount of interest capitalised in construction-in-progress amounted to RMB3,552,000 (2001: RMB2,082,000).

The net book value of property, plant and equipment of the Group at 31st December, 2002 includes an amount of approximately RMB5,534,000 (2001: RMB5,573,000) in respect of assets held under finance leases.

14. INTERESTS IN SUBSIDIARIES/AMOUNTS DUE FROM SUBSIDIARIES

	2002 RMB'000	2001 RMB'000
Unlisted shares, at cost	68,543	22,843
Amounts due from subsidiaries	25,654	—

During the year, the Company advanced approximately RMB25.7 million to certain non wholly-owned subsidiaries. Approximately RMB13.0 million of the amount advanced was for the purpose of additional capital contribution to two non wholly-owned subsidiaries which are in the process of applying to the relevant PRC authorities to increase their registered capital as approved by the Board of Directors on 8th August, 2002. The other advances of approximately RMB12.7 million were advanced in proportion to the Group's interests in these subsidiaries and were for the purpose of financing the operations of the non-wholly owned subsidiaries. These advances are unsecured and have no fixed repayment terms. In the opinion of the Directors, repayment of the amounts will not be demanded in the coming financial year, and therefore, they are classified as non-current. Other than an amount of approximately RMB6.0 million which carries interest at prevailing market rates, the balances are interest-free.

Details of the Company's subsidiaries at 31st December, 2002 are as follows:

Name of subsidiary	Place of incorporation and operations	Registered capital	Proportion of registered capital held directly by the Company	Principal activities
Xian Ser Turbo Machinery Equipment Company Limited 西安賽爾機泵成套設備有限公司	PRC	RMB2,000,000	80%	Design, develop and sales of turbo-machinery
Shaanxi Hengtong Intelligence Machine Company Limited 陝西恒通智慧機器有限公司	PRC	RMB600,000	90%	Develop and sale of manufacturing moulds, machinery, equipment, electronic products, software and hardware
西安交大思源智能電器有限公司	PRC	RMB35,000,000	78.03%	Research, develop manufacturing and sale of automatic machines for industries such as water utilities, civil engineering and construction
昆明交大昆機自動機器有限公司	PRC	RMB20,230,000	90.91%	Research, develop, manufacturing and sale of intelligent computerised coloured embroidery machines

None of the subsidiaries had any debt securities outstanding at the end of the year or at any time during the year.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

15. GOODWILL

	THE GROUP RMB'000	THE COMPANY RMB'000
GROSS AMOUNT		
At 1st January, 2002	24,430	9,359
Transferred to the subsidiaries during the year	—	(9,359)
At 31st December, 2002	24,430	—
AMORTISATION		
At 1st January, 2002	—	—
Provided for the year	2,443	936
Transferred to the subsidiaries during the year	—	(936)
At 31st December, 2002	2,443	—
CARRYING AMOUNT		
At 31st December, 2002	21,987	—
At 31st December, 2001	24,430	9,359

The amortisation period adopted for goodwill is 10 years.

16. INTANGIBLE ASSETS

	THE GROUP RMB'000 (Note)	THE COMPANY RMB'000 (Note)
COST		
At 1st January, 2002	39,444	39,444
Transferred to the subsidiaries during the year	—	(13,084)
At 31st December, 2002	39,444	26,360
AMORTISATION		
At 1st January, 2002	—	—
Provided for the year	3,945	3,945
Transferred to the subsidiaries during the year	—	(1,309)
At 31st December, 2002	3,945	2,636
NET BOOK VALUE		
At 31st December, 2002	35,499	23,724
At 31st December, 2001	39,444	39,444

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

16. INTANGIBLE ASSETS (Continued)

Note:

The intangible assets are technical knowhow.

The cost of technical knowhow of RMB26,360,000 represents the laser prototyping and manufacturing technology and the controllable centrifugal energy conservation compressor technology.

The remaining balance of RMB13,084,000 represents the technical knowhow of developing intelligent computerised coloured embroidery machines and intelligent electrical appliances.

The technical knowhow is amortised over 10 years.

