

REPORT OF THE DIRECTORS

The Directors submit their report together with the audited accounts for the year ended 31st December 1998.

PRINCIPAL ACTIVITIES AND GEOGRAPHICAL ANALYSIS OF OPERATIONS

The principal activity of the Company is investment holding and the principal activities of its subsidiaries, associated companies and jointly controlled entities are set out in notes 10, 11 and 12 on pages 36 to 42.

The turnover and contribution to the Group's results attributable to each principal activity and geographical location for the year ended 31st December 1998 are as follows:—

(a) By activity

	Turnover HK\$'000	Contribution to Group's operating profit before exceptional items, associated companies, jointly controlled entities and taxation HK\$'000	Exceptional items HK\$'000	Contribution to Group's operating profit before associated companies, jointly controlled entities and taxation HK\$'000
Securities investment	307,780	2,880	—	2,880
Direct investments	46,373	(9,812)	—	(9,812)
Sales of infant products	527,492	46,581	—	46,581
Consultancy services	5,077	377	—	377
Corporate finance	5,929	5,929	—	5,929
Treasury income	17,156	7,658	—	7,658
Others	4,202	4,202	—	4,202
Provision for permanent diminution in value of long term listed and unlisted investments	—	—	(76,438)	(76,438)
Provision for minority interests	—	—	(9,038)	(9,038)
Provision for deposit paid on purchase of property	—	—	(22,341)	(22,341)
Provision for loan to China Venturetech Investment Corporation	—	—	(21,762)	(21,762)
Losses arising from trading and holding of short term listed investments	—	—	(23,072)	(23,072)
	<u>914,009</u>	<u>57,815</u>	<u>(152,651)</u>	<u>(94,836)</u>
Less: General and administrative expenses	—	(27,153)	—	(27,153)
	<u>914,009</u>	<u>30,662</u>	<u>(152,651)</u>	<u>(121,989)</u>

(b) By geographical location

Hong Kong	336,815	(11,019)	(152,651)	(163,670)
Chinese Mainland	575,347	39,517	—	39,517
Others	1,847	2,164	—	2,164
	<u>914,009</u>	<u>30,662</u>	<u>(152,651)</u>	<u>(121,989)</u>

REPORT OF THE DIRECTORS (Cont'd)

RESULTS

The results for the year are set out in the consolidated profit and loss account on page 19.

DIVIDEND

Since the Board believes that sufficient cash resources should be maintained for the time being to counteract any possible financial impact that might occur in this deflationary economic environment, no interim dividend was paid and no final dividend is recommended (1997: final dividend of HK\$0.01 per ordinary share totalling HK\$10,277,382).

RESERVES

Movements in the reserves of the Group and the Company during the year are set out in note 19 to the accounts on page 47.

FIXED ASSETS

Details of the movements in fixed assets of the Group are set out in note 9 to the accounts on pages 35 and 36.

PURCHASE, SALE OR REDEMPTION OF 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 who held office during the year and up to the date of this report were:—

Ms CHEN Wei Li	
Mr LAO Yuan Yi	
Mr JIANG Guo Fang	
Mr LU Wen Qing	
* Prof. WOO Chia Wei	
* Mr KWOK Lam Kwong, Larry	
Mr XU Wei Ming	– appointed on 16th June 1998
Mr XIN Shulin, Steve	– appointed on 16th June 1998
Mr YEUNG Wai Kin	– appointed on 16th June 1998
Mr HU Yi Ming	– appointed on 16th June 1998
Mr ZHOU Xiao He	– resigned on 16th June 1998
Mr CHOW Fu Kee, Felix	– alternate director to Mr LAO Yuan Yi

* *Independent non-executive directors*

REPORT OF THE DIRECTORS (Cont'd)

DIRECTORS (Cont'd)

Mr JIANG Guo Fang and Mr LU Wen Qing retire in accordance with the Company's articles of association, and, being eligible, offer themselves for re-election.

DIRECTORS' SERVICE CONTRACTS

None of the directors who are 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.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

Biographical details of the directors of the Company and senior management of the Group are set out as follows (with age in brackets):-

Ms CHEN Wei Li (57) Chairman. Joined the Company in 1993. Currently Chairman of China International Intellectech Corporation and China Venturetechno International Co. Ltd.

Mr LAO Yuan Yi (53) President & Managing Director. Joined the Company in 1993. Currently board member of Shenyin & Wanguo Securities Co., Ltd., Chairman of China Assets (Holdings) Limited and a director of International Enterprises Investment Company Limited. Previously senior policy researcher at China's National Research Centre for Science & Technology and Social Development, senior staff officer with the PRC State Science & Technology Commission & the PRC Railway Ministry. Mr Lao graduated from Shanghai Fudan University and obtained his master degree from Harvard University.

