

REPORT OF THE BOARD OF DIRECTORS

The Board of Directors are pleased to submit its report together with the audited financial statements for the year ended 31 December 2004 to the shareholders.

(I). DISCUSSION AND ANALYSIS TO OPERATIONS DURING THE PERIOD UNDER REVIEW

Result

In the financial statements prepared in accordance with PRC Accounting Rules and Regulations for the year ended 31st December 2004, the principal operating income of the Group amounted to RMB2,363.4 million, representing a decrease of 16.79% over that of last year. The audited consolidated net profit after taxation and minority interest amounted to RMB33.67million representing a decrease of 21.78% over that of last year. The earnings per share and that after deduction of exceptional items was RMB0.07 and RMB0.07 respectively, representing a decreases of 22.22% and 3.77% respectively.

In the financial statements prepared in accordance with accounting principles generally accepted in Hong Kong for the year ended 31st December 2004, the turnover of the Group amounted to RMB2,363.40 million , representing a decrease of 16.79% over that of last year. The profit attributable to shareholders after taxation and minority interest amounted to RMB60.95 million, representing an increase of 148.20% over that of last year. The earnings per share was RMB0.1232.

In 2004, affected by the sustained price rising of steel products and the appreciation in value of Euro, the Company was faced with huge challenge in shipbuilding and other business. The Company insisted on the policy of "strengthen the core competence in shipbuilding, vivify the development in non-shipbuilding operations", and focused on the improvement in the quality and benefit of business and marketing, advanced production efficiency, shorten shipbuilding cycle and improved economic benefit through changing shipbuilding mode, strengthen cost controlling and management. Besides, the Company enhanced its risk defence consciousness and avoided exchange rate risk reasonably.

In 2004, the turnover of the Group was decreased compared with that of last year due to the discontinuance of container manufacturing business. The gross profit of the Group increased by 35.24% compared with that of last year, this is mainly due to the Company's strengthening work in cost control to shipbuilding and the adjustment of shipbuilding products structure, which resulted in a decrease of construction proportion of domestic ocean-going vessels.

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Major operation information divided into products

Unit: RMB

Products	Turnover	Proportion in total turnover(%)	Profit from major operations	Proportion in total profit from major operations (%)
Shipbuilding	2,105,612	89.09	68,477	57.73
Container manufacturing	1,133	0.05	333	0.28
Steel structure	140,962	5.96	12,802	10.79
Electrical & mechanical products and others	100,444	4.25	33,862	28.55
Ship repairing	15,252	0.65	3,141	2.65
Including: connected transactions	12,949	0.55	5,050	0.21
Total	2,363,403	100	118,614	100

During the period under review, the connected transactions that the Company sold products to CSSC and its subsidiaries amounted to RMB21,261,246.40.

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PRINCIPAL OPERATIONS



Shipbuilding

In the year 2004, the Group completed and delivered 10 vessels including three 35,000dwt product oil tankers for a Danish customer, three 38,000dwt product oil tankers for a Malta customer, and two 40,000dwt product oil tankers, a 3000 ton oil tanker and a large size auxiliary ship for domestic customers. The total completed tonnage amounted to 315,500dwt.

Moreover, there were 15 vessels commenced construction work, and 12 vessels launched in 2004. These vessels included, 35,000dwt product oil tankers for a Danish customer, 38,000dwt product oil tankers for a Malta customer, 40,000dwt product oil tankers, 3000t patrol ship and 3000t oil tankers for domestic customers.

The turnover from shipbuilding amounted to RMB2,105.61 million which represented an decrease of 0.58% over that of last year. The turnover attributable to shipbuilding represents 89.09% of the Group's turnover, the gross profit of shipbuilding products accounted to RMB68.48 million, and the gross profit rate accounted to 3.25%. In 2004, the Group took the opportunity of the flourishing shipbuilding market and secured new orders for 15 vessels, with a total tonnage of 456,800dwt. As at 31 December 2004, the Group has secured orders for 34 vessels with a total tonnage of 1,060,000dwt and a total contract value of RMB7.062 billion (RMB5.725 billion upon deducting those booked in the 2004 financial accounts in accordance with the ships process percentage).



