

Report of the Directors

The directors submit their report together with the audited accounts for the year ended 31st December 2005.

PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding.

The principal activities and other relevant details of the subsidiaries and associates are set out in notes 13 and 14 to the accounts respectively.

The Group's turnover and operating results are attributable to its principal activity of investment holding carried out in Hong Kong. The major contribution to net profit and loss is attributable to its investments in associates operating in Hong Kong and the Mainland China.

An analysis of the Group's performance for the year by business and geographical segments is set out in note 6 to the accounts.

The Company, being an investment holding company, has no supplier or customer. All the subsidiaries are either investment holding companies or dormant companies and have no supplier or customer.

RESULTS AND APPROPRIATIONS

The results of the Group for the year are set out in the consolidated profit and loss account on page 29.

The directors do not recommend the payment of a dividend for the year ended 31st December 2005.

RESERVES

Movements in the reserves of the Group and the Company during the year are set out in note 21 to the accounts.

DISTRIBUTABLE RESERVES

The Company had no distributable reserves at 31st December 2005.

FIVE-YEAR FINANCIAL SUMMARY

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on page 76.

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PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S SHARES

The Company has not redeemed any of its shares during the year. Neither the Company nor any of its subsidiaries has purchased or sold any of the Company's shares during the year.

DIRECTORS

The directors during the year and up to the date of this report were:

Lao Yuan Yi

Wang Jun Yan

Lao Yuan Yuan (appointed on 20th September 2005)

Zhao Yu Qiao

Jiang Wei

Yeung Wai Kin

* Peter Duncan Neil Robertson

* Fan Jia Yan

* Wu Ming Yu

Non-executive directors

* *Independent non-executive directors*

In accordance with Articles 90 and 98 of the Company's Articles of Association, Mr. Wang Jun Yan and Ms. Lao Yuan Yuan will retire at the forthcoming annual general meeting and be eligible to offer themselves for re-election.

All the non-executive directors were appointed for a term of two years.

DIRECTORS' SERVICE CONTRACTS

No director (whether or not he is proposed for re-election at the forthcoming annual general meeting) has a service contract with the Company which is not determinable within one year without payment of compensation, other than statutory compensation (if any).

BIOGRAPHICAL DETAILS OF DIRECTORS

Brief biographical details of directors are set out on pages 12 and 13.

CONTINUING CONNECTED TRANSACTIONS

The related party transactions disclosed in note 24(a)(i) to the accounts constituted continuing connected transactions under the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") up to 30th December 2005.

On 28th March 1991, the Company entered into a management agreement (the "Management Agreement") with China Assets Investment Management Limited ("CAIML") whereby CAIML was appointed to act as investment manager of the Company and agreed to provide management services to the Company and present suitable investment opportunities to the Company. The Management Agreement was subsequently amended on 8th April 1992. The Management Agreement is not for a fixed term but may be terminated by either party serving not less than six months' written notice on the other party provided that the Company is required to have the approval of its shareholders before giving such notice.

On 11th October 2004, the Company and CAIML entered into a supplemental agreement ("Supplemental Agreement") to fix the term of the Management Agreement so that the Management Agreement, together with the Supplemental Agreement ("Amended Management Agreement") will continue until 31st December 2006, and thereafter renewable for further terms of 2 years each provided that the requirements of the Listing Rules are complied with before renewal. The Amended Management Agreement may be terminated by either party by serving not less than six months' written notice to the other party provided that the Company is required to have the approval of its shareholders (by way of ordinary resolution) before giving such notice.

Under the Amended Management Agreement, CAIML is entitled to receive from the Company a management fee at the rates of (i) 2.75% per annum on the aggregate cost to the Company of the investment (less any provisions in respect thereof) held by it from time to time; and (ii) 1% per annum on the value of the uninvested net assets of the Company. In addition, CAIML is entitled to performance bonus based on a specified formula on the return on net assets and net capital gains of the Company.

CAIML is a subsidiary of First Shanghai Investments Limited ("FSIL"), a substantial shareholder of the Company holding approximately 33.82% of the issued capital of the Company as at 31st December 2005. The Company is a substantial shareholder of FSIL holding approximately 21.002% of the issued share capital of FSIL as at 31st December 2005. On 30th December 2005, FSIL disposed of part of its shareholding in CAIML and as a result, CAIML ceased to be a subsidiary of FSIL. Accordingly, the above related party transactions discontinued to constitute continuing connected transactions from 31st December 2005.

During the year, the Company paid US\$1,264,301 (2004: US\$1,026,795) to CAIML under the Amended Management Agreement. No performance bonus had been paid to CAIML (2004: Nil). As the amount paid under the Amended Management Agreement is below the applicable percentage ratio under the Listing Rules. As a result, independent shareholders' approval of the Amended Management Agreement was exempted under the Listing Rules. As at the date of this report, the directors of the Company are not aware of any circumstances as a result of which the exemption may cease to apply.

