

Report of the Directors

The directors have pleasure in presenting their annual report and the audited financial statements for the year ended 31st December, 2003.

PRINCIPAL ACTIVITIES

The Company acts as an investment holding company.

The Group is principally engaged in the manufacturing of polishing compounds and polishing wheels in Mainland China under its own brand name "*Pme*" and the trading of different types of industrial abrasive products in Hong Kong and Mainland China.

Details of the activities of the principal subsidiaries of the Company are set out in note 33 to the financial statements.

SEGMENT INFORMATION

An analysis of the Group's turnover, revenue and segment information for the year ended 31st December, 2003 is set out in note 5 to the financial statements.

RESULTS AND APPROPRIATIONS

The results of the Group for the year ended 31st December, 2003 are set out in the consolidated income statement on page 22 of the annual report.

During the year, final dividend of HK1.125 cents per share (totaling HK\$9,000,000) and special dividend of HK0.375 cent per share (totaling HK\$3,000,000) for the year ended 31st December, 2002 have been approved and paid to the shareholders of the Company.

An interim dividend of HK0.3 cent per share (totaling HK\$2,400,000) for the year ended 31st December, 2003 was paid to the shareholders during the year.

The directors now recommend the payment of a final dividend of HK1.25 cents per share (totaling HK\$12,000,000) to the shareholders on the register of members on 28th May, 2004.

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 pages 57 and 58 of the annual report.

FIXED ASSETS

During the year, the Group spent approximately HK\$8.4 million on leasehold land and buildings and plant and machinery to improve its production facilities. The Group revalued its self-occupied leasehold land and buildings at 31st December, 2003 and there was no material change arising from the revaluation.

Details of the movements in the fixed assets of the Group during the year are set out in note 14 to the financial statements.

SHARE CAPITAL

Details of the movements in the share capital of the Company for the year ended 31st December, 2003 and up to the date of this report together with the reasons therefore, are set out in notes 23 and 32 to the financial statements.

SHARE PREMIUM AND RESERVES

Under the Companies Law (Revised) Chapter 22 of the Cayman Islands, the share premium of the Company is available for paying distributions or dividends to shareholders subject to the provisions of its Memorandum or Articles of Association and provided that immediately following the distribution or dividend the Company is able to pay its debts as they fall due in the ordinary course of business.

At the balance sheet date, in the opinion of the directors, the Company's reserves available for distribution to shareholders amounted to HK\$135,828,000.

Movements in the share premium and reserves of the Company for the year ended 31st December, 2003 are set out in note 25 to the financial statements. Movements in the share premium and reserves of the Group for the year ended 31st December, 2003 are set out on pages 25 and 26 of the annual report.

SHARE OPTION SCHEME

The Company operates a share option scheme for the purposes to enable the directors of the Company to grant options to certain full-time employees (including executive directors, non-executive directors and independent non-executive directors of the Company) of the Group in recognition of their contributions to the Group. Summary of the terms of the share option scheme are set out in note 24 to the financial statements.

No share option has been offered and/or granted to any participants since the adoption of the share option scheme.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's Articles of Association or the laws of the Cayman Islands.

Report of the Directors (Continued)

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

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

MAJOR CUSTOMERS AND SUPPLIERS

The aggregate sales attributable to the Group's largest customer and the five largest customers taken together accounted for approximately 9 per cent and 27 per cent respectively of the Group's total turnover for the year.

The aggregate purchases attributable to the Group's largest supplier and the five largest suppliers taken together accounted for approximately 13 per cent and 31 per cent respectively of the Group's total purchases for the year.

None of the directors, chief executive, their associates, or any shareholder (which to the knowledge of the directors owns more than 5 per cent of the Company's share capital) has any interest in the Group's five largest customers and suppliers.

USE OF PROCEEDS FROM ISSUE OF NEW SHARES

The proceeds from the issue of new shares of the Company in connection with the listing of the Company's shares on The Stock Exchange of Hong Kong Limited (the "Stock Exchange") on 13th November, 2002, after deduction of related expenses, amounted to approximately HK\$23.6 million. Part of the net proceeds has been applied as follows:

- as to approximately HK\$8 million to improve the production facilities of Dongguan PME Polishing Materials & Equipments Co., Ltd. and the technical application center of the Group;
- as to approximately HK\$2.5 million to expand the Group's sales and marketing network and set up representative office in the PRC;
- as to approximately HK\$5 million to reduce the Group's bank borrowings; and
- as to approximately HK\$4.6 million as general working capital of the Group.

