Notes to the Financial Statements

31 December 2001

1. ORGANISATION AND PRINCIPAL ACTIVITIES

Heshun Specialised Fibre Holdings Limited (formerly known as Heshun Holdings Company Limited) (the "Company") was incorporated in Bermuda on 28 June 2000 as an exempted company with limited liabilities under the Companies Act 1981 of Bermuda. The Company's shares have been listed on The Stock Exchange of Hong Kong Limited since 15 November 2000.

The Company is an investment holding company. Its subsidiaries are principally engaged in the production and distribution of differential chemical fibre products. The Group ceased to provide engineering and installation services for chemical fibre projects and the design and installation of chemical fibre production machinery and equipment upon disposal of Dalian Huayang Engineering Co., Ltd. ("Dalian Huayang").

The Directors of the Company consider Process Logistics Limited, a company incorporated in British Virgin Islands, to be the ultimate holding company.

2. BASIS OF PREPARATION

As at 31 December 2001, the Group had net current liabilities of approximately RMB327,104,000. As explained in the consolidated cash flow statement, despite the positive net cash flows from operating activities, the Group had a significant negative cash flows after investing activities had been taken into consideration. The directors are of the opinion that the Group's financial position and tight cash flows are mainly attributable to the investing activities which are principally related to the Spandex project and development of new production lines. As at 31 December 2001, the Group had total borrowings of approximately RMB424,089,000 of which approximately RMB207,204,000 was overdue. The Group is currently under negotiations with the bankers to reschedule the bank borrowings and to seek their ongoing support to the Group. As at the date of approval of these financial statements, certain bankers have given written indications that they have the intention to provide continuing financial support to the Group. The directors believe that the negotiations will be successful and that the bank borrowings will be repaid through the funds generated from continuing profitable operations and additional resources from future fund raising exercises, including the procurement of new banking facilities and new equity financing.

Included in the current portion of long-term borrowings is a syndicated bank loan of approximately RMB90,217,000. One of the guarantors of the loan is Mr Chen Shunli, a director of the Company. On 10 January 2002, Mr Chen was involved in a personal civil litigation. This led to a breach of certain terms of the deed of guarantee which in turn led to a breach of certain terms of the loan agreement. As a result, the loan has become technically repayable on demand and has been re-classified as a current liability. As at the date of approval of these financial statements, the banks have not demanded repayment of the loan. The directors are of the opinion that the banks will give continuing financial support to the Group and allow the Group to repay the loan in accordance with the original terms of the loan agreement.

Included in the current portion of long-term borrowings are two term loans in an aggregate amount of approximately RMB27,872,000. Their loan agreements contain certain financial covenants. The publication of these financial statements discloses the fact that the Group has not complied with the covenants which give rise to defaults. As a consequence, the loans have become technically repayable on demand and have been re-classified as current liabilities. The directors are of the opinion that they are able to negotiate successfully with the financial institutions and to repay the loans in accordance with the original terms of the loan agreements.

2. BASIS OF PREPARATION (continued)

In light of the measures taken and the expected outcome, the directors are satisfied that it is appropriate to prepare the financial statements on a going concern basis.

If the going concern basis was not to be appropriate, adjustments would have to be made to restate the values of the assets to their recoverable amounts, to provide for any further liabilities which might arise and to reclassify non-current assets and long term liabilities as current assets and current liabilities, respectively.

3. PRINCIPAL ACCOUNTING POLICIES

The financial statements have been prepared in accordance with generally accepted accounting principles in Hong Kong and comply with Statements of Standard Accounting Practice ("SSAPs") issued by the Hong Kong Society of Accountants ("HKSA"), the disclosure requirements of the Hong Kong Companies Ordinance and the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited. Principal accounting policies are summaries below.

In the current year, the Group adopted the following SSAPs issued by the HKSA which are effective for accounting periods commencing on or after 1 January 2001:

SSAP 9 (revised)	:	Events after the balance sheet date
SSAP 14 (revised)	:	Leases (effective for periods commencing on or after 1 July 2000)
SSAP 26	:	Segment reporting
SSAP 28	:	Provisions, contingent liabilities and contingent assets
SSAP 29	:	Intangible assets
SSAP 30	:	Business combinations
SSAP 31	:	Impairment of assets
SSAP 32	:	Consolidated financial statements and accounting for investments in subsidiaries

The effect of adopting these new standards is set out in the accounting policies detailed below.

(a) Basis of measurement

The financial statements are prepared under the historical cost convention.

3. PRINCIPAL ACCOUNTING POLICIES (continued)

(b) Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries made up to 31 December 2001. The subsidiaries are those entities in which the Group controls the composition of the board of directors, controls more than half the voting power or holds more than half of the issued share capital or has power to govern the financial and operating policies.

The results of subsidiaries as 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. All significant intercompany transactions and balances within the Group are eliminated on consolidation.

The gain or loss on the disposal of a subsidiary represents the difference between the proceeds of the sale and the Group's share of its net assets together with any unamortised goodwill or negative goodwill or goodwill/negative goodwill taken to reserves and which was not previously charged or recognised in the consolidated income statement.

Minority interests represent the interests of outside shareholders in the operating results and net assets of subsidiaries.

In the Company's balance sheet the investments in subsidiaries are stated at cost less provision for impairment losses. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable.

(c) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net assets of the acquired subsidiary at the date of acquisition.

In accordance with SSAP 30, goodwill on acquisitions occurring on or after 1 January 2001 is included in intangible assets and is amortised using the straight-line method over its estimated useful life. Goodwill arising on acquisitions is amortised over a maximum period of 10 years.

Goodwill on acquisitions that occurred prior to 1 January 2001 was written off against reserves. The Group has taken advantage of the transitional provision 1(a) in SSAP 30 and goodwill previously written off against reserves has not been restated. However any impairment arising on such goodwill is accounted for in accordance with SSAP 31.

Negative goodwill represents the excess of the fair value of the Group's share of the net assets acquired over the cost of acquisition.

3. PRINCIPAL ACCOUNTING POLICIES (continued)

(c) Goodwill (continued)

For acquisitions after 1 January 2001, negative goodwill is presented in the same balance sheet classification as goodwill. To the extent that negative goodwill relates to expectations of future losses and expenses that are identified in the Group's plan for the acquisition and can be measured reliably, but which do not represent identifiable liabilities at the date of acquisition, that portion of negative goodwill is recognised in the income statement when the future losses and expenses are recognised. Any remaining negative goodwill, not exceeding the fair values of the non-monetary assets acquired, is recognised in the income statement over the remaining weighted average useful life of those assets; negative goodwill in excess of the fair values of those non-monetary assets is recognised in the income statement immediately.

For acquisitions prior to 1 January 2001, negative goodwill was taken directly to reserves on acquisition. The Group has taken advantage of the transitional provisions in SSAP 30 and such negative goodwill has not be restated.

The gain or loss on disposal of an entity includes the unamortised balance of goodwill relating to the entity disposed of or, for pre 1 January 2001 acquisitions, the related goodwill written off against or negative goodwill taken directly to reserves to the extent it has not previously been realised in the income statement.

(d) Associates

An associate is a company in which the Group has significant influence but not control or joint control, and thereby has the ability to participate in its financial and operating policy decisions.