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CONTINUING CONNECTED TRANSACTIONS (Continued)

The directors of the Company confirm that none of them has any equity interest in CAIML or any personal interest in the Amended Management Agreement except that (a) Mr. Lao Yuan Yi, a director of the Company, FSIL and CAIML, has an indirect interest in CAIML through his 7.64% personal interests and 6.18% corporate interests in FSIL; (b) Mr. Yeung Wai Kin, a director and a shareholder (effective from 30th December 2005) of CAIML, is also a director of FSIL and the Company (c) Mr. Wang Jun Yan, a director of the Company, is also a director and a shareholder (effective from 30th December 2005) of CAIML.

As a result of the annual review of the Amended Management Agreement as a continuing connected transactions from 1st January 2005 to 30th December 2005, the directors of the Company (including the independent non-executive directors) confirm their views that the Amended Management Agreement has been entered into (i) in the ordinary and usual course of business of the Company; (ii) on normal commercial terms; and (iii) on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

SHARE OPTIONS

Options in respect of shares in the Company

At the Annual General Meeting of the Company held on 19th May 2004, the shareholders of the Company approved the adoption of a share option scheme (the "Scheme"). The purpose of the Scheme is to enable the Company to grant options for the subscription of shares in the Company to selected participants as incentives or rewards for their contribution to the Group. Pursuant to the terms of the Scheme, the Directors may at their discretion offer any employee, proposed employee or director of the Company, any of its subsidiaries, its investment manager, CAIML (the "Manager") or any invested entity in which the Group holds not less than 20% of its equity interest to take up options to subscribe for the shares in the Company.

Details of the share options granted under the Scheme and remain outstanding as at 31st December 2005 are as follows:

	Options held at 1st January 2005	Options exercised during the year	Options held at 31st December 2005	Exercise price HK\$	Closing price before the date of grant HK\$	Date of grant	Exercise period
Directors:							
Lao Yuan Yi	740,000	(15,000) ¹	725,000	2.65	2.50	21/05/2004	25/05/2004-23/05/2014
Wang Jun Yan	700,000	—	700,000	2.65	2.50	21/05/2004	25/05/2004-23/05/2014
Jiang Wei	50,000	—	50,000	2.65	2.50	21/05/2004	25/05/2004-23/05/2014
Yeung Wai Kin	700,000	—	700,000	2.65	2.50	21/05/2004	25/05/2004-23/05/2014
Zhao Yu Qiao	700,000	—	700,000	2.65	2.50	21/05/2004	25/05/2004-23/05/2014
Peter Duncan Neil Robertson	70,000	—	70,000	2.65	2.50	21/05/2004	25/05/2004-23/05/2014
Fan Jia Yan	70,000	—	70,000	2.65	2.50	21/05/2004	25/05/2004-23/05/2014
Wu Ming Yu	70,000	—	70,000	2.65	2.50	21/05/2004	25/05/2004-23/05/2014
Employees of the Manager	700,000	—	700,000	2.65	2.50	21/05/2004	25/05/2004-23/05/2014
	3,800,000	(15,000)	3,785,000				

¹ The exercise date was 7th June 2005. The closing price before the date of exercise was HK\$4.20.

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SHARE OPTIONS (Continued)

Options in respect of shares in associated corporations

			Balance of options not exercised (percentage of issued share capital) as at 31st December 2005	Exercise price HK\$	Exercise period
Directors:					
Lao Yuan Yi	First Shanghai Investments Limited	11/07/1996	5,503,900	0.318	11/01/1997 — 15/07/2006
		01/11/1997	10,000,000	0.816	01/05/1998 — 12/11/2007
		30/11/2005	22,842,000	0.564	30/05/2006 — 11/12/2015
			38,345,900 (3.24%)		
Wang Jun Yan	First Shanghai Investments Limited	08/07/1998	1,000,000	0.283	08/01/1999 — 15/07/2008
		30/11/2005	11,810,000	0.564	30/05/2006 — 11/12/2015
			12,810,000 (1.08%)		
Yeung Wai Kin	First Shanghai Investments Limited	11/07/1996	1,494,304	0.318	11/01/1997 — 15/07/2006
		01/11/1997	2,500,000	0.816	01/05/1998 — 12/11/2007
		08/07/1998	6,980,000	0.283	08/01/1999 — 15/07/2008
		30/11/2005	11,810,000	0.564	30/05/2006 — 11/12/2015
			22,784,304 (1.93%)		

The above share options were granted under the share option scheme of First Shanghai Investments Limited adopted on 24th May 2002.