The remaining balance of the net proceeds of approximately HK\$3.5 million, which has been placed with licensed banks in Hong Kong as at 31st December, 2003, will be applied in accordance with the plans set out in the Company's prospectus dated 31st October, 2002.

Report of the Directors (Continued)

DIRECTORS

The directors of the Company during the year ended 31st December, 2003 and up to the date of this report were:

Executive directors

Mr. Cheng Kwok Woo, *Chairman*

Mr. Cheng Kwong Cheong, *Vice Chairman and CEO*

Ms. Cheng Wai Ying

Mr. Chow Yin Kwang

Ms. Chan Yim Fan

Mr. Chung Kam Fai Raymond (re-designated on 28th May, 2003)

Non-executive directors

Mr. Zheng Jin Hong

Mr. Charles Woo (resigned on 19th April, 2004)

Independent non-executive directors

Mr. Anthony Francis Martin Conway (appointed on 28th May, 2003)

Mr. Li Kin Kent (appointed on 28th May, 2003)

Mr. Chow Chun Kwong (resigned on 28th May, 2003)

Mr. Chung Kam Fai Raymond (re-designated on 28th May, 2003)

In accordance with Article 87(1) of the Company's Articles of Association, Mr. Chow Yin Kwang and Ms. Chan Yim Fan shall retire from offices by rotation in the forthcoming annual general meeting, and being eligible, offer themselves for re-election.

In accordance with Article 86(3) of the Company's Articles of Association, Messrs. Anthony Francis Martin Conway and Li Kin Kent shall retire from offices in the forthcoming annual general meeting, and being eligible, offer themselves for re-election.

The biographic details of the directors are set out on pages 11 and 12 of the annual report.

DIRECTORS' SERVICES CONTRACTS

Except for Mr Chung Kam Fai Raymond, each of the executive directors has entered into a service agreement with the Company for an initial term of three years commencing from 1st October, 2002, and will continue thereafter until terminated by not less than three months' notice in writing served by either party on the other. Mr. Chung Kam Fai Raymond has entered into a service agreement with the Company for an initial term of three years commencing from 28th May, 2003, and will renew for one year thereafter until terminated by not less than three months' notice in writing served by either party on the other.

Saved as disclosed above, no director proposed for re-election at the forthcoming annual general meeting has a service contract with the Company which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

Report of the Directors (Continued)

MANAGEMENT CONTRACTS

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.

RELATED PARTY TRANSACTIONS

Details of the related party transactions during the year are set out in note 31 to the financial statements.

DIRECTORS' INTERESTS IN COMPETING BUSINESS

None of the directors have any interest in competing business to the Group.

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES

At 31st December, 2003, the directors and chief executive of the Company have the following interests and short positions in shares, underlying shares and debentures of the Company or any associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) as recorded in the register required to be kept under section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO and the Model Code for Securities Transactions by Directors of Listed Companies ("Model Code"), were as follows:

Long positions in the ordinary shares of the Company:

Directors	Number of shares held			Percentage of interests
	Personal interests	Corporate interests	Total interests	
Mr. Cheng Kwok Woo	54,400,000	358,328,000 <i>(note)</i>	412,728,000	51.59%
Mr. Cheng Kwong Cheong	54,400,000	358,328,000 <i>(note)</i>	412,728,000	51.59%
Ms. Cheng Wai Ying	54,400,000	358,328,000 <i>(note)</i>	412,728,000	51.59%
Ms. Chan Yim Fan	8,205,333	–	8,205,333	1.03%
Mr. Charles Woo	16,342,667	–	16,342,667	2.04%

Note: These shares are held by PME Investments (BVI) Co., Ltd. ("PME Investments"), a company incorporated in the British Virgin Islands (the "BVI"). The entire issued share capital of PME Investments is beneficially owned as to one-third by each of Mr. Cheng Kwok Woo, Mr. Cheng Kwong Cheong and Ms. Cheng Wai Ying.

Report of the Directors (Continued)

Save as disclosed above, none of the directors, chief executive and their associates had any interests or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations, within the meaning of Part XV of the SFO, as recorded in the register kept by the Company under Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO and the Model Code.