In the consolidated financial statements, investment in associate is accounted for under the equity method of accounting, whereby the investment is initially recorded at cost and the carrying amount is adjusted to recognise the Group's share of the post-acquisition profits or losses of the associate, distributions received from the associate and other necessary alterations in the Group's proportionate interest in the associate arising from changes in the equity of the associate that have not been included in the income statement.

3. PRINCIPAL ACCOUNTING POLICIES (continued)

(e) Revenue recognition

Provided it is probable that the economic benefits associated with a transaction will flow to individual companies of the Group and the revenue and costs, if applicable, can be measured reliably, turnover and other revenue are recognised on the following basis:

i) Revenue on sales of goods is recognised when the significant risks and rewards of ownership of goods, have been transferred to customers.

ii) Revenue on subcontracting work services is recognised when the subcontracting work services are rendered.

iii) Revenue from a fixed price contract is recognised using the percentage of completion method measured by reference to the proportion that completed contract work bear to estimated total contract work.

iv) Operating lease rental income is recognised when the right to receive is established.

v) Interest income is recognised on a time proportion basis on the principal outstanding and at the applicable rate.

(f) Fixed assets and depreciation

Fixed assets are stated at cost less accumulated depreciation. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

Expenditure incurred after the fixed assets have been put into operation, such as repairs and maintenance and overhaul costs, is normally charged to the income statement in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of the fixed assets, the expenditure is capitalised as an additional cost of the fixed assets.

Depreciation is calculated on the straight-line basis at annual rates estimated to write off the cost of each asset over its expected useful lives, after deducting the estimated residual value. The annual rates of depreciation are as follows:

Land	1.9%
Buildings	4.75%
Machinery	4.75%
Motor vehicles	19%
Other equipment	19%

Assets held under finance leases are depreciated over their expected useful lives, after deducting the estimated residual value, on the same basis as owned assets.

When assets are sold or retired, their cost and accumulated depreciation and amortisation are eliminated from the financial statements and any gain or loss resulting from their disposals is included in the determination of profit and loss.

3. PRINCIPAL ACCOUNTING POLICIES (continued)

(g) Construction-in-progress

Construction-in-progress represents facilities under construction and plant and machinery pending installation, and is stated at cost. This includes the costs of construction, the costs of plant and machinery and interest charges arising from borrowings used to finance these assets during the period of construction or installation and testing.

No provision for depreciation is made on construction-in-progress until such time as the relevant assets are completed and put into operational use.

(h) Prepayments for fixed assets

Prepayments for fixed assets represents downpayment for acquisition of machinery and land and buildings and are stated at cost. Prepayments for fixed assets are reclassified to fixed assets when the relevant assets are delivered and put into operational use.

(i) Impairment of assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the assets may be impaired or an impairment loss previously recognised no longer exists or may have decreased.

If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset exceeds its recoverable amount.

(i) Calculation of recoverable amount
The recoverable amount of an asset is the greater of its net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

(ii) Reversals of impairment losses
In respect of assets other than goodwill, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss in respect of goodwill is reversed only if the loss was caused by a specific external event of an exceptional nature that is not expected to recur, and the increase in recoverable amount relates clearly to the reversal of the effect of that specific event.

A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. Reversals of impairment losses are credited to the income statement in the year in which the reversals are recognised.

3. PRINCIPAL ACCOUNTING POLICIES (continued)

(j) Inventories

Inventories are stated at the lower of cost and net realisable value. Cost, calculated on a weighted average basis, comprises all costs of purchases, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Net realisable value is calculated based on the estimated normal selling price in the ordinary course of business less further costs expected to be incurred to completion and related selling and distribution expenses.

When inventories are sold, the carrying amount of those inventories is recognised as an expense in the period in which the related revenue is recognised. The amount of any write-down of inventories to net realisable value and all losses of inventories are recognised as an expense in the period in which the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realisable value, is recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

(k) Trade receivables

Provision is made against trade receivables to the extent that they are considered to be doubtful. Trade receivables in the balance sheet is stated net of such provision.

(l) Cash equivalents

Cash equivalents are short-term, highly liquid investments which are readily convertible into known amounts of cash without notice and which were within three months of maturity when acquired; less advances from banks repayable within three months from the date of the advance. Cash equivalents include investments and advances denominated in foreign currencies provided that they fulfil the above criteria.

(m) Provisions and contingent liabilities

A provision is recognised when there is present obligation, legal or constructive, as a result of a past event and it is probable (i.e. more likely than not) that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. Provisions are reviewed regularly and adjusted to reflect the current best estimate. Where the effect of the time value of money is material, the amount of a provision is the present value of the expenditures expected to be required to settle the obligation.

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised but is disclosed in the notes to the financial statements. When a change in the probability of an outflow occurs so that outflow is probable, they will then be recognised as a provision.

3. PRINCIPAL ACCOUNTING POLICIES (continued)

(n) Related parties

Two parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence.

(o) Taxation

Individual companies within the Group provide for profits tax on the basis of their profit for financial reporting purposes, adjusted for income and expense items which are not assessable or deductible for profits tax purposes.

Deferred taxation is accounted for under the liability method in respect of timing differences between profit as computed for taxation purposes and profit as stated in the financial statements to the extent that a liability or asset is expected with reasonable probability to crystallise in the foreseeable future. Deferred tax asset is not recognised unless its realisation is assured beyond reasonable doubt.

(p) Leases

i) Finance leases

Leases that transfer to the Company substantially all the rewards and risks of ownership of the assets, other than legal title, are accounted for as finance leases.

Fixed assets held under financial leases are initially recorded at the present value of the minimum lease payments at the inception of the leases, with the equivalent liabilities recorded as appropriate under current or non-current liabilities.

Finance charges, which represent the difference between the minimum lease payments at the inception of the leases and the fair value of the assets, are allocated to accounting periods over the period of the relevant leases so as to produce a constant period rate of charge on the outstanding balances.

ii) Operating leases

Lease where substantially all the rewards and risks of ownership remain with the leasing company are accounted for as operating leases. Rental payments under operating lease are charged to the income statement on a straight-line basis over the period of the relevant leases.

Lease income from operating leases is recognised in income statement on a straight-line basis over the lease term. Assets subject to operating leases in their balance sheet are presented according to the nature of the assets.

3. PRINCIPAL ACCOUNTING POLICIES (continued)

(q) Translation of foreign currencies

Individual companies within the Group maintain their books and records in the primary currencies of their respective operations ("functional currencies"). In the financial statements of the individual companies, transactions in other currencies during the year are translated into the respective functional currencies at the applicable rate of exchange prevailing at the time of the transactions. Monetary assets and liabilities denominated in other currencies are translated into their respective functional currencies at the applicable rates of exchange in effect at the balance sheet date. Exchange gains or losses are dealt with in the income statement of the individual companies.

The Group prepares the consolidated financial statements in Renminbi ("RMB"). For the purpose of consolidation, assets and liabilities of subsidiaries with functional currencies other than RMB are translated into RMB at the applicable rates of exchange in effect at the balance sheet date; income and expense items are translated into RMB at the average applicable rates during the year. Exchange differences arising from such translation are dealt with as movements in reserves.