17. INVESTMENT IN AN ASSOCIATE

	THE GROUP	
	2002 RMB'000	2001 RMB'000
Share of net assets	250	—

Details of the associate which was held indirectly by the Company at 31st December, 2002 are as follows:

Name of associate	Place of incorporation /operation	Form of business structure	Proportion of nominal value of issued capital held indirectly by the Company	Principal activity
西安通大思源電器有限公司	PRC	Limited liability company	25%	Research, develop and sales of intelligent electrical appliance

The associate did not generate any profit or loss during the year.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

18. DEFERRED COSTS

THE GROUP AND THE COMPANY	Prepaid rental RMB'000
COST	
At 1st January, 2002 and 31st December, 2002	4,486
AMORTISATION	
At 1st January, 2002	560
Provided for the year	94
At 31st December, 2002	654
NET BOOK VALUE	
At 31st December, 2002	3,832
At 31st December, 2001	3,926

Pursuant to an agreement entered into between the Company and Kun Ji Group Company on 10th December, 1993, the Company and Kun Ji Group Company paid RMB2,000,000 and RMB3,000,000 respectively for the purpose of joint construction of staff quarters. In 1995, a further sum of RMB297,000 was paid by the Company. The staff quarters were completed in October 1995. Subsequently, the Company and Kun Ji Group Company are entitled to the ownership of the staff quarters and the Company is entitled to lease five floors as staff quarters for 48 years commencing January 1996. The lease rental is calculated with reference to the floor area occupied and the actual construction cost of the building. On this basis a further sum of RMB2,189,000 was paid by the Company in 1996, bring the aggregate sum paid for the lease to RMB4,486,000 which is accounted for as prepaid rental and is amortised over the lease period of 48 years.

19. INVENTORIES

	THE GROUP		THE COMPANY	
	2002	2001	2002	2001
	RMB'000	RMB'000	RMB'000	RMB'000
Raw materials	31,283	24,504	23,725	24,041
Work-in-progress	105,437	101,468	93,442	93,825
Finished goods	58,759	36,289	52,217	35,485
	<u>195,479</u>	<u>162,261</u>	<u>169,384</u>	<u>153,351</u>

Included in the above were inventories carried at net realisable value as follow:

	THE GROUP		THE COMPANY	
	2002	2001	2002	2001
	RMB'000	RMB'000	RMB'000	RMB'000
Raw materials	31,283	16,201	23,725	16,201
Work-in-progress	105,437	83,014	93,442	83,014
Finished goods	58,759	10,187	52,217	10,187
	<u>195,479</u>	<u>109,402</u>	<u>169,384</u>	<u>109,402</u>

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

20. TRADE RECEIVABLES

The Group agrees credit terms with its trade customers on an individual basis. An aged analysis of the Group's trade receivables is as follows:

	THE GROUP	
	2002 RMB'000	2001 RMB'000
Within one year	47,372	32,647
Between one to two years	5,932	7,013
Between two to three years	—	58
Over three years	2,818	1,535
	<u>56,122</u>	<u>41,253</u>

21. OTHER INVESTMENTS

	THE GROUP AND THE COMPANY	
	2002 RMB'000	2001 RMB'000
Equity securities:		
Listed in the PRC, at market value	<u>13</u>	<u>42,130</u>

22. BANK BALANCES AND CASH

	THE GROUP		THE COMPANY	
	2002 RMB'000	2001 RMB'000	2002 RMB'000	2001 RMB'000
Bank balances and cash	79,446	98,781	42,062	97,120
Time deposits	—	7,424	—	7,424
	<u>79,446</u>	<u>106,205</u>	<u>42,062</u>	<u>104,544</u>

23. TRADE PAYABLES

Details of the aged analysis of trade payables are as follows:

	THE GROUP	
	2002 RMB'000	2001 RMB'000
Within one year	11,538	7,837
Between one to two years	5,581	1,180
Between two to three years	1,098	11
Over three years	809	1,137
	<u>19,026</u>	<u>10,165</u>

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

24. OBLIGATIONS UNDER FINANCE LEASES

	THE GROUP AND THE COMPANY			
	Minimum lease payments		Present value of minimum lease payments	
	2002 RMB'000	2001 RMB'000	2002 RMB'000	2001 RMB'000
The maturity of obligations under finance leases is as follows:				
Within one year	342	710	213	468
In the second to fifth year inclusive	6,159	6,817	3,838	4,439
	6,501	7,527	4,051	4,907
Less: Future finance charge	(2,450)	(2,620)	—	—
Present value of obligations under finance leases	4,051	4,907	4,051	4,907
Less: Amount due for settlement within one year (shown under current liabilities)			(213)	(468)
Amount due after one year			3,838	4,439

All leases are on a fixed repayment basis and no arrangements have been entered into for contingent rental payments. The average term of the finance leases entered into is 20 years (2001: 6 years).