Mr JIANG Guo Fang (42) Director. Acquired MBA Master Degree from the Asia (Macau) International Open University. Joined the Company in 1996. Currently Executive Vice President of Shenyin & Wanguo Securities Co., Ltd. and Chairman of Shenyin Wanguo (Hong Kong) Ltd. He has over 12 years' working experience in the People's Bank of China, Shanghai Branch and the Industrial & Commercial Bank of China, Shanghai Branch. He took the position of Executive Vice President of Shanghai Shenyin Securities Co., Ltd. since 1992, and that of Shenyin & Wanguo Securities Co., Ltd. since 1996.

Mr LU Wen Qing (41) Director. Joined the Company in 1996. Currently Managing Director of International Business Division of Shenyin & Wanguo Securities Co., Ltd. and a non-executive Director of Shenyin Wanguo (Hong Kong) Ltd. He graduated from the Shanghai University of Finance and Economics. Prior to joining Shanghai Shenyin Securities Co. Ltd., he served as a senior officer in Shanghai Trust & Investment Corporation of Industrial & Commercial Bank of China and as an attaché of the Chinese Embassy in Gabon.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT (Cont'd)

Professor WOO Chia Wei (61). Appointed as Independent Non-Executive Director in 1993. Currently President of Hong Kong University of Science & Technology. Previously President, Provost, Department Chairman and Professor of several reputable universities in the United States of America. He is also an independent non-executive director of Shanghai Industrial Holdings Limited, MAE Holdings Limited and Midas Printing Group Ltd. In addition, he serves on the Commission on Strategic Development of Hong Kong Special Administrative Region of the PRC, and the Chinese People's Political Consultative Conference.

Mr KWOK Lam Kwong, Larry (43). Appointed as Independent Non-Executive Director in 1995. Mr Kwok is a practising solicitor in Hong Kong and also qualified to practise as a solicitor in Australia, England and Singapore. He is also qualified as an accountant in Hong Kong and Australia. He graduated from the University of Sydney, Australia with bachelor degrees in economics and laws respectively as well as a master degree in laws. He is currently a member of the Consumer Council, a member of the Hospital Governing Committee of the Princess Margaret Hospital, a member of the Criminal & Law Enforcement Injuries Compensation Boards and Deputy Chairman of the Consumer Goods Safety Appeal Board Panel. He is a member of the Political Consultative Committee of Guangxi of the People's Republic of China. He also serves on the boards of several Hong Kong listed companies.

Mr XU Wei Ming (52). Appointed as Director of the Company in 1998. Currently Managing Director of Shanghai Jing Long Business Co Ltd. He graduated from English Department of Shanghai Fudan University, got the Master of Arts of California State University, Sacramento in the United States. Before that, he served as a teacher in the Economic Administration Department of China Textile University.

Mr XIN Shulin, Steve (45). Appointed as Director of the Company in 1998. He joined the Company in 1994 as Executive Vice President in charge of direct investment. Previously Mr Xin worked as registered Financial Planner for Merrill Lynch and Senior Financial Analyst and Partner for Vail Securities Inc in Vail Colorado. He graduated from Lanzhou University in 1982 and obtained his MBA degree from University of Denver in 1992. Mr Xin is also a director of China Assets (Holdings) Limited and RBI Holdings Limited, the Group's associated companies which are listed on The Stock Exchange of Hong Kong Limited.

REPORT OF THE DIRECTORS (Cont'd)**BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT (Cont'd)**

Mr YEUNG Wai Kin, Rankine (37). Appointed as Director of the Company in 1998. He is also Chief Financial Officer and Company Secretary of the Company. Mr Yeung joined the Company in 1993 and has over 15 years' experience in auditing, finance and management positions. He is also a director of International Enterprises Investment Company Limited and China Assets (Holdings) Limited, the Group's associated company which is listed on The Stock Exchange of Hong Kong Limited. Mr Yeung possesses professional membership of the Association of Chartered Certified Accountants, the Hong Kong Society of Accountants and the Taxation Institute of Hong Kong.