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Ship repairing



In 2004, ship repairing operation of the Group was reduced compared with that of last year due to restriction of the geographical environment and the adjustment of product structure. The repairing services for 14 vessels with various types were completed including 4 foreign vessels. The turnover from the ship repairing operation amounted to RMB15.25 million, the turnover attributable to the ship repairing operation represents 0.65% of the Group's turnover, and its gross profit amounted to RMB3.14 million with gross profit rate of 20.59%.

Steel structure

In 2004, the steel structure completed by the Group amounted to 14,353 ton, which were reduced due to the price competition and higher cost. The turnover contributed from the steel structure operation amounted to RMB140.96 million and its gross loss amounted to RMB12.80 million with gross profit rate of 9.08. The turnover attributable to the steel structure operation represents 5.96% of the Group's turnover.



Mechanical and electrical equipment and other operations



The mechanical and electrical equipment operations of the Group including Hydraulic Bending Machine, Hydraulic Shearing Machine, Ship Elevator, Refrigerator Processing Equipments, various Elevators Manufacture and Installation and maintenance and alternation of hydrofoil of hovercraft. In 2004, the turnover from the mechanical and electrical equipment amounted to RMB100.44 million, the gross profit amounted to RMB33.86 million with gross profit rates of 33.71%. The turnover attributable to mechanical and electrical and other operations represents 4.25% of the Group's turnover.

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Geographical analysis of turnover

Countries or Regions	Proportion in total		Proportion in total	
	Principal operation income (RMB'000)	Principal operation income (%)	Principal operation profit (RMB'000)	Principal operation profit (%)
Malta	343,030,776.80	14.51	34,553,812.32	29.13
Denmark	1,197,260,301.32	50.66	22,567,180.12	19.03
Macau	675,709.56	0.03	161,165.40	0.14
The Philippines	2,595,952.57	0.11	111,740.31	0.09
USA	85,297.60	0.00	-30,164.17	-0.03
Hong Kong	17,758,804.82	0.75	3,248,698.18	2.74
Subtotal	1,561,406,842.67	66.07	60,612,432.16	51.10
Mainland China	801,995,907.85	33.93	58,002,044.67	48.90
Total	2,363,402,750.52	100.00	118,614,476.83	100.00

Major product and its marketing occupancy

During the period under review, the major product of the Company is handy size tanker, with its occupancy of 11% in the international market.

Major product whose turnover or profit representing more than 10% of the total amount

Unit: RMB

Product	Principal operating income	Principal operating cost	Gross profit(%)
Shipbuilding	2,105,611,528.25	2,037,134,355.79	3.25
Steel Structure	140,961,939.86	128,159,600.15	9.08
Electrical and Mechanical Products and others	100,444,374.78	66,582,598.26	33.71

Turnover from export operation

During the year, the Group's turnover attributable to exports amounted to US\$188.66 million (2003: US\$191.16 million).

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Major customers and suppliers

In 2004, the turnover from the Group's five largest customers amounted to RMB1,965.26 million and accounted for 83.15% of the turnover of the Group.

The purchase of raw materials and equipment from the Group's five largest suppliers amounted to RMB648.90 million and accounted for 16.47% of the total purchases of the Group in 2004.

Except for Zhenjiang CSSC Equipment Co., Ltd. Zhengjiang Marine Diesel Factory, one of the five largest suppliers of the Company in 2004, is a subsidiary of CSSC, the controlling holder of the Company, none of the directors, supervisors and their respective associates had any interests in the major customers and suppliers noted above, nor had any of the Company's shareholders disclosed to the Company that he or she had an interest in the above mentioned major customers or suppliers.

Major subsidiaries

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

No	Company Name	Principal Activities	Registered Capital <i>RMB'000</i>	Interest Attributable to the Company (%)	Assets <i>RMB'000</i>	Net profit (loss) <i>RMB'000</i>
Direct holding subsidiaries						
1	Guangdong Guangzhou Shipyard International Elevator Company Limited	Elevator production and sales	21,000	95	35,720	-361
2	Guangzhou Hongfan Information Technique Company Limited	Development of computer software, system integration and sales of hardware	5,000	77	6,660	508
3	Guangzhou Xinsun Shipping Service Company Limited	Welding and coating of ships	2,000	83	15,697	-3,895
4	Masterwood Company Limited	Furniture manufacturing	3,315	51	7,631	219
5	Guangzhou Guanglian Container Transportation Company Limited	Container transportation	20,000	75	21,058	76
6	Xinhui City Nanyang Shipping Industrial Company	Ship dismantling	34,800	70	21,736	-3,580
7	United Steel Structures Limited	Large-sized steel structure	73,573	51	98,205	2,296
8	Rongguang Developing Co., Ltd.	Trading	HKD 10,000	100	30,058	131