25. BANK BORROWINGS

	THE GROUP		THE COMPANY	
	2002 RMB'000	2001 RMB'000	2002 RMB'000	2001 RMB'000
The maturity of the bank borrowings is as follows:				
Within one year	188,800	130,200	188,800	130,000
More than one year but not exceeding two years	3,000	29,800	—	29,800
More than two years but not exceeding five years	—	—	—	—
	191,800	160,000	188,800	159,800
Less: Amount due within one year shown under current liabilities	(188,800)	(130,200)	(188,800)	(130,000)
Amount due after one year	3,000	29,800	—	29,800
Analysed as:				
- secured	118,800	89,800	118,800	89,800
- unsecured	73,000	70,200	70,000	70,000
	191,800	160,000	188,800	159,800

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

26. DEFERRED GAIN

	THE GROUP AND THE COMPANY RMB'000
GROSS AMOUNT	
At 1st January, 2002 and 31st December, 2002	4,023
AMORTISED TO INCOME	
Amortised during the year and balance at 31st December, 2002	(201)
CARRYING AMOUNT	
At 31st December, 2002	3,822

The gain on disposal of certain buildings is deferred as the buildings are subsequently leased back by the Group. Such leases qualify as finance leases and the gain is deferred and amortised to income over the lease term of 20 years.

27. SHARE CAPITAL

	Registered, issued and fully paid 2002 & 2001 RMB'000
Ordinary shares of RMB1 each	
- A shares	180,007
- H shares	65,000
	245,007

Except for the currency in which dividends are paid and the restrictions as to whether the shareholders can be PRC investors or foreign investors, A shares and H shares rank pari passu in all material respects with each other.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

28. RESERVES

	Share premium RMB'000	Capital reserve RMB'000	Statutory surplus reserve RMB'000	Statutory public welfare fund RMB'000	Accumulated losses RMB'000	Total RMB'000
THE GROUP						
At 1st January, 2001	293,745	10,225	8,406	8,406	(66,349)	254,433
Net profit for the year	—	—	—	—	8,236	8,236
At 31st December, 2001	293,745	10,225	8,406	8,406	(58,113)	262,669
Net profit for the year	—	—	—	—	6,726	6,726
At 31st December, 2002	293,745	10,225	8,406	8,406	(51,387)	269,395
THE COMPANY						
At 1st January, 2001	293,745	10,225	8,406	8,406	(66,349)	254,433
Net profit for the year	—	—	—	—	8,236	8,236
At 31st December, 2001	293,745	10,225	8,406	8,406	(58,113)	262,669
Net profit for the year	—	—	—	—	4,119	4,119
At 31st December, 2002	293,745	10,225	8,406	8,406	(53,994)	266,788

The balance of capital reserve represents the profit of Kunming Machine Tool Plant (a stated-owned enterprise before the reorganisation in 1993) for the period from 1st July, 1993 to 18th October, 1993 less an amount of RMB7,000,000 which the Company paid in cash to Yunnan Provincial People's Government pursuant to a demerger agreement dated 20th November, 1993 between Kun Ji Group Company and the Company.

The balance of statutory surplus reserve represents appropriations from profit after taxation in accordance with the PRC Company Law. Statutory surplus reserve is part of the shareholders' equity and when its balance reaches an amount equal to 50% of the Company's registered capital, further appropriation need not be made. According to PRC Company Law, the statutory surplus reserve may be used to make up past losses, to increase production and business operations or to increase capital by means of conversion. However, when funds from the statutory surplus reserve are converted to capital, the funds remaining in such reserve shall amount to not less than 25% of the registered capital.

According to Article 66 of Accounting Standards for Industrial Enterprises issued by the Finance Department of the PRC, the statutory public welfare fund is principally used for expenditure on staff welfare facilities. The statutory public welfare fund cannot be used for the payment of staff welfare expenses.

No profit is available for distribution as the Company had accumulated losses of RMB60,322,000 in accordance with the PRC accounting standards as at 31st December, 2002 (2001: RMB66,400,000).