(r) Staff retirement benefits

Costs of staff retirement benefits are recognised as an expense in the period in which they are incurred.

(s) Borrowing costs

Borrowing costs that are directly attributable to the acquisition, construction or production of an assets that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of that asset.

All other borrowing costs are charged to the income statement in the year in which they are incurred.

(t) Segment reporting

In accordance with the Group's internal financial reporting the Group has determined that business segments be presented as the primary reporting format and no geographical segments is presented as all the Group's turnover and operating profit are derived from activities in Mainland China.

Segment assets consist primarily of fixed assets, construction-in-progress, prepayments for fixed assets, inventories, receivables, deposits, prepayments and operating cash and mainly exclude investments. Segment liabilities comprise operating liabilities and exclude items such as taxation and certain borrowings. Capital expenditure comprise additions to fixed assets, construction-in-progress and prepayments for fixed assets.

4. TURNOVER, REVENUE AND SEGMENT INFORMATION

The Group is principally engaged in the production and distribution of differential chemical fibre products, and in the provision of engineering and installation services for chemical fibre projects and the design and installation of chemical fibre production machinery and equipment. Revenues recognised during the year are as follows:

	Group	
	2001	2000
	RMB'000	*RMB'000*
Sales of goods	**617,745**	480,106
Processing fees	**4,771**	135,475
Fees from construction contracts	**33,340**	18,404
Total turnover	**655,856**	633,985
Other income	**2,704**	2,117
Operating lease income	**—**	174
Interest income	**134**	164
Total revenue	**658,694**	636,440

Primary reporting format - business segments

The Group is organised, in Mainland China, into two main business segments:

- Production and sales of differential chemical fibre products and provision of subcontracting services for manufacturing differential chemical fibre products.
- Provision of engineering and installation services for chemical fibre projects and machinery and equipment.

There are no sales or other transactions between the business segments.

Since all the Group's turnover and operating profit are derived from activities in Mainland China, no geographical analysis is shown.

Notes to the Financial Statements

31 December 2001

4. TURNOVER, REVENUE AND SEGMENT INFORMATION (continued)

Primary reporting format - business segments (continued)

	2001		
	Continuing operations sales of goods *RMB'000*	**Discontinued operations construction contracts** *RMB'000*	**Group** *RMB'000*
Turnover	**622,516**	**33,340**	**655,856**
Segment results	**184,897**	**4,512**	**189,409**
Unallocated costs			**(23,389)**
Other income			**2,704**
Operating profit			**168,724**
Finance costs, net			**(25,066)**
Share of loss of an associate			**—**
Gain on disposal of discontinued operations	**—**	**23,710**	**23,710**
Profit before taxation			**167,368**
Taxation			**(23,951)**
Profit after taxation			**143,417**
Minority interests			**263**
Profit attributable to shareholders			**143,680**
Segment assets	**1,461,476**	**—**	**1,461,476**
Unallocated assets			**7,235**
Total assets			**1,468,711**
Segment liabilities	**101,326**	**—**	**101,326**
Unallocated liabilities			**510,231**
Total liabilities			**611,557**
Capital expenditure	**254,556**	**7**	**254,563**
Depreciation			
— segment depreciation	**39,076**	**2,373**	**41,449**
— unallocated depreciation			**456**
			41,905

4. TURNOVER, REVENUE AND SEGMENT INFORMATION (continued)

Primary reporting format - business segments (continued)

	2000		
	Continuing operations sales of goods *RMB'000*	Discontinued operations construction contracts *RMB'000*	Group *RMB'000*
Turnover	615,581	18,404	633,985
Segment results	222,137	6,048	228,185
Unallocated costs			(4,284)
Other income			2,117
Operating profit			226,018
Finance costs, net			(23,538)
Share of loss of an associate			(22)
Gain on disposal of discontinued operations			—
Profit before taxation			202,458
Taxation			(24,776)
Profit after taxation			177,682
Minority interests			4,739
Profit attributable to shareholders			182,421
Segment assets	1,118,638	85,386	1,204,024
Investment in an associate			70,303
Unallocated assets			3,197
Total assets			1,277,524
Segment liabilities	114,879	28,876	143,755
Unallocated liabilities			415,948
Total liabilities			559,703
Capital expenditure	447,788	15,459	463,247
Depreciation			
— segment depreciation	33,622	65	33,687
— unallocated depreciation			110
			33,797

5. FINANCE COSTS, NET

	Group	
	2001	2000
	RMB'000	*RMB'000*
Interest income		
Bank deposits	**(134)**	(164)
Interest expenses		
— Bank loans wholly repayable within five years	**22,831**	23,674
— Other loans wholly repayable within five years	**2,298**	—
Finance charges in respect of finance lease	**71**	28
	25,066	23,538

6. GAIN ON DISPOSAL OF DISCONTINUED OPERATIONS

On 29 November 2001, in view of the decrease in profit margin and intensive competition, the directors announced to dispose of the operations of the engineering and installation services for chemical fibre projects and design and installation of chemical fibre production machinery and equipment.

The subsidiary comprising the engineering and installation operation, Dalian Huayang, was sold to Mr. Chen Shunli (note 33 to the financial statements). The revenue and operating profit relating to this segment are disclosed in note 4 to the financial statements.

The gain on disposal of the discontinued operations of approximately RMB23,710,000, which represents the difference between the sales proceeds and the Group's share of net assets of the subsidiary together with negative goodwill previously taken directly to reserve to the extent it has not previously been realised in the income statement.

7. PROFIT BEFORE TAXATION

Profit before taxation is stated after crediting and charging the following:

	Group	
	2001	2000
	RMB'000	*RMB'000*
Crediting		
Net exchange gain	**—**	373
Charging		
Auditors' remuneration	**1,114**	1,245
Cost of inventories sold#	**413,133**	370,221
Cost of construction contract income	**24,267**	11,590
Staff costs		
— Basic salaries and allowances	**12,346**	10,062
— Pension scheme contribution	**425**	537
Depreciation		
— Owned assets	**41,675**	33,721
— Leased assets	**230**	76
Operating lease rentals		
— Office premises	**619**	258
— Plant	**580**	—
Loss on disposal of fixed assets	**13**	87
Net exchange loss	**390**	—

Cost of inventories sold includes staff costs of approximately RMB5,847,000 (2000: RMB6,418,000) and depreciation charge of approximately RMB34,329,000 (2000: RMB29,446,000) that have been included in the respective total amounts disclosed above.

8. DIRECTORS' AND SENIOR EXECUTIVES' EMOLUMENTS

(a) Directors' emoluments

The emoluments of the Company's directors disclosed pursuant to Section 161 of the Companies Ordinance are as follows:

	2001	2000
	RMB'000	*RMB'000*
Fees for executive and non-executive directors	**—**	—
Other emoluments for executive directors		
— basic salaries and allowances	**4,104**	1,754
— discretionary bonuses	**1,230**	—
— contributions to pension schemes	**31**	2
— gratuity on termination of service contract	**1,126**	—
Other emoluments for independent non-executive directors		
— basic salaries and allowances	**40**	—
	6,531	1,756

None of the directors waived any emoluments during the year. No incentive payment was paid or payable to any directors during the year.