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No	Company Name	Principal Activities	Registered Capital <i>RMB'000</i>	Interest Attributable to the Company (%)	Assets <i>RMB'000</i>	Net profit (loss) <i>RMB'000</i>
Indirect holding subsidiaries						
9	Masterwood Company Limited	Furniture manufacturing	3,315	25	7,631	219
10	Guangzhou Hongfan Hotel	Traveling and catering services	10,000	86.16	5,073	268
11	Guangdong Guangzhou Elevator Shipyard International Company Limited	Elevator production and sales	21,000	3.8	35,720	-361
12	Fonkwang Development Ltd.	General trade	HKD 200,000	70	6,228	450

Except for Rongguang Development Co., Ltd. and Fonkwang Development Ltd. were registered in Hong Kong, other above-mentioned subsidiaries are established and operated in Mainland China.

Problems and difficulties of operation and their solutions

During the period under review, the Company met problems and difficulties principally in respect of the increase in exchange rate risk, prices fluctuate and supply of raw materials, and the shortage of power supply.

In order to solve the problem of the increase in exchange rate risk, the Company established exchange rate risk leader party, appointed finance institution to assist the analysis of changes of the market exchange rate, and determined to timely adopt appropriate measure, such as adjusting payment receiving structure of new orders, optimising debts structure, locking exchange rate and fixing cost with other measure, to decrease the risk of exchange rate fluctuate.

To solve the problem of the prices fluctuate and supply of raw materials, the Company signed a long-term supply agreement with major material suppliers to establish strategic purchasing relation, and executed ordering goods in advance to ensure the normal supply and reduce the effect of prices fluctuate.

Apart from those, the Company adjusted the working days and hours to cope with the temporary shortage of power supply.

Application of proceeds from share offering

The Company had not raised funds during the year nor utilized any proceeds previously raised.

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Application of other capital

During the year, the investment capital not from share offering of Company amounted to RMB35.79 million, decreased by RMB28.1 million and representing a decrease of 44.06% compared with that of last year. The major invested projects including: the construction of technical centre building, purchasing movable air compressor, reforming of shipbuilding assembly yard, and purchasing system software for Tribon Working Station.

Financial position of the Group during 2004

RMB'000

Item	Closing balance	Opening balance	Increase/ decrease (+/-)	Change ratio (%)
Total assets	2,213,066,567.01	2,513,408,415.37	-300,341,848.36	-11.95
Principal operating profit	116,660,476.17	84,376,007.42	32,284,468.75	38.26
Net profit	33,672,983.77	43,051,774.75	-9,378,790.98	-21.78
Net increase in cash and cash equivalents	-13,834,823.29	106,686,651.68	-120,521,474.97	-112.97
Shareholders' equity	710,262,688.89	676,589,705.12	33,672,983.77	4.98

Responsibility ascertainment and treatment to relevant person for significant loss in assets

During the period under review, the Company had not happened any significant loss in assets.

Prospects for the coming year

In the coming year, the principal operation shipbuilding resumed continuous and balanced production, and the ships constructed in 2005, which were signed in 2003, have higher prices compared with those constructed in 2004. But the Group still faces huge pressure of cost control resulted from price rising of steel, raw materials and equipments, and the non-operating risk in term of fluctuation of exchange rates.

Being faced with such situation, the Group will still insist in the policy of "strengthen the core competence in shipbuilding, vivify the development in non-shipbuilding operations", enhance statistics and analyses on shipbuilding basic data for the realization of meticulous management; continue to change shipbuilding mode, realize the mode changing works' improvement from the aspect of technical to management; strengthen and consummate cost management, increase shipbuilding production efficiency constantly; carry out active and reliable measure and normative action, to avoid exchange ratio risk and improve the ability in risk defence; enhance shipbuilding technology development to further achieve the strategy development scheme, exert ourselves to further develop the shipbuilding business in the year 2005.