Mr HU Yi Ming (36). Appointed as Director of the Company in 1998. He joined the First Shanghai Group in 1996 as Managing Director of its Assets Management Division. Prior to joining the First Shanghai Group, Mr Hu was Vice President – Foreign Exchange of Banque Paribas, Hong Kong Branch. Mr Hu graduated with a Bachelor of Economics degree from the Shanghai University of Finance and Economics. After his graduation, he gained extensive experience in money market dealing from several reputable corporations in PRC, USA and Singapore.

Mr ZHOU Xiao He (47) Director. Joined the Company in 1995 and resigned on 16th June 1998. Currently Managing Director of China Venturetechno International Co. Ltd. and Chairman of the China Venture Group Pte Ltd. (Singapore subsidiary). Previously Deputy Director, Strategic Research Department of the China Science & Technology Development Research Centre, the PRC State Science & Technology Commission.

Mr CHOW Fu Kee, Felix (64), was the president of the Hong Kong Society of Accountants in 1992, Chief Executive of the Hong Kong Securities Clearing Company Limited in 1989 and a senior executive of Kowloon Canton Railway Corporation for 6 years since 1982. He is an independent non-executive Director of Arts Optical International Holdings Limited, which is listed on The Stock Exchange of Hong Kong Limited. He holds a diploma from Harvard Business School for the study under its Corporate Financial Management Program and Advance Management Program, and has over 41 years' experience in management, accounting and finance in major international companies. He joined the Group in 1993 as Executive Vice President & Chief Financial Officer and is now a Consultant to the Group and Alternate Director to Mr LAO Yuan Yi.

Mr WANG Jun-Yan (29), who joined the Company in October 1997, is the Managing Director of First Shanghai Capital Limited, the Company's subsidiary. Mr Wang has 6 years' experience in securities business. He is also director of China Assets (Holdings) Limited, the Group's associated company which is listed on The Stock Exchange of Hong Kong Limited. Mr Wang graduated from Zhongshan University in 1992 specializing in International Trade. He has studied in Ph. D. program of Finance in the City University of New York.

REPORT OF THE DIRECTORS (Cont'd)

DIRECTORS' INTERESTS IN CONTRACTS

No contract of significance in relation to the Company'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.

DIRECTORS' INTERESTS IN SHARE EQUITY OR DEBT SECURITIES

At 31st December 1998, the interests of the directors in the shares, warrants and options of the Company or any of its associated corporations, as recorded in the register maintained by the Company under Section 29 of the Securities (Disclosure of Interests) Ordinance (the "SDI Ordinance") or as notified to the Company were as follows:-

Name of Directors	Number of ordinary shares in the Company		
	Family interests	Personal interests	Corporate interests
Mr Lao Yuan Yi	–	500,000	–
Mr Hu Yi Ming	–	920,000	–
Prof. Woo Chia Wei	72,000	–	–

Arrangement on share options granted to the directors are set out in note 7(b) to the accounts on page 32.

Save as disclosed above,

- (a) none of the directors (including their spouse or children under 18 years of age) of the Company had any right to subscribe for the securities of the Company, or had exercised any such right; and
- (b) at no time during the year was the Company, or any of its subsidiaries a party to any arrangements to enable the directors of the Company to acquire benefits by means of acquisition of shares in, debentures of, the Company or any other body corporate.

REPORT OF THE DIRECTORS (Cont'd)

SUBSTANTIAL SHAREHOLDERS

The register of substantial shareholders maintained under section 16(1) of the Securities (Disclosure of Interests) Ordinance shows that as at 31st December 1998, the Company had been notified of the following substantial shareholders' interests, being 10% or more of the Company's issued share capital.

<u>Name of shareholders</u>	<u>Number of ordinary shares in the Company</u>
International Enterprises Investment Company Limited	213,033,850
China Assets (Holdings) Limited	206,296,000

International Enterprises Investment Company Limited is a Hong Kong company owned equally by two Chinese Mainland companies, China Venturetech Investment Corporation and Shenyin & Wanguo Securities Co., Ltd.

China Assets (Holdings) Limited is a Hong Kong listed company which is also an associated company of the Group.

Apart from the above, so far as the directors are aware, there are no parties which were, directly or indirectly, interested in 10% or more of the Company's issued share capital of the Company as at 31st December 1998.

MANAGEMENT CONTRACTS

No contract 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.

MAJOR CUSTOMERS AND SUPPLIERS

The aggregate percentages of sales and purchases attributable to the Group's five largest customers and suppliers respectively are both less than 30% for 1998 and 1997.

EMPLOYEES

As at 31st December 1998, the Group employed 4,504 staff, out of which 4,474 are located in Chinese Mainland. Employee remuneration is performance based and is reviewed annually. In addition to basic salary payments, other staff benefits include medical schemes, defined contribution provident fund schemes and employee share option scheme. Training courses are provided to staff where necessary.