29. OTHER LONG-TERM LOANS

The amounts are unsecured and non-interest bearing. These amounts will not be demanded within the next twelve months from the balance sheet date and the amounts are therefore shown in the balance sheet as non-current.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

30. ASSETS RESTRUCTURING TRANSACTIONS

In 2001, the Company acquired two subsidiaries and certain businesses together with their related assets and liabilities from Xian Jiaotong University Industrial (Group) Incorporation ("Jiaotong Group") and several individuals (collectively the "Acquired Businesses"). The Company also disposed of certain assets, comprising principally land use rights, buildings and inventories to Yunnan Provincial People's Government ("Yunnan Government"), the substantial shareholder of the Company. These transactions were collectively referred to as assets restructuring transactions. An agreement was entered into amongst all the relevant parties involved to settle the payment of the assets restructuring transactions by way of set-off of accounts (the "Settlement Agreement"). Details of the assets and liabilities involved were as follows:

	THE GROUP	
	2002 RMB'000	2001 RMB'000
Net assets acquired:		
Property, plant and equipment	—	24,456
Intangible assets	—	39,444
Inventories	—	13,019
Trade receivables	—	10,002
Other receivables	—	12,265
Tax recoverable	—	126
Bank balances and cash	—	5,212
Trade payables	—	(6,299)
Other payables	—	(19,050)
Amount due to a shareholder	—	(12,800)
Bank borrowings	—	(200)
Taxation payable	—	(969)
Obligations under finance leases	—	(642)
Minority interests	—	(2,175)
	—	62,389
Goodwill arising on acquisition	—	24,430
Consideration on acquisition	—	86,819
	THE GROUP	
	2002 RMB'000	2001 RMB'000
Net assets disposed of:		
Inventories	—	46,986
Land use rights and buildings	—	24,566
Deferred income on disposal of buildings	—	4,023
Business tax payable on disposal of land use rights and buildings	—	2,706
VAT payable on disposal of inventories	—	5,442
	—	83,723
Net gain arising from assets restructuring	—	7,858
Consideration for disposals	—	91,581
Net consideration receivable	—	4,762
Satisfied by:		
Amount due from a shareholder	—	4,762

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

30. ASSETS RESTRUCTURING TRANSACTIONS *(Continued)*

Analysis of the inflow of cash and cash equivalents in respect of the assets restructuring transactions:

	2002 RMB'000	2001 RMB'000
Bank balances and cash acquired	—	5,212

31. MAJOR NON-CASH TRANSACTIONS

During the year ended 31st December, 2001, the major non-cash transactions were as follows:

- (a) The Group entered into finance leases for its use of certain buildings with a total capital value at the inception of these leases of RMB4,265,000.
- (b) The Settlement Agreement as set out in note 30.

32. OPERATING LEASE COMMITMENTS

At the balance sheet date, the Group and the Company had commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

	THE GROUP		THE COMPANY	
	2002 RMB'000	2001 RMB'000	2002 RMB'000	2001 RMB'000
Within one year	1,060	720	673	720
In second to fifth year inclusive	3,175	2,692	2,692	2,692
Over five years	9,424	10,097	9,424	10,097
	13,659	13,509	12,789	13,509

Operating lease payment represent rental payable by the Group for certain of its office properties, factories and staff quarters. Significant leases are negotiated for an average term of 20 years.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

33. CAPITAL COMMITMENTS

At the balance sheet date, the Group and the Company had the following capital commitments:

	THE GROUP		THE COMPANY	
	2002	2001	2002	2001
	RMB'000	RMB'000	RMB'000	RMB'000
Capital expenditure in respect of the acquisition of property, plant and equipment contracted for but not provided in the financial statements	10,419	5,489	9,977	4,670

In addition, the Company has authorised to make a further capital contribution of approximately RMB39,360,000 to increase the registered capital of certain non wholly-owned subsidiaries as approved by the Board of Directors in August 2002. In the opinion of the Directors, upon completion of the procedures for the increase in registered capital of these subsidiaries, an amount of RMB13,000,000 which was previously advanced to these subsidiaries during the year will be capitalised as the Company's additional capital contribution.

34. PLEDGE OF ASSETS

At the balance sheet date, the Group had pledged land and buildings having a net book value of approximately RMB79,855,000 (2001: RMB75,400,000) and pledged time deposits of RMB40,505,000 (2001: RMB31,818,000) to secure bank loans granted to the Group.

At the balance sheet date, the Company had pledged land and buildings having a net book value of approximately RMB79,855,000 (2001: RMB75,400,000) and pledged time deposits of RMB37,142,000 (2001: RMB31,818,000) to secure bank loans granted to the Company.