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(II). REPORT OF THE DAILY OPERATIONS OF THE BOARD OF DIRECTORS

Meetings and resolutions of the Board of Directors

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

1. The twelfth meeting of the fourth term of the Board of the Company was held at the reception room of the Company on 6th February 2004. All the eleven directors with a proxy of the fourth term of the Board of Directors attended the meeting. The resolutions passed at the meeting are as follows: (1) Approved the proposal of establishing Emolument and Examination Committee, and submit it to the general meeting for approval. (2) Approved the implementing rules for Emolument and Examination Committee. (3) Approved the proposal of establishing Nomination Committee, and submit it to the general meeting for approval. (4) Approved the implementing rules for Nomination Committee. (5) Approved the implementing rules for Audit Committee. (6) Approved the implementing rules for Strategy Committee. (7) Approved the proposal of revising several items of the Articles of Association of the Company, and submit it to the general meeting for approval. (8) Approved the amended Inner Control System for Connected Transactions. (9) Approved the amended Managerial System for Information Disclosing. (10) Approved and stipulated the audit fee of domestic and international auditors of the Company for the year of 2003 with amount of RMB420,000 and HKD1,180,000 respectively. (11) Approved the proposal of holding extraordinary general meeting on 26th March 2004.
2. The thirteenth meeting of the fourth term of the Board of the Company was held at the reception room of the Company on 16th April 2004. All the eleven directors with three proxies of the fourth term of the Board of Directors attended the meeting. The resolutions passed at the meeting are as follows: (1) Approved the business report of the president for the year 2003. (2) Approval of loss provision in the amount of RMB5.91 million and RMB7.65 million for the No.15 and No.16 vessel of 35000dwt product tankers respectively. (3) Approved the decision of exiting from container manufacturing business by the Company. (4) Approved to write off after verification an aggregate amount of RMB9,007,897.57 in respect of preliminary development expenses incurred for the re-location of the container factory for environmental reasons. (5) Approved to write off after verification provision for diminution in value of fixed assets of the container factory in the aggregate amount of RMB18,539,764.31. (6) Approved the annual report and its summary for the year 2003. (7) Approved the 2003 profit distribution proposal of neither distribution nor capital increment and submission of the same to the shareholders' general meeting for consideration. (8) Approved the first quarterly report for the year 2004. (9) Approved to authorize the executive directors of the Company to execute the relevant loan agreements (including but not limited to loan agreements, debt confirmations, mortgages, credit agreements, counter-guarantees in respect of loan guarantees and other related legal documents) with an aggregate loan amount of not exceeding RMB1.05 billion for the year 2004. (10) The Framework Agreement for Continuing Connected Transactions between CSSC and the Company was discussed at the meeting, 7 related directors of the Company abstained from voting and 4 independent non-executive directors of the Company all voted for the proposal. But in accordance with the Company Law, the proposal was not passed at the meeting and should be submitted to general meeting for consideration. (11) Approved to award the executive directors,

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internal supervisors and senior management of the Company with an aggregate amount of RMB566,930 for the year 2003. (12) Approved the appointment of Mr. Yu Baoshan as vice chairman of the Board of Directors. (13) Approved the resignation of Mr. Ye Peihua, Mr. Xu Guoqing and Ms. An Xiaofei as directors of the Company for work reason, and submit it to general meeting for consideration. (14) Approved the nomination of Mr. Han Guangde, Mr. Zhongjian and Mr. Wang Yi as candidates of directors of the Company, and the submission of the nomination to general meeting for consideration. (15) Approved the resignation of Mr. Yu Baoshan as president due to job relocation, and Mr. Ye Peihua, Mr. Zhong Jian and Mr. Yin Xueming as vice presidents. (16) Approved the appointment of Mr. Han Guangde, Mr. Chen Ji and Mr. Zeng Xiangxin as president, vice president and chief accountant of the Company respectively. (17) Approved the appointment of Ms. Yang Ping as securities affairs representative of the Company. (18) Approved the amendment of certain clauses of Articles of Association of the Company in accordance with the Listing Rules of The Stock Exchange of Hong Kong Limited as recently amended, and submission of the amendments to general meeting for consideration. (19) Approved the reappointment of Guangdong Yangcheng Certified Public Accountants Company Limited and PricewaterhouseCoopers Certified Public Accountants as domestic and international auditors respectively for the year 2004, and submission of the matter to general meeting for consideration. (20) Approved to hold the 2003 Annual General Meeting on 25th June 2004.