REPORT OF THE DIRECTORS (Cont'd)

GROUP'S BORROWINGS AND INTEREST CAPITALISED

Particulars of the Group's borrowings are set out in notes 17 and 21 on pages 46 and 48 respectively. No interest was capitalised by the Company or any of its subsidiaries during the year.

FIVE-YEAR FINANCIAL SUMMARY

The summary of assets, liabilities and results of the Group for the last five financial years is as follows:—

	1998	1997	1996	1995	1994
	HK\$	HK\$	HK\$	HK\$	HK\$
Total assets	1,261,502,323	1,400,985,047	566,051,627	404,834,782	412,986,425
Total liabilities (Including minority interests)	422,823,274	451,887,777	185,518,461	94,485,982	82,614,408
Total net assets	838,679,049	949,097,270	380,533,166	310,348,800	330,372,017
Turnover	914,008,502	636,126,098	147,300,465	73,353,657	97,195,197
(Loss)/profit attributable to shareholders	(143,029,322)	16,893,743	(13,876,273)	(17,371,047)	64,809,558
(Loss)/earnings per share	(13.92 cents)	2.03 cents	(3.09 cents)	(4.52 cents)	16.84 cents

The calculation of (loss)/earnings per share is based on the Group's (loss)/profit attributable to shareholders and on the weighted average number of shares in issue.

RESPONSE TO YEAR 2000 ISSUE

The Group fully realizes that certain computer software and hardware in use might not function effectively in Year 2000. Systems which use only two digits to identify the year may fail to differentiate between Year 1900 and Year 2000.

The Board of Directors has researched the potential risk to the Group's own business as well as outsiders, and has taken appropriate remedial action to preclude any potential influence of the above problem; for which a designated team with top management and computer specialist has been addressing this issue.

REPORT OF THE DIRECTORS (Cont'd)

RESPONSE TO YEAR 2000 ISSUE (Cont'd)

The Group's major business information systems and related computing equipment have undergone extensive upgrades and most of which are now Year 2000 compliant. These systems include office automation, internet and financial management systems. The accounting system is currently under final testing and implementation. In terms of percentage, approximately 98% of the computer software and hardware used by the Group that could develop the Year 2000 computer problem have either already been upgraded or replaced. The Board therefore expects that the Year 2000 Problem will completely and satisfactorily be resolved by the end of June 1999, so there will not have any significant adverse effect on the operations of the Group.

As at the date of this report, no material cost has been or expected to be incurred in relation to the resolution of the Year 2000 Problem, so the Board believes that any such costs of rectification will not have a significant impact on the Group's financial position, operation results or cash flow.

As the EDP Department is capable of implementing most of the tasks for systems upgrades, the Group only requires minimal external resources. Thus, except for the maintenance and renewal of the computerized accounting system and server operation system, the Group has not entered into any agreement or made any external commitment with any software company for this issue.

Based on our evaluation, the Company does not anticipate any threat to the continuity of its operations. Nevertheless a contingency plan, in particular of the computerized accounting system, has been developed to allow the Company to continue operating in the event of unforeseen disruptions to the operations.

COMPLIANCE WITH THE CODE OF BEST PRACTICE OF THE LISTING RULES

In the opinion of the directors, the Company has complied with the Code of Best Practice as set out in Appendix 14 of the Rules Governing the Listing of Securities on the Stock Exchange throughout the year.

REPORT OF THE DIRECTORS (Cont'd)

AUDIT COMMITTEE

The Audit Committee of the Board of Directors was established on 27th December 1998. To comply with the revised Code of Best Practice as set out in Appendix 14 of the Listing Rules, the Company has appointed the two independent non-executive directors of the Company, Prof. Woo Chia Wei and Mr Kwok Lam Kwong, Larry as members of the Audit Committee. The Audit Committee acts in an advisory capacity and make recommendations to the Board. The Audit Committee met in the late April 1999 to review the Group's 1998 final results announcement and the Annual Report before they were tabled for the Board's approval.

AUDITORS

Our auditors, Coopers & Lybrand, have merged their practice with Price Waterhouse and now practise in the name of PricewaterhouseCoopers. They have signed the auditors' report in their new name. PricewaterhouseCoopers, being eligible, offer themselves for re-appointment, and a resolution to this effect will be proposed at the Annual General Meeting.

On behalf of the Board

LAO Yuan Yi

Managing Director

Hong Kong, 29th April 1999