

## DIRECTORS' REPORT

### PRINCIPAL ACTIVITIES

The Group is principally engaged in the manufacture and sale of a wide range of zirconium chemicals.

### RESULTS AND APPROPRIATIONS

The results of the Group for the year ended 31 December 2003 are set out in the consolidated income statement on page 23.

The Board has recommended the payment of a final dividend of HK3.7 cents per ordinary share for year 2003.

In the event that the resolution on the proposed payment of the final dividend for ordinary share is passed at the annual general meeting to be held on 18 May 2004, such dividend will be paid on 27 May 2004 to shareholders whose names appear in the register of members of the Company on 18 May 2004.

The register of members of the Company will be closed from 14 May 2004 to 18 May 2004, both days inclusive, during which period no transfer of shares of the Company will be registered. In order to qualify for the proposed final dividend and to attend and vote at the Company's annual general meeting to be held on 18 May 2004, all transfer documents accompanied by the relevant share certificates must be lodged with the Company's Branch Registrar in Hong Kong, Tengis Limited, at G/F., Bank of East Asia Harbour View Centre, 56 Gloucester Road, Wanchai, Hong Kong for registration by no later than 4:30 p.m. on 13 May 2004.

### FINANCIAL SUMMARY

A summary of the results and the assets and liabilities of the Group for the last five financial years is set out on page 3.

### PROPERTY, PLANT AND EQUIPMENT

Details of movements in the property, plant and equipment of the Group and the Company during the year 2003 are set out in note 13 to the financial statements.

### SHARE CAPITAL

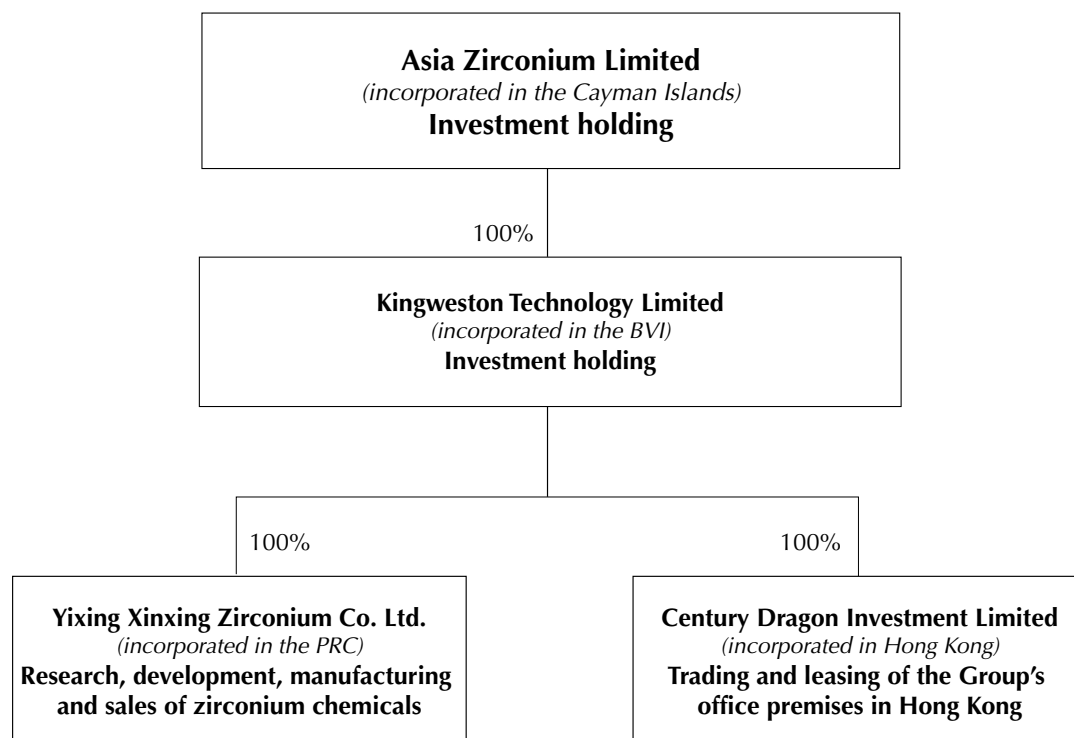
Details of movements in the share capital of the Company during the year 2003 are set out in note 24 to the financial statements.

### RESERVES

Details of movements in the reserves of the Group and the Company during the year 2003 are set out in consolidated statement of changes in equity on pages 26 to 27.