DIRECTORS' INTERESTS IN CONTRACTS OF SIGNIFICANCE

Save for the Amended Management Agreement as disclosed in the section headed Continuing Connected Transactions above, no other contracts of significance in relation to the Group's business to which the Company or its subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

Save for the Amended Management Agreement as disclosed in the section headed Continuing Connected Transactions above, no contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

DIRECTORS' INTERESTS AND SHORT POSITIONS IN THE SHARES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS

As at 31st December 2005, the interests and short positions of the directors and chief executives of the Company in the shares of the Company or its associated corporations (within the meaning of the Securities and Futures Ordinance (Cap. 571) ("SFO") recorded in the register maintained by the Company under section 352 of the SFO or notified to the Company and The Stock Exchange of Hong Kong Limited pursuant to the Model Code for Securities Transactions by Directors of Listed Companies contained in the Listing Rules, were as follows:

Shares in associated corporations

			Number of ordinary shares interested (percentage of issued share capital)
Associated corporation	Name	Type of interest	
First Shanghai Investments Limited	Lao Yuan Yi	Personal	90,216,000
		Corporate	72,952,000
			163,168,000 (13.82%)

Apart from the Amended Management Agreement and the share option schemes stated above, at no time during the year had the Company, its subsidiaries, its associates, its fellow subsidiaries a party to any arrangement to enable the directors and chief executives of the Company to hold any interests or short positions in the shares or underlying shares in, or debentures of, the Company or its associated corporation.

SUBSTANTIAL SHAREHOLDERS' INTERESTS AND SHORT POSITIONS IN THE SHARES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS

The register of substantial shareholders' interests maintained under section 336 of the SFO reveals that as at 31st December 2005, the Company had been notified of the following interests of the substantial shareholders of the Company, being 5% or more of the Company's issued shares that carry a right to vote at general meetings of the Company.

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SUBSTANTIAL SHAREHOLDERS' INTERESTS AND SHORT POSITIONS IN THE SHARES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS (Continued)

Name	Type of interest	Capacity	Number of ordinary shares held	Percentage of issued share capital
First Shanghai Investments Limited ("FSIL") (Note 1)	Corporate	Interest of Controlled Corporation	25,162,866	33.82%
First Shanghai Direct Investments Limited ("FSDI") (Note 1)	Corporate	Interest of Controlled Corporation	25,162,866	33.82%
Golad Resources Limited (Note 1)	Corporate	Beneficial Owner	25,162,866	33.82%
Deutsche Bank Aktiengesellschaft	Corporate	Security Interest	13,420,000	18.04%
QVT Financial LP (Note 2)	Corporate	Investment Manager	13,405,000	18.02%
QVT Financial GP LLC (Note 2)	Corporate	Interest of Controlled Corporation	13,405,000	18.02%
QVT Associates GP LLC (Note 3)	Corporate	Interest of Controlled Corporation	10,444,000	14.04%
QVT Fund LP (Note 3)	Corporate	Beneficial Owner	10,444,000	14.04%
Chen Dayou	Personal	Beneficial Owner	8,405,000	11.30%

Notes:

- (1) Both FSIL and FSDI had corporate interests in the issued share capital of the Company through their indirect or direct share interests in Golad Resources Limited. Golad Resources Limited is wholly-owned by FSDI, which is, in turn, wholly-owned by FSIL.
- (2) QVT Financial GP LLC had interest in QVT Financial LP which is deemed to have interest in the issued share capital of the Company since QVT Financial LP acts in the capacity of investment manager to QVT Fund LP.
- (3) QVT Associates GP LLC had interest in the issued share capital of the Company through its interest in QVT Fund LP.

Save as disclosed above, no other shareholders of the Company had any beneficial or legal interests in 5% or more of the Company's issued shares that carry a right to vote in general meetings of the Company as recorded in the register maintained by the Company. All the interests described above represent long position in the shares of the Company and no short positions, deemed interests or derivative interests were recorded in the register maintained by the Company as at 31st December 2005.

CODE ON CORPORATE GOVERNANCE PRACTICES

The Company has complied with the code provisions of the Code on Corporate Governance Practices as set out in Appendix 14 of the Listing Rules during the year ended 31st December 2005 except for the deviations set out in the Corporate Governance Report on pages 14 and 19.

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AUDIT COMMITTEE

By reference to "A Guide for the Formation of An Audit Committee" published by the Hong Kong Institute of Certified Public Accountants, the written terms of reference which describe the authority and duties of the audit committee were prepared and adopted by the Board of the Company on 30th December 1998. The principal activities of the Audit Committee include the review and supervision of the Group's financial reporting process and internal controls. The Committee comprises three independent non-executive directors and a non-executive director.

MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted Appendix 10 of the Listing Rules "Model Code for Securities Transactions by Directors of Listed Issuers" as rules for securities transactions initiated by the directors of the Company. After specifically inquiring with all the directors of the Company, the Company confirms that its directors' securities transactions have been fully complied with the standard laid down in the said rules at any time during the year ended 31st December 2005.

INDEPENDENCE OF INDEPENDENT NON-EXECUTIVE DIRECTORS

The Company has received, from each of the independent non-executive directors, a confirmation of his independence pursuant to rule 3.13 of the Listing Rules. The Board believes that the existing independent non-executive directors are independent based on the guidelines set out in rule 3.13 of the Listing Rules.

SUFFICIENCY OF PUBLIC FLOAT

Based on the information that is publicly available to the Company and within the knowledge of the directors, it is confirmed that there is sufficient public float of more than 25% of the Company's issued shares as at the date of this report.

AUDITORS

The accounts have been audited by PricewaterhouseCoopers who retire and, being eligible, offer themselves for re-appointment.

On behalf of the Board

Lao Yuan Yi

Chairman

Hong Kong, 21st April 2006