3. The fourteenth meeting of the fourth term of the Board of the Company was held on 28th April, 2004, all eleven directors voted by means of written resolution for approval the proposal of the basic wage or remuneration of the director candidates and supervisor candidates, and submit it to the general meeting for consideration.
4. The fifteenth meeting of the fourth term of the Board of the Company was held at the reception room of the Company on 25th June 2004. All the eleven directors with a proxy of the fourth term of the Board of Directors attended the meeting. The resolutions passed at the meeting are as follows: (1) Approved the appointment of three directors, namely, Mr. Wu Fabo, Mr. David Hon To, Yu and Mr. Miao Jian as members of the Audit Committee. (2) Approved the appointment of five directors, namely, Mr. Hu Guoliang, Mr. Han Guangde, Mr. Wang Yi, Mr. Zhong Jiang and Mr. Li Junfeng as members of the Strategy Committee. (3) Approved the appointment of three directors, namely, Mr. Bu Miaojin, Mr. Wu Fabo and Mr. Yu Baoshan as members of the Emolument and Examination Committee. (4) Approved the appointment of three directors, namely, Mr. Bu Miaojin, Mr. Philip Pat Yiu, Yuen and Mr. Zhong Jian as members of the Nomination Committee. (5) Approved the management system regulating the relationship between the Company and its investors.
5. The sixteenth meeting of the fourth term of the Board of the Company was held at the reception room of the Company on 13th August 2004. All the eleven directors with two proxies of the fourth term of the Board of Directors attended the meeting. The resolutions passed at the meeting are as follows: (1) Approved the Interim Report for the Six Months Ended 30th June 2004 of the Company. (2) Approved the proposal for profit distribution for the first half of 2004: no profit distribution or capital increment. (3) Approved the proposal that the Company transfer 24% shares with an amount of RMB1,552,677 of Guangzhou Masterwood Co., Ltd, a subsidiary of the Company, to the connected party Guangzhou Huangpu Shipyard, which is an enterprise wholly controlled by CSSC,

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whom controls 42.61% shares of the Company, and authorize the management to finalize the items of the shares transferring contract and sign the shares transferring contract with Guangzhou Huangpu Shipyard. The four independent directors issued independent opinions to this transferring and considered such connected transaction is fair and reasonable to independent shareholders. The five connected directors abstained from voting on this resolution.

6. The seventeenth meeting of the fourth term of the board of the Company was held at the reception room of the Company on 21st October 2004. All the eleven directors with three proxies of the fourth term of the Board of Directors attended the meeting. The resolutions passed at the meeting are as follows: (1) Approved the Third Quarterly Report as at 30th September 2004 of the Company. (2) Approved the proposal that the operating of Guangzhou Guanglian Container Transportation Co., Ltd., a subsidiary of the Company will be extended for 8 years, and will be terminated in case its return on net assets is less than 6% for any 2 consecutive years. (3) Approved to terminate the operating of Guangzhou Sanlong Industrial Trading Develop Co., Ltd., a subsidiary of the Company.
7. The eighteenth meeting of the fourth term of the Board of the Company was held on 19th November 2004, all eleven directors voted by means of written resolution for the proposals and the resolutions passed at the meeting are as follows: (1) Approved the annual budget of the year 2004. (2) Approved the proposal of Guangzhou International Trust and Investment Company ("GZITIC") debts restructuring. Besides the proposal of accepting cash to cover 50% debts, the Board of Directors authorized the management group of the Company to determine and come to a scheme of using assets, creditor's rights and share rights of GZITIC to restructure the debts owned by the Company with GZITIC under the preconditions of thorough consideration of the cash-exchangeable and operateable of the assets.
8. The nineteenth meeting of the fourth term of the Board of the Company was held on 20th December 2004, all eleven directors voted by means of written resolution for the proposal of the connected transaction that Guangzhou Xinshun Shipping Service Co., Ltd., a subsidiary of the Company, provides service to Guangzhou Wenchong Shipyard, a connected party of the Company, and the total amount of the transaction in 2004 would less than RMB10 million. The five connected directors abstained from voting on the proposal, other six directors including four independent directors were all voted for the proposal.