The emoluments of the directors were within the following bands:

i) Executive directors

		Number of directors	
RMB	**Equivalent HK$**	**2001**	2000
Nil — 1,060,700	Nil — 1,000,000	**3**	4
1,060,701 — 1,591,050	1,000,001 — 1,500,000	**—**	1
1,591,051 — 2,121,400	1,500,001 — 2,000,000	**1**	—
4,242,801 — 4,773,150	4,000,001 — 4,500,000	**1**	—
		5	5

ii) Independent non-executive directors

		Number of directors	
RMB	**Equivalent HK$**	**2001**	2000
Nil — 1,060,700	Nil — 1,000,000	**3**	3

8. DIRECTORS' AND SENIOR EXECUTIVES' EMOLUMENTS (continued)

(b) Five highest-paid individuals

The five individuals whose emoluments were the highest in the Group for the year include two (2000: four) executive directors whose emoluments are reflected in the analysis presented above. The emoluments payable to these five individuals during the year are as follows:

	2001	2000
	RMB'000	*RMB'000*
Basic salaries and allowances	**5,014**	1,779
Discretionary bonuses	**1,230**	—
Contributions to pension schemes	**58**	3
Gratuity on termination of service contract	**1,126**	—
	7,428	1,782

The emoluments fell within the following bands:

		Number of individuals	
RMB	**Equivalent HK$**	**2001**	2000
Nil — 1,060,700	Nil — 1,000,000	**3**	4
1,060,701 — 1,591,050	1,000,001 — 1,500,000	**—**	1
1,591,051 — 2,121,400	1,500,001 — 2,000,000	**1**	—
4,242,801 — 4,773,150	4,000,001 — 4,500,000	**1**	—
		5	5

During the year, no emolument was paid to the five highest-paid individuals (all senior executives including directors) as inducement to join or upon joining the Group.

9. TAXATION

	Group	
	2001	2000
	RMB'000	*RMB'000*
Mainland China enterprise income tax	**23,951**	24,776
Hong Kong profits tax	**—**	—
	23,951	24,776

No Hong Kong profits tax was provided for as the Group had no assessable profits arising in Hong Kong (2000: Nil). Provision for taxation by subsidiaries operating in Mainland China has been calculated at the rates applicable, based on existing laws, interpretations and practice, during the year.

Notes to the Financial Statements

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9. TAXATION (continued)

In accordance with the applicable enterprise income tax law of Mainland China, Heshun (China) Industrial Group Co., Ltd. ("Heshun China") and Fujian Shunda Polyester Fibre Co., Ltd. ("Fujian Shunda"), as wholly foreign-owned enterprises incorporated in Fuzhou Coastal Economic Open Zone, are exempt from the enterprise income tax ("EIT") for the first two profitable years of operations after offsetting prior year losses and are entitled to a 50% reduction on the EIT for the following three years. Heshun China and Fujian Shunda began their first profitable year in the year ended 31 December 1997 and were entitled to a 50% reduction on EIT, at an effective tax rate of 12% for the years from 1999 to 2001.

Heshun (Fujian) Spandex Co., Ltd. ("Heshun Spandex") is an equity joint venture established in Mainland China in 2000. In accordance with the applicable EIT law of Mainland China, Heshun Spandex is exempt from the EIT for the first two profitable years of operations after offsetting prior year losses and is entitled to a 50% reduction on the EIT for the following three years. Heshun Spandex is still at its development stage and hence has no assessable profit since its establishment.

During the year, the Group had no significant deferred taxation (2000: Nil).

10. PROFIT ATTRIBUTABLE TO SHAREHOLDERS

The consolidated profit attributable to shareholders included a loss of approximately RMB21,867,000 (2000: RMB4,164,000) dealt with in the financial statements of the Company.

11. EARNINGS PER SHARE

The calculation of basic earnings per share for the year ended 31 December 2001 is based on the profit attributable to shareholders of approximately RMB143,680,000 (2000: RMB182,421,000) and 1,860,000,000 (2000: weighted average of 1,454,700,000) ordinary shares in issue during the year.

No diluted earnings per share is presented as there were no dilutive potential shares in existence during the years ended 31 December 2000 and 2001.

12. DIVIDENDS

The directors do not recommend the payment of a dividend for the year ended 31 December 2001 (2000: Nil).

13. GOODWILL

	Group	
	2001	2000
	RMB'000	*RMB'000*
Beginning of year	**—**	—
Arising from acquisition of further interest in a subsidiary	**2,403**	—
Impairment charge	**(2,403)**	—
End of year	**—**	—

Notes to the Financial Statements

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14. FIXED ASSETS

Group

	2001					2000
	Land and buildings	Machinery	Motor vehicles	Other equipment	Total	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Cost						
Beginning of year	125,483	627,547	4,743	2,273	760,046	704,827
Acquisition of a subsidiary	—	—	—	—	—	15,389
Transfer from construction in progress *(Note 15)*	—	237,760	—	—	237,760	—
Additions	27,480	2,784	537	108	30,909	40,047
Disposal of discontinued operations	(1,908)	(14,806)	—	(498)	(17,212)	—
Disposals	—	—	(16)	—	(16)	(217)
End of year	151,055	853,285	5,264	1,883	1,011,487	760,046
Accumulated depreciation						
Beginning of year	10,472	105,821	1,762	474	118,529	84,862
Charge for the year	5,196	35,097	953	659	41,905	33,797
Disposal of discontinued operations	(350)	(3,431)	—	(401)	(4,182)	—
Disposals	—	—	(3)	—	(3)	(130)
End of year	15,318	137,487	2,712	732	156,249	118,529
Net book value						
End of year	135,737	715,798	2,552	1,151	855,238	641,517
Beginning of year	115,011	521,726	2,981	1,799	641,517	619,965

14. FIXED ASSETS (continued)

Company

	2001			2000
	Motor vehicles	**Other equipment**	**Total**	Total
	RMB'000	***RMB'000***	***RMB'000***	*RMB'000*
Cost				
Beginning of year	**1,162**	**593**	**1,755**	—
Additions	**62**	**45**	**107**	1,755
Disposals	**(16)**	**—**	**(16)**	—
End of year	**1,208**	**638**	**1,846**	1,755
Accumulated depreciation				
Beginning of year	**76**	**34**	**110**	—
Charge for the year	**235**	**221**	**456**	110
Disposals	**(3)**	**—**	**(3)**	—
End of year	**308**	**255**	**563**	110
Net book value				
End of year	**900**	**383**	**1,283**	1,645
Beginning of year	**1,086**	**559**	**1,645**	—

Land and buildings are outside Hong Kong and held on lease terms of between 10 to 50 years. Land and buildings with net book value of approximately RMB108,232,000 (2000: RMB82,539,000) and machinery of approximately RMB305,209,000 (2000: Nil) were pledged as securities for borrowings from banks and financial institutions.

The net book value of a motor vehicle held by the Company under finance lease amounted to approximately RMB840,000 (2000: RMB1,070,000).