35. RETIREMENT BENEFIT SCHEME

The Group is a participant in a state-managed retirement benefits plan pursuant to which the Company pays a fixed percentage of its qualifying staff's wages as contribution to the plan. The Company's financial obligation under this plan is limited to the payment of the employer's contribution.

During the year, the contributions made by the Group relating to the arrangement were approximately RMB4,541,000 (2001: RMB4,096,000). There was no forfeited contribution for reduction in the Company's future contribution during the year.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

36. CONNECTED PARTIES AND RELATED PARTY TRANSACTIONS AND BALANCES

During the year, the Group had significant transactions with connected parties as defined in the Rules Governing the Listing of Securities on the Stock Exchange ("Listing Rules"). The transactions with these connected parties during the year and balances with them at the balance sheet date are as follows:

Name of company	Nature of transactions	THE GROUP	
		2002 RMB'000	2001 RMB'000
(I) CONNECTED PARTIES			
(A) TRANSACTIONS			
<i>Substantial shareholders of the Company:</i>			
Jiaotong Group (including its associates as defined by the Listing Rules, other than members of the Group)	Utility service fee paid to Jiaotong Group (note a)	557	—
	Interest expense paid to Jiaotong Group (note b)	408	—
	Sales of raw materials to Jiaotong Group (note c)	177	—
	Sales of machinery to Jiaotong Group (note d)	—	997
	Research and development expenditure paid to Jiaotong Group (note e)	550	—
	Acquisition of Acquired Businesses from Jiaotong Group (note f)	—	86,819
	Guarantees given by Jiaotong Group (note g)	10,000	200
Yunnan Government	Rental for land to Yunnan Government (note h)	408	—
	Rental for buildings to Yunnan Government (note h)	608	—
	Sales of assets to the Yunnan Government (note i)	—	91,581
	Interest expenses on obligations under finance lease paid to Yunnan Government (note j)	129	—
<i>Companies controlled by the substantial shareholders</i>			
Kun Ji Group Company ("Kunji") (including its associates as defined by the Listing Rules, other than members of the Group)	Sales of raw materials to Kunji (note c)	—	68
	Sales of finished goods to Kunji (note c)	671	—
	Sub-contracting fees received from Kunji (note c)	—	126
	Sub-contracting fees paid to Kunji (note c)	—	95
	Construction costs paid to Kunji (note c)	857	330
	Environmental charges paid to Kunji (note c)	1,044	—
	Sales commission to Kunji (note k)	—	59
	Sales through Kunji as agent (note k)	—	1,174
	Utility services income received from Kunji (note l)	611	192
	Transportation fee paid to Kunji (note l)	—	318
	Payment to Kunji for provision of social, education and medical services to the Company's employees (note l)	1,913	3,617
	Guarantees given by Kunji (note m)	40,000	40,000

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

36. CONNECTED PARTIES AND RELATED PARTY TRANSACTIONS AND BALANCES (Continued)

(B) BALANCES

Name of company	Nature of balances	THE GROUP		THE COMPANY	
		2002	2001	2002	2001
		RMB'000	RMB'000	RMB'000	RMB'000
Substantial shareholder of the Company					
Jiaotong Group	Balance due from (to) Jiaotong Group				
	- non-trade receivable (note n)	—	—	—	4,605
	- non-trade payable (note n)	(197)	(8,038)	—	—
Kunji	Balance due from Kunji				
	- trade receivable	28	—	28	—
Yunnan Government	Balance due to Yunnan Government				
	- non-trade payable (notes j and n)	(4,051)	(4,264)	(4,051)	(4,264)
(II) RELATED PARTIES, OTHER THAN CONNECTED PARTIES					
Associate:					
西安通大思源電器有限公司 (「通大思源」)	Balance due from通大思源				
	- non-trade receivable (note n)	400	—	—	—

Notes:

- The Company entered into an agreement with Jiaotong Group whereby Jiaotong Group provides certain housing facilities and utilities services to the subsidiaries at prices to be determined by reference to the State stipulated price for utility services. The agreement has a term of three years commencing 31st December, 2001. The aggregate consideration for the payment under this agreement is below HK\$1 million each year.
- Interest expense was determined with reference to the prevailing market interest rates.
- In the opinion of the Directors, these transactions were carried out at market price or, where no market price was available, at cost plus a percentage profit mark up, or determined and agreed by both parties.
- Sales of machinery were carried out at market prices or, where no market prices were available, at cost plus a percentage profit mark-up.
- Research and development expenditure was determined by terms agreed by both parties.
- The consideration for the acquisition of the "Acquired Businesses" was arrived at with reference to their net asset value per valuation reports prepared by PRC valuers. Details of these acquisitions were set out in a circular to shareholders dated 5th December, 2001.
- At 31st December, 2002, Jiaotong Group had given corporate guarantee of RMB10,000,000 (2001: RMB200,000) to a bank to secure bank loan granted to a subsidiary of the Group.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31ST DECEMBER, 2002

