

MANAGEMENT DISCUSSION AND ANALYSIS

RESULTS PERFORMANCE

During the period, revenue of the Group was HK\$88,140,000 (the corresponding period in 2005: HK\$6,061,000), representing an increase of 13.5 times compared with the corresponding period last year. Due to the completion of the first phase of Suifenhé project located across the border of the PRC and Russia, most of the revenue generated from the pre-sale in 2005 has been recognised as revenue during the period. As a result, profit attributable to shareholders of the Group in the first half of 2006 increased to HK\$40,890,000, a growth of 3.5 times as compared to 2005 (the corresponding period in 2005: HK\$9,179,000). Earnings per share rose to HK4.94 cents (2005: HK1.11 cents). The Board resolved not to declare the payment of interim dividend for the six months ended 30 June 2006.

MARKET REVIEW

Russia

Underpinned by the climbing oil price over the recent years and the existing support of a financially stable government, Russian economy continued to boost with a substantial growth in its domestic consumption. As at July 2006, the Gross Domestic Product ("GDP") of Russia grew to 7.4%, representing an increase of 1% as compared to 6.4% for the corresponding period last year. In addition, the Russian government has lifted its GDP target in 2006 from 6.4% to 6.6%. Based on the figures provided by Bloomberg News, the stock market capitalisation of Russia reached a record high of US\$946.2 billion and the RTS Index in Russia surged 88% over the past 12 months, indicating the satisfactory performance of the overall economy in Russia.

Having long and established history and deep-rooted traditional culture, the PRC and Russia are two largest neighbouring countries and have strategically built a stable relationship in terms of political affairs. Given a proven track record of economic cooperation, they are highly supportive of each other economically. Throughout these years, the cross-boundary trade between these two countries experienced rapid development.

According to the Ministry of Commerce of the PRC, export trade between the PRC and Russia in 2005 reached US\$29.01 billion, representing a sharp increase of 37.1% as compared to 2004. The PRC has become one of the largest trading partners of Russia. The PRC's investment in Russia from January to September 2005 amounted to US\$368 million, doubling the amount in 2004.

For the first eleven months in 2005, cross-border trade between the PRC and Russia reached US\$5.13 billion with a year-on-year growth rate of 35%, representing 20% of the total trade in Russia. The Sino-Russian import and export trade through the land port of Suifenhe for the year 2005 also exceeded US\$2.5 billion, the highest among all the Sino-Russian trading land ports, contributing to a robust economic growth in the region.

Hong Kong

In the first half of 2006, Hong Kong's economy displayed strong growth momentum. Real GDP growth recorded 5.2% in the second quarter as compared to the corresponding period last year. With the continual improvement in the employment market, trading of the property market resumed its activeness.

Due to continuous limited land supply for luxury residential development, demand for residential property is in excess of supply, which stimulated property prices to increase. The number of property transactions rises gradually, with the most spectacular performance in the luxury residential property sector. Demand for luxury residential properties on the Hong Kong Island has always been in excess of supply, and it is expected that the supply of luxury residential properties in the second half of 2006 will be inadequate. As demand for these properties will remain high, prices of luxury residential properties will continue to bolster an upward trend.

BUSINESS REVIEW

During the period under review, the Group strategically focused on the development of international real estate and investment business by actively exploring opportunities in overseas markets. Under the new direction for business development, the Group will strive to enhance its competitiveness so as to capture potential opportunities ahead.

PROJECT DEVELOPMENT

“Suifenhe-Pogranichny Cross-border Trade Zone”

The Suifenhe Shimao development project is located at the commercial and tourist development zone across the national boundary of the PRC and Russia with a total site area of approximately 4.53 sq. km., of which two-thirds is within the Russian territory. The project is located at the largest Sino-Russian land checkpoint for trade and close to Nakhodka, the Far East free economic zone. Having a railway and two highways connecting directly to Russia, it is strategically located with various geographical competitive edges. The project is positioned as the first of its kind across the Sino-Russian border, and through the

exchange of documents between the PRC and Russia, the project is recognised as the first independent trade zone by integrating all trading, logistics, modern industry, business, exhibition, entertainment and leisure and travelling activities. This has brought significant effect to the economy and trade between the PRC and Russia. Capitalising on the highly correlated competitive edges of the PRC and Russia economies, the project will develop into an extensive and energetic trade zone with various traders and enormous potential cross-border opportunities.