## Directors' Report (cont'd)

## GROUP STRUCTURE



## DIRECTORS

The Directors at the date of this report are shown below. Their biographies are set out on pages 18 to 19.

| Name            | Position                           | Term of office   |
|-----------------|------------------------------------|--|
| Yang Xin Min    | Chairman, Managing Director        | Since 17 September 2000                                |
| Yang Zhen       | Executive Director                 | Since 17 September 2000<br>(resigned on 15 April 2003) |
| Huang Yue Qin   | Executive Director                 | Since 17 September 2000                                |
| Zhou Quan       | Executive Director                 | Since 1 April 2003                                     |
| Guo Lu Cun      | Executive Director                 | Since 1 January 2002<br>(resigned on 1 January 2004)   |
| Li Fu Ping      | Executive Director                 | (Appointed on 9 January 2004)                          |
| Sik Siu Kwan    | Non-executive Director             | Since 2 March 2002<br>(resigned on 17 March 2003)      |
| Cheng Faat Ting | Independent Non-executive Director | Since 16 November 2001                                 |
| Guo Jing Mao    | Independent Non-executive Director | Since 26 October 2000                                  |

Each of the above Directors has entered into a service contract with the Company for an initial term of three years. Each service contract will continue thereafter unless terminated by either party thereto giving to the other at least three months' notice in writing.

## Directors' Report (cont'd)

**DIRECTORS' INTERESTS IN SECURITIES**

As at the date of this report, the interests of the Directors and chief executive of the Company in the equity or debt securities and underlying Shares of the Company or any associated corporations (within the meaning of the Securities and Futures Ordinance ("SFO")) which (a) were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which the Director is taken or deemed to have under such provisions of the SFO); or (b) were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein; or (c) were required, pursuant to the Model Code for Securities Transactions by Directors of Listed Companies to be notified to the Company and the Stock Exchange were as follows:

| Name of Director | Capacity   | Nature of interest | Number of Shares   | Issued share capital of the Company % |
|------------------|------------|--------------------|--------------------|---------------------------------------|
| Yang Xin Min     | Beneficial | Personal           | 320,970,946 Shares | 63.92                                 |

**SUBSTANTIAL SHAREHOLDERS' INTERESTS IN SECURITIES**

As at the date of this report, so far as was known to the Directors and the chief executive of the Company, the following persons, other than a Director or chief executive of the Company, had an interest or short position in the Shares and underlying Shares which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or who were, directly or indirectly, interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of the Company or any other member of the Group.

| Name of Shareholder    | Number of Shares   | Issued share capital of the Company % |
|------------------------|--------------------|---------------------------------------|
| Yang Xin Min           | 320,970,946 Shares | 63.92                                 |
| Value Partners Limited | 47,000,000 Shares  | 9.36                                  |

**DIRECTORS' INTERESTS IN COMPETING BUSINESS**

None of the Directors had any interest, either direct or indirect, in any business, which may compete or constitute a competition with the business of the Group.

**DIRECTORS' INTERESTS IN CONTRACTS**

None of the Directors of the Company had a material interest, either direct or indirect, in any significant contract to which the Company or its holding companies or any of its subsidiaries was a party at the year end of or during the year 2003.

At no time during the year was the Company or any of its subsidiaries, a party to any arrangements to enable the Directors of the Company to acquire benefits by means of the acquisition of shares or debentures of the Company or any other body corporate.

## Directors' Report (cont'd)

**SHARE OPTIONS GRANTED PURSUANT TO THE SHARE OPTION SCHEME**

Pursuant to the written resolution by the shareholders of the Company on 24 September 2002, the Share Option Scheme (the "Scheme") was approved and adopted and, the Board may, at its discretion, grant options (the "Options") to any Director (whether executive or non-executive and whether independent or not), any employee (whether full-time or part-time), any consultant or adviser of or to the Company or the Group (whether on an employment or contractual or honorary basis and whether paid or unpaid) (the "Eligible Persons"). The Scheme will expire on 23 September 2012.

As at 31 December 2003, Options to subscribe for a total of 2,000,000 shares of the Company have been granted pursuant to the Scheme, representing 0.5% of the Company's shares in issue as at the date of grant. No Options have been exercised during the year.