DIRECTORS' AND CHIEF EXECUTIVE'S RIGHTS TO ACQUIRE SHARES OR DEBENTURES

Saved as disclosed under the heading "Directors' and Chief Executive's Interests and Short Positions in Shares, Underlying Shares and Debentures" above, at no time during the year were rights to acquire benefits by means of acquisition of shares in or debentures of the Company granted to any directors, chief executive, or their respective spouse or minor children, or were any such rights exercised by them; or was the Company or any of its holding company, or subsidiaries a party to any arrangement to enable the directors or chief executive to acquire such rights in any other corporate.

SUBSTANTIAL SHAREHOLDERS AND OTHER PERSONS' INTERESTS AND SHORT POSITIONS IN SHARES AND UNDERLYING SHARES

At 31st December, 2003, in accordance with the register of the substantial shareholders kept by the Company under Section 336 of the SFO, or to be disclosed under the provisions of Divisions 2 and 3 of Part XV of the SFO and the Rules Governing the Listing of Securities on the Stock Exchange ("Listing Rules"). The following persons were interested (including short positions) in the shares or underlying shares of the Company:

Long positions in the ordinary shares of the Company:

Name	Number of shares held	Percentage of interests
PME Investments (<i>note 1</i>)	358,328,000	44.79%
Mr. Cheng Kwok Woo (<i>note 2</i>)	412,728,000	51.59%
Mr. Cheng Kwong Cheong (<i>note 2</i>)	412,728,000	51.59%
Ms. Cheng Wai Ying (<i>note 2</i>)	412,728,000	51.59%
Ms. Tsang Sui Tuen (<i>note 3</i>)	412,728,000	51.59%
Ms. Wan Kam Ping (<i>note 4</i>)	412,728,000	51.59%
Mr. Cheng Yau Kuen (<i>note 5</i>)	412,728,000	51.59%

Report of the Directors (Continued)

Notes:

1. PME Investments is an investment holding company incorporated in the BVI and its entire issued share capital is beneficially owned as to one-third by each of Mr. Cheng Kwok Woo, Mr. Cheng Kwong Cheong and Ms. Cheng Wai Ying.
2. Each of Mr. Cheng Kwok Woo, Mr. Cheng Kwong Cheong and Ms. Cheng Wai Ying personally holds 54,400,000 shares of the Company, being approximately 6.8% of the entire issued share capital of the Company. Each of them is further beneficially interested in one-third of PME Investments and is accordingly deemed to be interested in the entire interests of PME Investments in the Company.
3. Ms. Tsang Sui Tuen is the spouse of Mr. Cheng Kwok Woo and is accordingly deemed to have interest in 412,728,000 shares of the Company that Mr. Cheng Kwok Woo has interest in.
4. Ms. Wan Kam Ping is the spouse of Mr. Cheng Kwong Cheong and is accordingly deemed to have interest in 412,728,000 shares of the Company that Mr. Cheng Kwong Cheong has interest in.
5. Mr. Cheng Yau Kuen is the spouse of Ms. Cheng Wai Ying and is accordingly deemed to have interest in 412,728,000 shares of the Company that Ms. Cheng Wai Ying has interest in.

Saved as disclosed above, no other parties were recorded in the register required to be kept under Section 336 of the SFO as having an interest or a short position in the shares or underlying shares of the Company as at 31st December, 2003.

POST BALANCE SHEET EVENTS

Details of the significant post balance sheet events of the Group are set out in note 32 to the financial statements.

CODE OF BEST PRACTICE

In the opinion of the directors, the Company has complied throughout the year with the Code of Best Practice (the "Code") as set out in Appendix 14 to the Rules Governing the Listing of Securities on the Stock Exchange through out the year, except that the current independent non-executive directors of the Company are not appointed for specific terms as required by the Code, but are subject to retirement by rotation and re-election in accordance with the Company's Articles of Association.

AUDIT COMMITTEE

The Company has an audit committee which was established in accordance with the requirements of the Code for the purposes of reviewing and providing supervision over the financial reporting process and internal controls of the Group. The audit committee comprises two independent non-executive directors of the Company.

AUDITORS

A resolution to re-appoint Messrs. Deloitte Touche Tohmatsu as auditors of the Company will be proposed at the forthcoming annual general meeting.

On behalf of the Board

Cheng Kwok Woo

Chairman

Hong Kong, 21st April, 2004