During the period under review, Shimao International and its Russian partner have jointly developed a large-scale comprehensive commercial project, namely Sino-Russian "Suifenhe-Pogranichny Cross-border Trade Zone". The project, located at the Municipality of Suifenhe, Heilongjiang Province, commenced its formal operation on 16 August 2006 and the first phase of construction has already been completed.

The first phase of construction includes Shimao International Commercial and Exhibition Centre (Phase 1) and Holiday Inn Suifenhe. These two projects are the landmarks of "Suifenhe-Pogranichny Cross-border Trade Zone".

- *Shimao International Commercial and Exhibition Centre*

The four-storeyed Shimao International Commercial and Exhibition Centre (Phase 1) has a total site area and a total gross floor area of approximately 38,000 sq. m. and 83,000 sq. m., respectively, offering around 1,800 shops suitable for wholesale, retail, exhibition, food and beverage and entertainment businesses. It gathers special commodities with the PRC and Russian characteristics and acts as the best platform for cross-boundary trading.

- *Holiday Inn Suifenhe*

Holiday Inn Suifenhe is the first five-star hotel in the region. It has a total site area and a total gross floor area of 33,924 sq. m. and 49,000 sq. m., respectively. The eight-storeyed building comprises one basement floor and seven floors above the ground level. The hotel is designed by a renowned U.S. design company, and will be managed by the globally renowned hotel group InterContinental Hotels Group. The hotel offers approximately 300 guest rooms and comprehensive ancillary facilities, including a magnificent café, Chinese and western restaurants, ballrooms, multifunctional conference rooms, swimming pools, entertainment centres and business centres, etc. The hotel has also commenced trial operation on 16 August 2006. Because of the less costly labour force in the region, the hotel has been able to lower its operating cost. The Group is highly optimistic about the future prospects of this hotel.

The Baltic Pearl Project

The Group intended to participate in the property investment and development of the Baltic Pearl Project in St. Petersburg of Russia and despatched relevant circular to the Company's shareholders during the period.

The Baltic Pearl Project is a large-scale project invested by the PRC enterprises in St. Petersburg of Russia. Currently, it is the largest real estate investment project of the PRC enterprises in Russia. Upon completion, it will become the largest complex with well-equipped facilities across northern Europe.

The Baltic Pearl Project is a multifunctional complex encompassing residential buildings, hotels, offices, shopping and entertainment facilities as well as convention centres with a total gross floor area of approximately 1,640,000 sq. m..

HONG KONG BUSINESS

The luxurious residential project "No. 21 Severn Road", which is wholly-owned by the Group, is located in the upmarket residential district of Severn Road, The Peak. The two four-storeyed detached houses offer a spectacular sea view and a total gross floor area of approximately 6,000 sq. ft. each. Each detached house has an area of over 6,000 sq. ft. of garden, swimming pool, sheltered parking and sightseeing elevator, plus a spectacular 180-degree sea view of the Victoria Harbour. The entire architectural and interior design seamlessly combines life style, architecture and nature. Its premier design has won the Annual Awards 2004 — Merit by the Hong Kong Institute of Architects.

PROSPECTS FOR THE SECOND HALF OF 2006

The Board is confident of the Group's future development prospects. Given the booming global economy and favourable prospects of the property industry, Shimao International has implemented a series of strategies as follows:

- actively seek development opportunities on a global level
- continue to explore new opportunities of the Group's business in Russia
- sale of the project "No. 21 Severn Road" to bring favourable returns for the Group
- enhance regional management, attract high calibre personnel and place emphasis on staff training

With the implementation of business strategies in respect of properties development and investment in international market, the Group will leverage its extensive experience in the property market to bring remarkable return for its shareholders.