Details of the movement of the Options granted during the year were as follows:

| Name of Employee     | Date of Grant   | Exercise Period                         | Subscription Price per Share | Number of share options            |                         |                           | Outstanding as at 30 March 2004 |
|----------------------|-----------------|---|------------------------------|------------------------------------|-------------------------|---------------------------|---------------------------------|
|                      |                 |   |                              | Outstanding as at 31 December 2003 | Granted during the Year | Exercised during the Year |                                 |
| Wong Hoi Yan, Audrey | 1 November 2002 | 1 May 2003 to 30 April 2008<br>(Note 4) | HK\$0.87                     | 2,000,000                          | 2,000,000               | —                         | 2,000,000                       |

*Note 4:* The Options will vest in five tranches in the grantee at a 20%: 20%: 20%: 20%: 20% ratio. The first tranche of the Options will vest in the grantee on 1 May 2003. The second, third, fourth and fifth tranches will vest in the grantee on 1 May 2004, 1 May 2005, 1 May 2006 and 1 May, 2007 respectively.

**CONNECTED TRANSACTIONS**

The following connected transactions have been carried out by the Group during year 2003:

**Trademark**

Pursuant to the trademark licensing agreement dated 12th July 2000 entered into between Jiangsu Xinxing Chemicals Group Corp. ("Xinxing Chemicals Group") and Yixing Xinxing Zirconium Co. Limited ("Yixing Zirconium"), Xinxing Chemicals Group has agreed to grant an exclusive license to Yixing Zirconium or the Group to use the "Long Jing" trademarks in the PRC, the USA and Japan respectively, during their respective legally valid periods at nil consideration. Xinxing Chemicals Group is beneficially owned by Mr. Yang Xin Min, and Yixing Zirconium is a wholly-owned subsidiary of the Company. Accordingly, the transactions contemplated under the trademark licensing agreement constitutes a connected transaction pursuant to the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules") upon the listing of the shares of the Company on the Stock Exchange.

This transaction falls within the de minimis provision under Rule 14.24(5) of the Listing Rules. Accordingly, upon the listing of the Company's shares on the Stock Exchange, the trademark licensing agreement will not be subject to disclosure or shareholders' approval requirements.

## Directors' Report (cont'd)

**CONNECTED TRANSACTIONS (Cont'd)****Supply of power and steam**

Xinxing Chemicals Group (as supplier) and Yixing Zirconium (as purchaser) have entered into the supply agreement dated 1 September 2000 and the two supplemental agreements thereto dated 16 September 2000 and 21 March 2002, respectively ("the Agreements"), pursuant to which Xinxing Chemicals Group agreed, inter alia, to provide electricity and steam (which is owned by Xinxing Chemicals Group) to Yixing Zirconium for the normal operation of Yixing Zirconium's production facilities for a term of 15 years commencing from 1st January 2001 to 31st December 2015. The directors expect that the power and steam annual expenses will not exceed 10% of the Group's total turnover in each financial year. The transactions contemplated under the Agreements constitute ongoing connected transactions pursuant to the Listing Rules upon the listing of the shares of the Company on the Stock Exchange.



Save as disclosed above, no other transactions were required to be disclosed as connected transactions pursuant to the Listing Rules. No Directors, directly or indirectly, had any material interests in any significant contracts entered into between the Company, the ultimate holding company or any subsidiaries of the ultimate holding company during the year.

Upon the listing of the shares of the Company on the Stock Exchange, the transactions contemplated under the Agreements constitute ongoing connected transactions of the Company pursuant to the Listing Rules. The Company has applied for a waiver from strict compliance of the transactions contemplated under the Agreements with the related provisions of the Listing Rules for the three years ended 31 December 2004, on the basis that the Company undertakes to strictly abide by the following terms and conditions, and the waiver has been granted by the Stock Exchange.

The Company's independent non-executive directors and auditors have reviewed the ongoing connected transactions as set out above and confirm that:

- the transactions have been entered into in the ordinary and usual course of the business of the Group;
- the transactions have been conducted on normal commercial terms and agree after arm's length negotiations, and in accordance with the terms of the relevant Agreements or on terms no less favourable than terms available to independent third parties;
- the transactions have been conducted in accordance with the relevant agreements on terms that are fair and reasonable so far as the shareholders of the Company are concerned and in the interest of the Company as a whole; and
- the transactions entered into during the year do not exceed, in aggregate, 10% of the Company's aggregate turnover in year 2003.

The power and steam generating plant has been acquired by the Company and this connected transaction was ceased on the approval of such acquisition at the extraordinary general meeting held on 29 March 2004.

Directors' Report (cont'd)

## USE OF PROCEEDS

As stated in the prospectus of the Company dated 17 October 2002, the proceeds would be used for the expansion of production lines. Such lines were in operation accordingly at the end of 2003.