The execution by the Board of Directors in respect of the resolutions passed at General Meetings

During the year, the Board of Directors had executed all the resolutions passed at the 2003 Annual General Meeting and the 2004 Extraordinary General Meeting.

Interests of directors and supervisors

Except for the disclosure under "Information of Directors, supervisors, senior management and staff", at no time during the year, had the Company been notified that any director and supervisor (including their spouses and children under 18 years of age) had any interest in, or had been granted, or exercised, any rights to subscribe for equity or debt securities of the Company and its associated corporations (within the meaning of the SFO), which were required to be notified to the Company and The Stock Exchange of Hong Kong Limited pursuant to section 341 of the SFO or the Model Code for Securities Transactions by Directors of listed issuers or which were required to be entered in the register referred to the section 352 of the SFO.

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Service contracts of directors and supervisors

None of members of the fourth term of the Board of Directors and supervisory committee of the Company had entered into any service contract with the Company with payment for compensation for early termination of the service contract or non re-election upon the expiration of the service contract.

Interests of directors and supervisors in contracts

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

The highest paid individuals

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

Profit forecast

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

Profit distribution for the year 2004

As the Company has a profit of RMB33.67 million in the financial statements prepared in accordance with the PRC Accounting Rules and Regulations and a profit attributable to shareholders of RMB60.95 million in the financial statements prepared in accordance with the accounting principles generally accepted in Hong Kong in 2004. Since the accumulated retained earnings of the Company is negative, the profit should firstly offset loss in accordance with the Articles of Association of the Company, the Board of Directors proposed not to recommend any profit distribution or capital increment for the year 2004. This proposal will be submitted to 2004 Annual General Meeting for approval.

Financial summary

Summaries of the results, assets and liabilities of the Group for the last five financial years in accordance with the accounting principles generally accepted in Hong Kong and the PRC Accounting Rules and Regulations are set out on page 6 and page 7 , respectively.

Results and profit distribution

The results and profit distribution of the Group for the year ended 31 December 2004 prepared under PRC Accounting Rules and Regulations and the accounting principals generally accepted in Hong Kong are set out in the profit and loss statement on pages 66 to 67 and consolidated profit and loss account on page 118.

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Dividend

The directors do not recommend the payment of a dividend or a capital increment for the year 2004.

Reserves

The movements in the reserves of the Group which are prepared under PRC Accounting Standards and Systems and the accounting principles generally accepted in Hong Kong are set out in note (V) 19 to (V) 21 to the financial statements on page 95 to 96 and note 23 on page 158 to 161, respectively.

Fixed assets

Details of movements in fixed assets (including properties and other tangible assets) of the Group which are prepared under PRC Accounting Standards and Systems and the accounting principles generally accepted in Hong Kong are set out in note (V) 6 to the financial statements on page 87 to 88 and note 10 on page 145 to 147, respectively.

As at 31st December 2004, the net book value of fixed assets pledged as security for the Group's banking facilities amounted to RMB161.14 million.

Properties held for development or sale

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

Share capital

Details of the share capital of the Company are set out in "Share capital structure" on page 11.

Pre-emptive rights

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

Warrants and others

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

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Purchase, sale or redemption of the Company's securities

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

Bank loans, overdraft and other borrowings

Details of bank loans, overdraft and other borrowings of the Group are set out in note (V) 10 and (V) 16 to the financial statements on page 90 and 94 and note 21 and 24 on page 157 and 162, respectively.

Interest capitalisation

Details of interest capitalization of the Group during the year are set out in note (V) 7 to the financial statement on page 88.

Application of Statutory Public Welfare Fund

During the year, the Company has not applied statutory public welfare fund on purchase of fixed assets.

Capital expenditure

The Group expects that capital expenditure during 2005 would be approximately RMB78.69 million. The Group has sufficient financial resources to meet the demand for capital expenditure and daily working capital.

Exposure to fluctuation in exchange rate

As at 31 December 2004, revenue, expenses, assets and liabilities denominated in foreign currency do not have significant risk in exposure to fluctuations in exchange rate.

Contingent liabilities

As at 31 December 2004, the Group had no significant contingent liabilities.