15. CONSTRUCTION-IN-PROGRESS

	Group	
	2001	2000
	RMB'000	*RMB'000*
Beginning of year	**238,100**	—
Additions	**91,444**	238,100
Transfer to fixed assets *(Note 14)*	**(237,760)**	—
End of year	**91,784**	238,100

16. PREPAYMENTS FOR FIXED ASSETS

	Group	
	2001	2000
	RMB'000	*RMB'000*
Beginning of year	**169,712**	—
Additions	**132,210**	169,712
End of year	**301,922**	169,712

17. INVESTMENTS IN SUBSIDIARIES

	Company	
	2001	2000
	RMB'000	*RMB'000*
Unlisted equity interests, at cost	**452,070**	452,070
Due from subsidiaries	**222,156**	208,505
Due to subsidiaries	**(21,179)**	—
	653,047	660,575

The directors are of the opinion that the underlying value of investments in subsidiaries is not less than the carrying value as at 31 December 2001.

The balances due from/(to) subsidiaries are unsecured, non-interest bearing and not repayable within the next twelve months.

17. INVESTMENTS IN SUBSIDIARIES (continued)

The following is a list of the subsidiaries as at 31 December 2001:

Name of subsidiaries	Place of incorporation	Percentage of equity interest attributable to the Group (i)	Capital Authorised/ Registered	Capital Paid up	Principal activities
Heshun Technology Holdings Limited	British Virgin Islands	100%	US$50,000	US$1	Investment holding
Central Harvest Holdings Ltd.	Hong Kong	100%	HK$121,000,000	HK$99,900,000	Investment holding
Central Harvest International Trading Ltd.	Hong Kong	100%	HK$10,000	HK$10,000	General trading
Heshun (China) Industrial Group Co., Ltd.	Mainland China	100%	US$38,000,000	US$38,000,000	Production and sales of polyester filaments
Fujian Shunda Polyester Fibre Co., Ltd.	Mainland China	100%	US$18,000,000	US$18,000,000	Production and sales of polyester filaments
Heshun (Fujian) Spandex Co., Ltd.	Mainland China	75%	US$31,050,000	US$5,253,736	Production and sales of spandex filaments

(i) The shares of Heshun Technology Holdings Limited are held directly by the Company. The shares and equity interests of other subsidiaries are held indirectly.

(ii) The Group increased the effective equity interest in Heshun Spandex from 52% to 75% during the year ended 31 December 2001.

(iii) Of the subsidiaries incorporated in Mainland China, Heshun China and Fujian Shunda are wholly foreign-owned enterprises and Heshun Spandex is a sino-foreign equity joint venture.

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18. INVESTMENT IN AN ASSOCIATE

	Group 2001 RMB'000	2000 RMB'000
Investment (unlisted), at cost	—	45,536
Share of losses	—	(22)
Share of net assets	—	45,514
Less: Provision for impairment in value	—	(9,600)
	—	35,914
Due from an associate	—	34,389
	—	70,303
Due to an associate	—	(143,029)
	—	(72,726)

The balance due from/(to) an associate is unsecured, non-interest bearing and not repayable within the next twelve months.

During the year, the Group disposed of the entire interest in the associate to a director, Mr. Chen Shunli, the details of the transaction are set out in note 33 to the financial statements.

The following was the details of the associate as at 31 December 2000:

Name	Date and place of incorporation/ establishment	Indirect equity held	Capital Registered	Capital Paid up	Principal activities
Changle City Shunshi Group Co. Ltd. ("Changle Shunshi")	23 February 1998 Mainland China	20%	RMB227,680,000	RMB227,680,000	Investment holding

18. INVESTMENT IN AN ASSOCIATE (continued)

Supplementary financial information of the associate:

	RMB'000
Balance sheet at 31 December 2000	
Fixed assets, net	220,266
Current assets	170,633
Current liabilities	(163,327)
	227,572
Income statement	
Net loss for the year ended 31 December 2000	108

19. INVENTORIES

	Group	
	2001	2000
	RMB'000	*RMB'000*
Raw materials	**11,635**	9,417
Work-in-progress	**9,089**	2,050
Finished goods	**4,317**	5,580
	25,041	17,047

All the inventories are stated at cost.

20. DUE FROM A DIRECTOR

	Group	
	2001	2000
	RMB'000	*RMB'000*
Mr. Chen Shunli		
Balance at end of year	**56,000**	—
Balance at beginning of year	**—**	—
Maximum outstanding balance during the year	**76,000**	—

The amount represents the balance of proceeds receivable from disposal of Dalian Huayang, the details of which are set out in note 33 to the financial statements. The amount is repayable within 6 months from the date of completion of the disposal.

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21. DUE FROM CUSTOMERS FOR CONSTRUCTION WORK

	Group	
	2001	2000
	RMB'000	*RMB'000*
Contract costs incurred	**—**	14,454
Recognised profits less recognised loss	**—**	6,814
	—	21,268
Progress payment	**—**	(18,404)
	—	2,864

22. ACCOUNTS RECEIVABLE

The sales of the individual companies of the Group, except for Dalian Huayang, are usually settled by "delivery upon payment" and credit terms up to 30 days. The credit terms of Dalian Huayang granted to the customers are governed by the contracts but usually not exceeding 365 days. The aging analysis of accounts receivable was as follows:

	Group	
	2001	2000
	RMB'000	*RMB'000*
Within 30 days	**48,991**	8,360
Over 30 days but within 180 days	**—**	31,229
Over 180 days but within 360 days	**—**	641
	48,991	40,230

23. DEPOSITS, PREPAYMENTS AND OTHER RECEIVABLES

Deposits, prepayments and other receivables represents mainly the deposits for utilities and the purchase of raw materials.

24. ACCOUNTS PAYABLE

	Group	
	2001	2000
	RMB'000	*RMB'000*
Within 1 year	**21,351**	11,315
Over 1 year but within 2 years	**1,799**	2,132
Over 2 years	**425**	253
	23,575	13,700

25. TAXES PAYABLE

	Group	
	2001	2000
	RMB'000	*RMB'000*
Mainland China EIT	**11,672**	14,764
Mainland China value-added tax	**4,997**	17,489
	16,669	32,253

26. SHORT-TERM BORROWINGS

	Group		Company	
	2001	2000	**2001**	2000
	RMB'000	*RMB'000*	***RMB'000***	*RMB'000*
Bank loans	**236,951**	251,280	**—**	—
Trust receipt loans	**30,707**	—	**—**	—
Bills payable	**14,800**	—	**—**	—
Bank overdrafts				
— Secured	**6,139**	—	**—**	—
— Unsecured	**217**	—	**217**	—
Other loans, unsecured	**15,100**	10,100	**—**	—
	303,914	261,380	**217**	—

26. SHORT-TERM BORROWINGS (continued)

Bank loans, trust receipt loans, bills payable and secured bank overdrafts were secured by:

- Land and buildings with net book value of approximately RMB103,760,000 (2000: RMB77,832,000).
- Guarantees issued by the Water Supply Company of Changle City, Changle Shunshi, a director and a related company.
- Machinery of approximately RMB103,050,000 (2000: Nil).
- Properties owned by a related company.