## MAJOR CUSTOMERS AND SUPPLIERS

For the year ended 31 December 2003, the aggregate turnover attributable to the largest customer and the five largest customers of the Group accounted for approximately 18% and 58% of the Group's total turnover for the year respectively; and the aggregate purchases from the largest and the five largest suppliers of the Group accounted for approximately 37% and 75% of the Group's total purchases in the corresponding year respectively.

As far as the directors are aware, none of the directors of the Company, their respective associates (as defined in the Listing Rules), and the existing shareholders of the Company who own more than 5% of the Company's issued share capital, had any interests in the Group's five largest customers or suppliers at any time during the year 2003.

## RESPONSIBILITY OF DIRECTORS ON FINANCIAL STATEMENTS

The Companies Ordinance requires the Directors to prepare financial statements for each financial year. Such financial statements should give a true and fair view of the state of affairs of the Company and of the Group as at the balance sheet date of a particular year and on the profit and loss of the Company and the Group for the year then ended. In preparing the financial statements, the Directors should:

- (a) select and apply consistently appropriate accounting policies, make prudent, fair and reasonable judgement and estimation;
- (b) report the reasons for any seriously deviation from accounting practice; and
- (c) prepare the financial statements on going concern basis, unless it is inappropriate to assume the Company and the Group could continue to operate;

The Directors are responsible for the proper keeping of accounting record in order to secure assets of the Company and the Group. The Directors are also responsible for adopting reasonable measures to prevent and check any fraudulences and irregularities.

## CORPORATE GOVERNANCE

### Code of Best Practice

The Code of Best Practice as set out in Appendix 14 of the Listing Rules has been complied with by the Company throughout the year 2003.

### Audit Committee

The Company set up an Audit Committee on 24 September 2002 with its written terms of reference being in compliance with Rules set out in "A Guide for the Formation of An Audit Committee" issued by Hong Kong Society of Accountants.

The primary duties of the Audit Committee are to review and supervise the financial reporting process and internal control systems of the Group. The Audit Committee comprises two independent non-executive directors, namely Mr. Gary Cheng Faat Ting and Mr. Guo Jing Mao, with Mr. Gary Cheng Faat Ting being Chairman of the Audit Committee.

## Directors' Report (cont'd)

**CORPORATE GOVERNANCE (Cont'd)****Donations**

For the year ended 31 December 2003, the Group did not make any donations.

**PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES**

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities during the year 2003.

**PRE-EMPTIVE RIGHTS**

There is no provision for pre-emptive rights under the Company's articles of association or the laws of the Cayman Islands, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

**POST BALANCE SHEET DATE EVENT**

The following events took place subsequent to 31 December 2003:

- (i) Pursuant to a placing agreement dated 3 February 2004 entered into between Mr. Yang Xin Min ("Mr. Yang"), a substantial shareholder of the Company, and a placing agent, 47,000,000 existing ordinary shares of HK\$0.1 each in the Company were placed to independent investors at a price of HK\$1.17 per share. Upon completion of the placement of shares and pursuant to a subscription agreement entered into between the Company and Mr. Yang, Mr. Yang subscribed for 47,000,000 new ordinary shares of HK\$0.1 each in the Company at a price of HK\$1.17 per share. The net proceeds of the subscription were intended to be used as general working capital for the Group.
- (ii) On 13 February 2004, Yixing Zirconium, a wholly-owned subsidiary of the Group, entered into an acquisition agreement (the "Agreement") with Jiangsu Xinxing Chemicals Group Corporation ("Xinxing Chemicals Group"), a private-owned enterprise wholly owned by Mr. Yang Xin Min, a substantial shareholder and director of the Company. Pursuant to the Agreement, Yixing Zirconium has agreed to acquire the electricity and steam generating plant and related facilities from Xinxing Chemicals Group at the consideration of approximately RMB77,880,000, which will be satisfied by the issue of the 55,170,946 ordinary shares of the Company to Mr. Yang Xin Min. The directors believe that the acquisition will reduce production cost, ensure stable and continuous electricity and steam supply, thus enhancing the Group's earning capacity in the long run. Details of the acquisition contemplated under the Agreement are set out in the Group's press announcement dated 17 February 2004.

**AUDITORS**

A resolution for the re-appointment of RSM Nelson Wheeler as the Company's auditors for 2004 is to be proposed at the forth coming annual general meeting.

By order of the Board

**Huang Yue Qin**

*Executive Director*

30 March 2004