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Connected transactions

The framework agreement for connected transactions of an operating nature made between the Company and CSSC was voted by independent shareholders and passed at the 2003 Annual General Meeting. Such transactions themselves are of an operational nature and in the normal and usual course of business of the Group, they allow the Group to leverage the reputation and bargaining power of the CSSC Group to provide a steady source of materials, labour and design and technology services necessary for the Group to conduct its business, they also allow flexibility in handling excess resources which are in short supply for the CSSC Group. The Directors including four independent non-executive directors named Mr. David Hon To, Yu, Mr. Philip Pat Yiu, Yuen, Mr. Bo Miaojin and Mr. Wu Fabo believe that the terms of the Framework Agreement, which are worked out in accordance with the provisions of relevant laws and regulations of mainland China and Hong Kong, are fair and reasonable and in the interests of the Independent Shareholders.

Apart from that, during the period under review, the Company's subsidiary Guangzhou Xinshun Shipping Service Co., Ltd. provided labor to an enterprise under CSSC with a total amount of RMB9.58 million. This connected transaction was reviewed by the Company's independent directors, and confirmed by its non-executive independent directors, Mr. David Hon To, Yu, Mr. Philip Pat Yiu, Yuen, Mr. Bo Miaojin and Mr. Wu Fabo, that it was carried out in the ordinary course of business and had been entered into accordance with the terms of the agreement covering such transaction or (where there is no such agreement) on terms no less favorable than terms available to third parties. The Group did not receive any extra ordinary benefit or loss from such transaction, which are considered as reasonable to the Group's shareholders.

Details of the transactions above-mentioned are set out in note (VI) to the financial statements prepared under PRC accounting standards on page 105. Furthermore, the above transactions, which also constitute connected party transactions under the listing rules of The Stock Exchange of Hong Kong Limited ("Listing Rules"), require disclosure in accordance with Chapter 14A of the Listing Rules. Details are set out in note 29 to the financial statements prepared under the accounting principals generally accepted in Hong Kong on page 167.

Employees' pension scheme

The Company and certain subsidiaries have joined the defined contribution retirement scheme operated by the provincial government of Guangdong Province since 1st January 1994. Under the scheme, the relevant group companies are required to make contributions at 18% of the standard salaries. Upon retirement, the retirees will receive monthly payments from the Social Insurance Bureau of Guangdong Province. Contributions made by the Group for the year ended 31 December 2004 was RMB23,821,000 (2003: RMB22,161,000). In addition, during the year the Group had made payments of RMB1,092,000 (2003: RMB897,755) as subsidies to retirees.

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Purchase of staff quarters by employees

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

Publications for disclosure

The publications used for disclosing information of the Company during the year 2004 are "Shanghai Securities News", "Hong Kong Commercial Daily" and "China Daily" (overseas version).

Significant litigation

The significant litigation of the Group happened during the period under review was set out in item 1 of Significant Events.

PRC Certified Accountants' Special Statement on the Capital Occupancy by the Controlling Shareholder and Connected Parties

Under the consignment of Guangzhou Shipyard International Company Limited ("the Company"), and in accordance with the requirements of the Guangzhou Zhen Jian [2004]15 "Notice of executing 'Notice of Regulating the Relevant Activities Concerning Funds Occupancy between Listed Companies and Connected Parties and External Guarantee by Listed Companies' "(the "Notice") issued by China Securities Regulatory Commission Guangzhou Securities Regulatory Office, Guangdong Yangcheng Certified Public Accountants Company Limited ("We") audited the transacted funds of the Company with its controlling shareholder and other connected parties. As at 31st December 2004, the funds transacted between the Company and CSSC and other connected parties are in the normal operational course of the Company (please refer to the audit report which reference of [2005] Yang Cha Zi Di4317). Apart from these, We has not found any breach by the Company to the requirements stated in the Notice, including without:

1. Providing operating capital such as wages, welfare, insurance and ads for controlling shareholder or other connected parties, or bearing cost and other expenses from each other.
2. Lending the fund of the Company to controlling shareholder or other connected parties with or without expenses.
3. Providing trust loans for connected parties through banks or non-banking financial institutions.
4. Consigning controlling shareholder or other connected parties to carry out investment activities.
5. Offering commercial honor draft without actual transaction backgrounds for controlling shareholder or other connected parties.
6. Returning debts for controlling shareholder or other connected parties.

Please refer to the Capital Occupancy Statement of Listed Company on page 52.