27. OBLIGATION UNDER FINANCE LEASE

	Group and Company			
	Minimum lease payments		Present value of minimum lease payment	
	2001	2000	**2001**	2000
	RMB'000	*RMB'000*	***RMB'000***	*RMB'000*
Amount payable under finance lease				
Within one year	**313**	626	**303**	555
In the second to fifth years inclusive	**—**	313	**—**	303
	313	939	**303**	858
Less: Future finance charges	**(10)**	(81)	**N/A**	N/A
Present value of lease obligations	**303**	858	**303**	858

The lease term is 2 years. For the year ended 31 December 2001, the average effective borrowing rate was approximately 12% (2000: 12%) per annum. Interest rates are fixed at the contract date. All leases are on a fixed repayment basis and no arrangements have been entered into for contingent rental payments.

28. LONG-TERM BORROWINGS

	Group	
	2001	2000
	RMB'000	*RMB'000*
Bank loans:		
Amount due within one year or on demand	**90,785**	493
Amount due in the second year	**610**	568
Amount due in the third to fifth years	**605**	1,178
	92,000	2,239
Loans from other financial institutions		
Amount due within one year or on demand	**27,872**	—
	119,872	2,239
Amount due within one year or on demand included under current liabilities	**(118,657)**	(493)
	1,215	1,746

i) The bank loans were secured by land and buildings with net book value of approximately RMB4,472,000 (2000: RMB4,707,000) and machinery with net book value of approximately RMB146,364,000 (2000: Nil) and guarantees issued by the Company, Central Harvest Holdings Limited and a director.

Included in the bank loans is a syndicated loan of approximately RMB90,217,000. On 10 January 2002, Mr Chen Shunli, a director and one of the guarantors of the loan, was involved in a personal civil litigation. This led to a breach of certain terms of the loan agreement. As a result, the loan has become technically repayable on demand and has been re-classified as a current liabilitiy.

ii) The loans from other financial institutions were secured by machinery with net book value of approximately RMB55,795,000 (2000: Nil) and guarantees issued by the Company, Central Harvest Holdings Limited and a director.

The loan agreements of these loans contain certain financial convenants. The publication of these financial statements discloses the fact that the Group has not complied with the financial convenants which give rise to defaults. As a consequence, the loans have become technically repayable on demand and have been re-classified as current liabilities.

29. DUE TO A MINORITY SHAREHOLDER

The amount due to a minority shareholder is unsecured, non-interest bearing and not repayable within the next twelve months.

30. DUE TO A DIRECTOR

The amount due to a director, Mr. Chen Shunli is unsecured, non-interest bearing and not repayable within the next twelve months.

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31. SHARE CAPITAL

	2001 Number of shares '000	**Nominal value HK$'000**	**Nominal value RMB'000 Equivalent**	2000 Number of shares '000	Nominal value HK$'000	Nominal value RMB'000 Equivalent
Authorised (ordinary shares of HK$0.10 each)						
Beginning of year	**5,000,000**	**500,000**	**530,350**	—	—	—
Incorporation of the Company (i)	**—**	**—**	**—**	1,000	100	106
Increase in authorised share capital (ii)	**—**	**—**	**—**	4,999,000	499,900	530,244
End of year	**5,000,000**	**500,000**	**530,350**	5,000,000	500,000	530,350
Issued and fully paid (ordinary shares of HK$0.10 each)						
Beginning of year	**1,860,000**	**186,000**	**197,290**	—	—	—
Issue of shares upon incorporation (i)	**—**	**—**	**—**	1,000	—	—
Issue of shares arising from the Reorganisation ((i) and (ii))	**—**	**—**	**—**	1,000	200	212
Issue of shares through a public offering and placing (iii)	**—**	**—**	**—**	465,000	46,500	49,322
Capitalisation of share premium (iv)	**—**	**—**	**—**	1,393,000	139,300	147,756
End of year	**1,860,000**	**186,000**	**197,290**	1,860,000	186,000	197,290

Notes:

(i) On 28 June 2000, the Company was incorporated with an authorised share capital of HK$100,000, divided into 1,000,000 shares of HK$0.10 each. 1,000,000 shares were issued at nil paid. On 25 September 2000, these 1,000,000 shares were credited as fully paid at par.

(ii) On 25 September 2000, the authorised share capital of the Company was increased from HK$100,000 to HK$500,000,000, by the creation of 4,999,000,000 shares of HK$0.10 each ranking pari pasu with the existing shares in all respects. On 25 September 2000, 1,000,000 shares were credited as fully paid at par.

(iii) On 9 November 2000, 465,000,000 share of HK$0.10 each were issued at HK$0.50 per share through a public offering and placing (the "New Issue"), resulting in net cash proceeds of approximately RMB212,788,000.

(iv) Immediately after the New Issue, share premium of approximately RMB147,756,000 (HK$139,300,000) was capitalised for the issuance of 1,393,000,000 shares of HK$0.10 each on pro-rata basis to the Company's shareholders before the New Issue.

32. RESERVES

Group

	Share premium RMB'000	Statutory reserve fund RMB'000	Statutory surplus reserve RMB'000	Staff welfare fund RMB'000	Merger reserve RMB'000	Currency translation reserve RMB'000	Retained profits/ (accumulated losses) RMB'000	Total RMB'000
Balance as at 31 December 1999	—	22,980	—	—	—	—	192,358	215,338
Premium on issue of shares	197,290	—	—	—	—	—	—	197,290
Share issuance expenses	(33,825)	—	—	—	—	—	—	(33,825)
Transfer from retained profits to statutory reserves	—	18,443	2,123	1,061	—	—	(21,627)	—
Capitalisation of share premium	(147,756)	—	—	—	—	—	—	(147,756)
Waivers of amount due to a director	—	—	—	—	—	—	104,904	104,904
Negative goodwill	—	—	—	—	—	—	3,548	3,548
Effect of the Reorganisation	—	—	—	—	(212)	—	—	(212)
Profit attributable to shareholders	—	—	—	—	—	—	182,421	182,421
Translation adjustments	—	—	—	—	—	1,125	—	1,125
Balance as at 31 December 2000	15,709	41,423	2,123	1,061	(212)	1,125	461,604	522,833
Disposal of a subsidiary	—	—	(2,123)	(1,061)	—	—	3,184	—
Negative goodwill released on disposal of a subsidiary	—	—	—	—	—	—	(3,548)	(3,548)
Transfer from retained profits to statutory reserves	—	16,571	—	—	—	—	(16,571)	—
Profit attributable to shareholders	—	—	—	—	—	—	143,680	143,680
Balance as at 31 December 2001	15,709	57,994	—	—	(212)	1,125	588,349	662,965
Attributable to								
At 31 December 2001								
The Company and subsidiaries	15,709	57,994	—	—	(212)	1,125	588,349	662,965
At 31 December 2000								
The Company and subsidiaries	15,709	41,423	2,123	1,061	(212)	1,125	461,626	522,855
Associate	—	—	—	—	—	—	(22)	(22)
	15,709	41,423	2,123	1,061	(212)	1,125	461,604	522,833

32. RESERVES (continued)

Company

	Share premium *RMB'000*	Contributed surplus *RMB'000*	Accumulated losses *RMB'000*	Total *RMB'000*
Balance as at 31 December 1999	—	—	—	—
Premium on issue of shares	197,290	—	—	197,290
Share issuance expenses	(33,825)	—	—	(33,825)
Capitalisation of share premium	(147,756)	—	—	(147,756)
Loss for the year	—	—	(4,164)	(4,164)
Effect of the Reorganisation	—	451,858	—	451,858
Balance as at 31 December 2000	15,709	451,858	(4,164)	463,403
Loss for the year	—	—	(21,867)	(21,867)
Balance as at 31 December 2001	15,709	451,858	(26,031)	441,536

Mainland China laws and regulations require the Group's Mainland China companies to provide for certain statutory funds, namely, reserve fund and staff welfare fund, which are appropriated from the net profit as reported in the statutory accounts but before dividend distribution. They are required to allocate 10% of their net profit to reserve fund until the balance of such fund has reached 50% of their registered capital. The reserve fund can only be used, upon approval by the relevant authority, to offset accumulated losses or increase capital. Appropriation to staff welfare fund is at the discretion of the directors. Since the dates of establishment, respective companies now comprising the Group have not appropriated any profit to the staff welfare fund.

The merger reserve of the Group represents the difference between the amount of the capital of the subsidiaries at the date on which they were acquired by the Company and the nominal amount of the Company's share issued as consideration for the acquisition.

The contributed surplus of the Company represents the difference between the nominal value of the ordinary shares issued by the Company and the net asset value of subsidiaries acquired through an exchange of shares pursuant to the Reorganisation.

The Company's reserves as at 31 December 2001 available for distribution to shareholders are represented by the contributed surplus of approximately RMB451,858,000 (2000: RMB451,858,000) less accumulated losses of approximately RMB26,031,000 (2000: RMB4,164,000).

33. RELATED PARTY TRANSACTIONS

(a) During the year, the Group had the following material transactions with related parties:

(i) On 5 July 2001, Heshun China entered into an agreement to dispose of its entire 20% equity interest in Changle Shunshi to a director, Mr. Chen Shunli for a consideration of approximately RMB35,914,000. The consideraton was arrived at based on arm's length negotiation with reference to the net asset value of Changle Shunshi. There were no gain or loss derived by the Group in this transaction. The consideration was satisfied by setting off and discharging the amount due to Changle Shunli. The details of the transaction was set out in the circular dated 30 July 2001.

On the same date, Central Harvest Holdings Limited entered into an agreement to acquire 35% equity interest in Heshun Spandex from Changle Shunshi for a consideration of RMB1. The consideration was arrived at based on arm's length negotiation with reference that Central Harvest Holdings Limited assuming the capital contribution obligations of Changle Shunshi in relation to the 35% equity interest to the registered capital of Heshun Spandex of US$31,050,000. The details of the transaction was set out in the same circular dated 30 July 2001.

Mr. Chen Shunli held 40% and three other directors, Mr. Huo Shizhi, Mr. Chan Guoli and Mr. Xiao Tiangnan held another 40% in total of the registered capital of Changle Shunshi before completion of this transaction.

(ii) On 29 November 2001, Heshun China entered into an agreement to dispose of its entire 95% equity interest in Dalian Huayang to a director, Mr. Chen Shunli for a consideration of RMB76,000,000. The consideration was arrived at based on arm's length negotiation with reference to the net book value of Dalian Huayang. The Group realised a gain of RMB23,710,000 on this transaction. Partial consideration of RMB20,000,000 was satisfied by setting off and discharging the amount due to Changle Shunshi and the balance of RMB56,000,000 shall be settled by Mr. Chen Shunli within 6 months from completion and is included in current assets. The details of the transaction was set out in the circular dated 12 December 2001.

(b) During the year ended 31 December 2000, Mr. Chen Shunli waived the amount of approximately RMB104,904,000 due to him.

(c) The balances with related parties were as follows:

	Group	
	2001	2000
	RMB'000	*RMB'000*
Due from an associate *(Note 18)*	**—**	34,389
Due to an associate *(Note 18)*	**—**	143,029
Due from a director *(Note 20)*	**56,000**	—
Due to a minority shareholder *(Note 29)*	**52,723**	—
Due to a director *(Note 30)*	**10,748**	—

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34. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

(a) Reconciliation of profit before taxation to net cash inflow from operating activities:

	Group	
	2001	2000
	RMB'000	*RMB'000*
Profit before taxation	**167,368**	202,458
Share of loss of associate	**—**	22
Depreciation	**41,905**	33,797
Loss on disposal of fixed assets	**13**	87
Impairment of goodwill	**2,403**	—
Gain on disposal of discontinued operations	**(23,710)**	—
Interest income	**(134)**	(164)
Interest expenses	**25,200**	23,702
(Increase)/decrease in inventories	**(8,855)**	6,026
Increase in accounts receivable	**(30,629)**	(28,341)
Decrease/(increase) in prepayments and other assets	**3,569**	(2,978)
Decrease in accounts payables, prepayments from customers and other liabilities	**(21,653)**	(27,492)
Net cash inflow from operating activities	**155,477**	207,117

34. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (continued)

(b) Analysis of changes in financing during the year was as follows:

Group

	Share capital and share premium	Advance from related parties	Due to a director	Due to a minority shareholder	Finance lease	Bills payable	Bank and other loans	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Balance as at 31 December 1999	1,070	54,216	—	—	—	—	285,835	341,121
Inception of finance lease	—	—	—	—	1,146	—	—	1,146
Advance from related parties	—	158,258	—	—	—	—	—	158,258
Waivers of an amount due to a director	—	(104,904)	—	—	—	—	—	(104,904)
New loans raised	—	—	—	—	—	—	8,841	8,841
Repayment of loans	—	—	—	—	(288)	—	(31,057)	(31,345)
Shares acquired from the then shareholder	(1,070)	1,070	—	—	—	—	—	—
Proceeds from issue of new shares	246,613	—	—	—	—	—	—	246,613
Expenses for issue of new shares	(33,825)	—	—	—	—	—	—	(33,825)
Balance as at 31 December 2000	212,788	108,640	—	—	858	—	263,619	585,905
New loans raised	—	—	—	—	—	14,800	189,271	204,071
Repayment of loans	—	(3)	10,748	—	—	—	(80,967)	(70,222)
Capital element of finance lease rental payments	—	—	—	—	(555)	—	—	(555)
Reclassification	—	(52,723)	—	52,723	—	—	—	—
Set off with consideration receivable from:								
— disposal of a subsidiary	—	(20,000)	—	—	—	—	—	(20,000)
— disposal of an associate	—	(35,914)	—	—	—	—	—	(35,914)
Balance as at 31 December 2001	212,788	—	10,748	52,723	303	14,800	371,923	663,285

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34. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (continued)

(c) Purchase of a subsidiary

	2001	2000
	RMB'000	*RMB'000*
Net assets acquired		
Fixed assets, net	—	15,389
Inventories	—	9,455
Accounts receivable	—	12,911
Prepayments and other assets	—	17,134
Cash and cash equivalents	—	21,998
Accounts payable and accruals	—	(26,704)
Taxes payable	—	(1,448)
	—	48,735
Minority interests	—	(2,437)
	—	46,298
Negative goodwill	—	(3,548)
Satisfied by cash	—	42,750

The subsidiary acquired in 2000 contributed approximately RMB3,974,000 to the Group's net operating cash flows and RMB2,000 in respect of the net returns on investments and servicing of finance, paid approximately RMB1,048,000 in respective of taxation for that year.