36. CONNECTED PARTIES AND RELATED PARTY TRANSACTIONS AND BALANCES *(Continued)*

- (h) Upon disposal of its land and buildings to Yunnan Government during the year ended 31st December, 2001, the Group entered into separate agreements to lease back certain land and buildings for its use for a term of 20 years. The annual rental for the first three years is approximately RMB408,000 per annum for the leaseback land and approximately RMB608,000 per annum for the leaseback buildings which were determined by reference to the prevailing market rates as certified by a professional valuer. The rental will be revised every three years based on market rates as certified by professional valuers. Details of these lease arrangement are set out in a circular to shareholders dated 5th December, 2001, as revised by a supplementary press announcement made by the Company on 25th February, 2002.
- (i) The consideration for the sale of the Company's assets to Yunnan Government was arrived at with reference to their book value per accounts prepared in accordance with PRC accounting principles and valuation reports prepared by PRC valuers. Details of the disposal were set out in a circular to shareholders dated 5th December, 2001.
- (j) Upon disposal of its land and buildings to Yunnan Government during the year ended 31st December, 2001, the Group entered into separate agreements with Yunnan Government to lease back certain land and buildings for a term of 20 years. The balance with Yunnan Government as the lessor of these arrangement are set out in note 24, obligations under finance leases. The relevant interest expenses on obligations under finance leases were determined with reference to the prevailing market rates.
- (k) On 15th November, 1993, the Company appointed Kunji as the Group's non-exclusive agent in the PRC. The commission was calculated with reference to the non-exclusive sale agency agreement entered into in 1993.
- (l) The receipt and payment of these service income and expenses were priced with reference to a composite service agreement entered into between Kunji and the Company in 1993.
- (m) At 31st December, 2002, Kunji had given corporate guarantee of RMB40,000,000 (2001: RMB40,000,000) to a bank to secure bank loan granted to the Company.
- (n) The balances are unsecured, interest-free and repayable on demand.

NOTES TO THE FINANCIAL STATEMENTS

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37. DIFFERENCES BETWEEN PRC ACCOUNTING STANDARDS ("PRC GAAP") AND HONG KONG ACCOUNTING STANDARDS ("HK GAAP") AS APPLICABLE TO THE GROUP

The major differences between the financial statements prepared under the PRC GAAP and HK GAAP are as follows:

Impact on the consolidated results

	2002 RMB'000	2001 RMB'000
Profit for the year as per financial statements prepared under the PRC GAAP	6,078	2,051
Unrealised holding gains on other investments recognised as income under HK GAAP in 2000	—	(396)
Interest subsidy from the PRC government recognised as income under HK GAAP only when the related interest expenses were incurred	1,312	1,688
Gain on sale and lease back transaction deferred under PRC GAAP but recognised as current year income under HK GAAP	—	8,288
Amortisation on deferred gain on sale and lease back transaction under PRC GAAP but recognised as income under HKGAAP in 2001	(664)	—
Impairment loss recognised in respect of property, plant and equipment charged directly to income under HK GAAP	—	(3,395)
Profit for the year as per financial statements prepared under the HK GAAP	6,726	8,236

Impact on the consolidated net assets as at 31st December

	2002 RMB'000	2001 RMB'000 (As restated)
Net assets as per financial statements prepared under the PRC GAAP	506,778	499,034
Interest subsidy from the PRC government recognised as income under HK GAAP only when the related interest expenses were incurred	—	(1,312)
Gain on sale and lease back transaction deferred and amortised under PRC GAAP but wholly recognised as income under HK GAAP when the transaction was entered into	7,624	8,288
Goodwill arising on acquisition of a net liability company dealt with directly in reserve under PRC GAAP but recognised as an intangible asset under HK GAAP	—	1,666
Net assets as per financial statements prepared under the HK GAAP	514,402	507,676

Note: There are also other differences in balance sheet items due to differences in classification between the PRC GAAP and the HK GAAP.