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Capital Occupancy Statement of Listed Company As at 31st December 2004

Share code	Listed company	Capital occupancy party	Relation between listed company and capital occupancy party	The date of the closing balance of the capital occupancy	The date of the opening balance of the capital occupancy	Corresponding item in accounting statement	Closing balance of capital occupancy (RMB)	Opening balance of capital occupancy (RMB)	Accumulated debit amount of capital occupancy (RMB)	Accumulated credit amount of capital occupancy (RMB)	occupancy measure	occupancy reason	Note
600685	GS Guangzhou Wenchong Shipyard	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Account receivable	1,276,498.04	733,813.13	13,033,975.41	12,491,290.50	Fund	for settlement		
600685	GS Guangzhou	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Account receivable	106,747.20	-	1,800,088.80	1,693,341.60	Fund	for settlement		
600685	GS Guangzhou Huangpu Shipyard	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Account receivable	0.00	102,578.39	2,986,896.50	3,071,474.89	Fund	for settlement		
600685	GS Guangzhou Shipyard	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Advanced payment	57,159.45	0.00	57,159.45		Fund	for settlement		
600685	GS Guangzhou Shipyard	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Account receivable	0.00	441,808.66	1,317,819.37	1,759,628.03	Fund	for settlement		
600685	GS Guangzhou Shipyard Guangda Company	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Advanced payment	4,596,057.79	7,647,297.52	716,044.53	3,767,284.26	Fund	for settlement		
600685	GS Guangzhou Shipyard Guangda Company	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Advanced payment	6,000,000.00	5,000,000.00	16,750,000.00	15,750,000.00	Fund	for settlement		
600685	GS Guangzhou Hudong Heavy Machine Company Limited	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Account receivable	0.00	20,314.30		20,314.30	Fund	for settlement		
600686	GS Guangzhou Holding Company	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Other receivable	47,971.75	0.00	47,971.75			for settlement		
600685	GS Guangzhou Zhenjiang Marine Diesel Factory	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Advanced payment	6,680,000.00	2,190,000.00	20,180,000.00	15,690,000.00	Fund	for settlement		
600685	GS Guangzhou Administrative Bureau	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Other receivable	-	27,000.00		27,000.00	Fund	for settlement		
600685	GS Guangzhou State Huanan Marine Mechanical Factory	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Account receivable	390,534.30	0.00	390,534.30			for settlement		
600685	GS Guangzhou State Huanan Marine Mechanical Factory	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Advanced payment	621,000.00	0.00	621,000.00		Fund	for settlement		
600685	GS Guangzhou China Shipbuilding International Trade Company	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Advanced payment	81,535.77	1,983,526.01		1,501,990.24	Fund	for settlement		
600685	GS Guangzhou Guilang Shipyard	Guangzhou Both controlled by CSC	31/12/2004	31/12/2003	Advanced payment	628,000.00	0.00	628,000.00					
Total				47,971.75	20,437,532.55	27,000.00	17,719,338.01	47,971.75	58,465,518.36	27,000.00	55,745,323.82		

REPORT OF THE BOARD OF DIRECTORS

Independent Directors' Special Statement on the External Guarantees of the Company

In accordance with the regulation stated in "Notice of Regulating the Finance Dealing with Connected Parties and the External Guarantees of Listed Companies", Zhen Jian Zi [2003] No. 56 (the "Notice") issued by China Securities Regulatory Commission (the "CSRC"), we, the independent directors of the Company, have thoroughly reviewed and checked the external guarantees of the Company and found that, the Company has abided by regulations of relevant law, regulations and rules issued by CSRC, and has not provided any guarantee for the controlling shareholder, other connected parties with less than 50% shares controlled by the Company, any unincorporated unit or individuals up to 31st December 2004.

Resolutions for significant assets loss result from external guarantees

During the period under review, the Company had not any external guarantees (except for the counter indemnity), and there were not any matters resulted from external guarantees.

Auditors

The financial statements for the year ended 31 December 2004 prepared under PRC accounting standards and Systems and the accounting principles generally accepted in Hong Kong have been audited by Guangdong Yangcheng Certified Public Accountants Company Limited and PricewaterhouseCoopers, Certified Public Accountants, respectively. They shall respectively resign and, being eligible, offer themselves for re-appointment.

Acknowledgment

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

On behalf of the Board of Directors

Chairman

Hu Guoliang

Guangzhou, 1st April 2005