Analysis of the net outflow of cash and cash equivalents in respect of the purchase of a subsidiary.

	2001	2000
	RMB'000	*RMB'000*
Cash consideration	—	42,750
Cash and cash equivalents acquired	—	(21,998)
Net outflow of cash and cash equivalents in respect of the purchase of a subsidiary	—	20,752

34. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (continued)

(d) Disposal of a subsidiary

	2001	2000
	RMB'000	*RMB'000*
Net assets disposed of:		
Fixed assets	**13,030**	—
Inventories	**861**	—
Accounts receivable	**21,868**	—
Deposits, prepayments and other receivables	**10,795**	—
Accounts payable	**(1,114)**	—
Other payable and accruals	**(5,793)**	—
Cash and bank deposits	**19,151**	—
Taxes payable	**(21)**	—
Minority interests	**(2,939)**	—
	55,838	—
Less: Negative goodwill released on disposal	**(3,548)**	—
Gain on disposal *(Notes 4 & 6)*	**23,710**	—
	76,000	—
Satisfied by:		
Due from a director	**56,000**	—
Set off with amount due to Changle Shunshi	**20,000**	—
	76,000	—

Analysis of the net outflow of cash and cash equivalents in respect of the disposal of a subsidiary.

	2001	2000
	RMB'000	*RMB'000*
Cash and cash equivalents disposed of with the subsidiary	**19,151**	—
Net outflow of cash and cash equivalents in respect of the disposal of a subsidiary	**19,151**	—

34. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (continued)

(e) Major non-cash transactions

(i) In 2001, the Group disposed of its entire 20% interest in Changle Shunshi for approximately RMB35,914,000 to Mr. Chen Shunli. The consideration was satisfied by way of setting off and discharging the amount due to Changle Shunshi.

(ii) In 2001, the Group disposed of Dalian Huayang to Mr. Chen Shunli for RMB76,000,000. The consideration was satisfied by setting off and discharging the amount of RMB20,000,000 due to Changle Shunshi and the amount of RMB56,000,000 due from a director.

(iii) In 2000, an amount of approximately RMB104,904,000 due to a director was waived by the director. The said amount was credited to the retained earnings.

35. COMMITMENTS

(a) Capital Commitments

As at 31 December 2001, the capital commitments of the Group and the Company in respect of purchase of land and buildings and machinery were as follows:

	Group		Company	
	2001	2000	**2001**	2000
	RMB'000	*RMB'000*	***RMB'000***	*RMB'000*
Contracted but not provided for				
— Machinery	**556,154**	358,444	**—**	—
— Land and buildings	**258,576**	146,996	**—**	—
	814,730	505,440	**—**	—
Authorised but not contracted for	**—**	121,263	**—**	—
	814,730	626,703	**—**	—

35. COMMITMENTS (continued)

(b) Operating lease commitments

Total commitments payable under non-cancellable operating lease agreements are analysed as follows:

Group

	Plant		Premises		Total	
	2001	2000	**2001**	2000	**2001**	2000
	RMB'000	*RMB'000*	***RMB'000***	*RMB'000*	***RMB'000***	*RMB'000*
Amount payable						
— within one year	**580**	1,389	**675**	675	**1,255**	2,064
— between one year and two years	**580**	580	**450**	675	**1,030**	1,255
— between two years and five years	**1,160**	1,740	**—**	450	**1,160**	2,190
	2,320	3,709	**1,125**	1,800	**3,445**	5,509

Company

	Premises	
	2001	2000
	RMB'000	*RMB'000*
Amount payable		
— within one year	**675**	675
— between one year and two years	**450**	675
— between two years and five years	**—**	450
	1,125	1,800

36. CONTINGENT LIABILITIES

As at 31 December 2001, the Company had issued guarantees of approximately RMB226 million (2000: Nil) to bankers to secure general banking facilities granted to certain subsidiaries of which approximately RMB184 million was utilised at 31 December 2001 (2000: Nil).

37. EMPLOYEE SHARE OPTIONS

The Company has a share option scheme, under which it may grant options to employees of the Group (including executive directors of the Company) to subscribe for shares in the Company, subject to a maximum of 10% of the nominal value of the issued share capital of the Company from time to time, excluding for this purpose shares issued on the exercise of options. The subscription price will be determined by the Company's board of directors, and will not be less than the higher of the nominal value of the shares and 80% of the average of the closing prices of the shares quoted on the Stock Exchange on the five trading days immediately preceding the date of offer of the options. No options have been granted since the adoption of the share option scheme.

Notes to the Financial Statements

31 December 2001

38. RETIREMENT SCHEME

The Group joined Mandatory Provident Fund Schemes ("the Schemes") for Hong Kong employees. Contributions to the Schemes (not more than HK$1,000) are based on 5% of the relevant income of the relevant staff in accordance with the requirements of the Mandatory Provident Fund Schemes Ordinance and related guidelines. Contribution paid or payable to the Schemes are charged to the income statements.

The employees of the Group's subsidiaries in Mainland China are members of a state-sponsored retirement plan operated by the local government in Mainland China and these subsidiaries make mandatory contributions to the state-sponsored retirement plan to fund the employees' retirement benefits. The retirement contributions paid by the Mainland China subsidiaries are based on 19% of the basic salary of its employees in accordance with the relevant regulations in Mainland China and are charged to the income statement as incurred. The Group discharges its retirement obligations upon payment of the retirement contributions to the state-sponsored retirement plan operated by the local government in Mainland China.

Details of the pension contribution made by the Group were as follows:

	2001	2000
	RMB'000	*RMB'000*
Contributions to retirement scheme	**456**	539

39. POST BALANCE SHEET EVENTS

(a) Included in the current portion of long-term borrowings is a syndicated bank loan of approximately RMB90,217,000. One of the guarantors of the loan is Mr Chen Shunli, a director of the Company. On 10 January 2002, Mr Chen was involved in a personal civil litigation. This led to a breach of certain terms of the deed of guarantee which in turn led to a breach of certain terms of the loan agreement. As a result, the loan has become technically repayable on demand and has been re-classified as current liabilities.

(b) Included in the current portion of long-term borrowings are two term loans in an aggregate amount of approximately RMB27,872,000. Their loan agreements contain certain financial covenants. The publication of these financial statements discloses the fact that the Group has not complied with the covenants which give rise to defaults. As a consequence, the loans have become technically repayable on demand and have been re-classified as current liabilities.

40. COMPARATIVE FIGURES

On 25 September 2000, the Company became the holding company of the other companies comprising the Group pursuant to a group reorganisation ("the Reorganisation"). The Reorganisation involved companies under common control, and the Company and its subsidiaries resulting from the Reorganisation are regarded as a continuing group. Accordingly, the Reorganisation has been accounted for on the basis of merger accounting, under which the consolidated income statement and cash flow statement for the year ended 31 December 2000 were prepared as if the Company had been the holding company of the other companies comprising the Group throughout that year, rather than from the date on which the Reorganisation was completed.

Certain comparative figures in 2000 have been reclassified to conform with the current year's presentation.