
THIS CIRCULAR IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION

If you are in any doubt as to any aspect of this circular or as to the action to be taken, you should consult your licensed securities dealer, bank manager, solicitor, professional accountant or other professional adviser.

If you have sold or transferred all your shares in Inner Mongolia Development (Holdings) Limited, you should at once hand this circular to the purchaser or transferee or the bank, licensed securities dealer or other agent through whom the sale was effected for transmission to the purchaser.

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INNER MONGOLIA DEVELOPMENT (HOLDINGS) LIMITED

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 279)

**MAJOR TRANSACTION —
ACQUISITION AND CONVERSION OF CONVERTIBLE NOTE**

A notice convening the EGM (as defined herein) to be held on Friday, 9 June 2006 at 9:00 a.m. at 30th Floor China United Centre, 28 Marble Road, North Point, Hong Kong is set out on pages 106 and 107 of this circular. If you are not able to attend the EGM, you are requested to complete and return the enclosed form of proxy in accordance with the instructions printed thereon to the branch share registrar of the Company, Secretaries Limited, at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong as soon as possible but in any event not less than 48 hours before the time appointed for holding the EGM. Completion and return of the form of proxy will not preclude you from attending and voting in person at the EGM or any adjournment of it should Shareholders so wish.

24 May 2006

CONTENTS

	<i>Page</i>
DEFINITIONS	1
LETTER FROM THE BOARD	3
APPENDIX I — FINANCIAL INFORMATION OF THE GROUP	11
APPENDIX II — ACCOUNTANTS' REPORT ON FINANCIAL INFORMATION OF HMIL GROUP	44
APPENDIX III — UNAUDITED PROFORMA STATEMENT OF ASSETS AND LIABILITIES OF THE ENLARGED GROUP	94
APPENDIX IV — GENERAL INFORMATION	100
NOTICE OF EGM	106

DEFINITIONS

In this circular, the following expressions have the following meanings unless the context requires otherwise:

“Agreement”	the conditional agreement dated 21 April 2006 and a supplemental agreement dated 2 May 2006 entered into between Yearwise and Equity Spin relating to the Transaction;
“Associates”	has the meaning ascribed thereto in the Listing Rules;
“Board”	the board of directors of the Company;
“Company”	Inner Mongolia Development (Holdings) Limited, a company incorporated in the Cayman Islands, the shares of which are listed on the Stock Exchange;
“Completion”	completion of the Transaction under the Agreement;
“Connected Person(s)”	the meaning ascribed thereto in the Listing Rules;
“Conversion”	the proposed exercise of conversion rights under the Convertible Note by Equity Spin to convert into shares in HMIL;
“Conversion Price”	the conversion price of the Convertible Note of HK\$0.15 per HMIL Share;
“Convertible Note”	a 8% convertible note issued by HMIL in the outstanding principal amount of HK\$131 million due on 20 September 2015, which is the subject of the sale under the Agreement;
“EGM”	the extraordinary general meeting of the Company to be held on Friday, 9 June 2006 at 9:00 a.m. at 30th Floor, China United Centre, 28 Marble Road, North Point, Hong Kong to approve matters related to the Transaction and the Conversion;
“Enlarged Group”	the Group as enlarged by the inclusion of the HMIL Group on Completion of the Conversion;
“Equity Spin”	Equity Spin Investments Limited, a wholly-owned subsidiary of the Company;
“Group”	the Company and its subsidiaries;
“HMIL”	Hennabun Management International Limited, a company incorporated in the British Virgin Islands;
“HMIL Group”	HMIL and its subsidiaries;
“HMIL Shares”	shares of par value of US\$0.01 each in HMIL;

DEFINITIONS

“Latest Practicable Date”	19 May 2006;
“Listing Rules”	the Rules Governing the Listing of Securities on the Stock Exchange;
“SFO”	the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong);
“Shareholders”	shareholders of the Company;
“Stock Exchange”	the Stock Exchange of Hong Kong Limited;
“Transaction”	the proposed acquisition of the Convertible Note pursuant to the Agreement;
“Willie International”	Willie International Holdings Limited, a company incorporated in Hong Kong, the shares of which are listed on the Stock Exchange of Hong Kong; and
“Yearwise”	Yearwise Finance Limited, a wholly-owned subsidiary of Willie International.



INNER MONGOLIA DEVELOPMENT (HOLDINGS) LIMITED

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 279)

Executive Directors

Ms Yau Shum Tek, Cindy (*Chairman*)
Mr Kwong Wai Tim, William (*Managing Director*)
Mr Lai Ming Wai
Ms Kwok Wai Ming

Registered Office

P.O. Box 309
George Town
Grand Cayman
Cayman Islands

Independent Non-executive Directors

Mr Lam Ping Cheung
Mr Lo Ming Chi, Charles
Mr Chiu Siu Po
Ms Hui Wai Man, Shirley
Mr Gary Drew Douglas

Principal place of business

in Hong Kong
31st Floor, China United Centre,
28 Marble Road, North Point,
Hong Kong

24 May 2006

To the Shareholders

Dear Sir/Madam,

**MAJOR TRANSACTION —
ACQUISITION AND CONVERSION OF CONVERTIBLE NOTE**

INTRODUCTION

On 21 April 2006, Equity Spin (a wholly-owned subsidiary of the Company) and Yearwise (a wholly-owned subsidiary of Willie International) entered into the Agreement whereby Equity Spin agreed to purchase and Yearwise agreed to sell its rights, title and interest in the Convertible Note. Equity Spin will exercise its conversion rights under the Convertible Note to convert into shares in HMIL as soon as practicable after Completion, subject to obtaining the necessary regulatory approvals, to the extent required.

The Transaction and the Conversion contemplated under the Agreement constitutes a major transaction of the Company under the Listing Rules and is subject to the approval of Shareholders at the EGM. This circular sets out the details of the Transaction and the Conversion required pursuant to Chapter 14 of the Listing Rules.

LETTER FROM THE BOARD

Terms of the Agreement

- Date: 21 April 2006 and 2 May 2006
- Parties:
- (i) Vendor: Yearwise
 - (ii) Purchaser: Equity Spin
 - (iii) Guarantor of Vendor: Willie International. To the best of the directors' knowledge, information and belief having made all reasonable enquiries, Willie International and the ultimate beneficial owners of Willie International are third parties independent of the Company.
 - (iv) Guarantor of Purchaser: The Company
- Terms: Subject to satisfaction of the Conditions described below:
- (i) Yearwise agreed to sell to Equity Spin all Yearwise's rights, title and interests in the Convertible Note for a consideration of HK\$100,000,000; and
 - (ii) the consideration shall be satisfied wholly by cash in the following manner:
 - (a) a refundable deposit of HK\$25,000,000, representing 25% of the total consideration has been paid by Equity Spin upon execution of the Agreement; and
 - (b) the balance of HK\$75,000,000 shall be paid by cash upon Completion.

The Consideration payable by Equity Spin was fixed after arm's length negotiation by Yearwise and Equity Spin having taken into account of the development of HMIL and the consolidated net asset value of HMIL after Completion.

Inner Mongolia and its subsidiaries would fund the Transaction by their internal resources.

LETTER FROM THE BOARD

Conditions: Completion of the Agreement is conditional upon the following conditions (the “Conditions”):

- (i) the Company, the ultimate holding company of Equity Spin having obtained the approval of its shareholders (as required by the Listing Rules) for the purchase of the Convertible Note as contemplated under the Agreement and the subsequent exercise of conversion rights under the Convertible Note in full by Equity Spin to convert into shares of HMIL;
- (ii) