

# Chairman's Statement

## BUSINESS REVIEW

During the financial year under review, international oil price reached record high, leading to the continuous price hike of petrochemical raw materials in the PRC market. The Group unavoidably has to face the competitive market environment resulting from the cost increment. The management responded quickly to the evolving market environment by actively negotiate with clients for price increase and strengthen its after sale services. As a result, the Group has managed to transfer part of the cost increment to its immediate customers. The Group continues to maintain its market competitiveness, thanks to its effective cost control measures and close monitoring of the changes in market price.

### Lubricants and anti-corrosive coating

Although gross profit of the lubricants and anti-corrosive coating segment was under pressure due to fluctuating crude oil price, the Group still managed to maintain its competitive advantages, satisfying the production needs of its customers through continuous improvement of its products according to their specific requirements. Also, thanks to the good long-term relationship with the large institutions (being both customers and suppliers to the Group), the Group can negotiate higher selling price and secure bulk raw materials purchase with better terms. As a result, the Group has successfully increased the sales during the year and thus offset the negative impact of cost increment on gross profit.

### Vinyl acetate

The Group's vinyl acetate plant situated in Mudanjiang has commenced production in October 2004. After continuous trial runs together with the improvement in production equipments, the annual output of the plant has already exceeded its designed production capacity of 15,000 tonnes. The vinyl acetate plant adopts the production technique of calcium carbide methodology (電石法化工工藝方法), which requires more downstream coal related chemical raw materials as ingredients comparing with that of the lubricants and anti-corrosive coating segment. As the prices of coal related chemical raw materials are relatively stable, so it could relieve the pressure on increasing production cost caused by the crude oil price hike. Comparing to those industry players who adopt the production technique of acetylene methodology (乙炔法化工工藝方法), the Group's products are more competitive in the market. Moreover, our Mudanjiang vinyl acetate plant is the first and only PRC plant using calcium carbide methodology to produce vinyl acetate with superior quality (concentration greater than 99.98%) which is higher than that of the PRC nation-wide recognized quality standard. During the financial year, the vinyl acetate business contributed significant profits to the Group.

### Prospects

The Board is very concerned about the impact of high crude oil price on the Group's results. The problem of global crude oil shortage and imbalanced supply and demand cannot be resolved in the near future, while the current global coal reserve is estimated to be able to meet the demand for over 100 years. Moreover, the supply and price of coal are relatively stable in the PRC. In view of the above, the Company is well prepared to increase and speed up the investment in coal related chemical field; which is in line with its strategy to develop its product chain through the coal related chemical methodology.

**PVC**

The Group successfully acquired the land, plants and production facilities of Mudanjiang PVC Factory through an auction in May 2005. The Board believes that the acquisition of Mudanjiang PVC Factory will expand the development of coal related chemical production, forming a part of calcium carbide production chain. At the same time, the acquisition will enhance the product range of the Group and alleviate the effects of high crude oil price on the Group's performance. In addition, the Group can also consolidate its presence in Mudanjiang, turning it into another major production base in the northeastern region of the PRC.

On 27 September 2005, the Group formally took over the assets and related operations of Mudanjiang PVC Factory. The Group is planning to secure bulk purchase on raw materials in order to achieve economy of scale. Meanwhile, the Group can utilize its management experience in relation to the calcium carbide methodology to enhance the efficiency and effectiveness of the PVC Factory. In addition, the Group is planning to upgrade the existing PVC production equipment attempting to produce high-grade PVC raw materials. The PVC business is expected to yield significant profits for the Group in the financial year of 2006.

In addition, the Group will continue to leverage on the business opportunities created by the government policy in relation to the reform and restructure of the existing state-owned industries in the northeastern region of the PRC. With the enhancement of the Group's coal related chemical production technique through advance technology and optimization to its downstream coal related chemical products, together with the continuous exploration for further opportunities to acquire or merge with other coal related chemical factories and businesses in the northeastern region of the PRC, the Board is confident that the Group will be able to establish a high value added production chain for coal related chemical products, the synergy effects of which will provide maximum return for shareholders.

**Gratitude**

On behalf of the Company, I would like to extend my heart-felt gratitude to all our staff, shareholders, investors, customers and business partners who have given continuous support to the Group.

By order of the Board

**Chan Yuk Foebe**

Chairman and Executive Director

Hong Kong, 10 October 2005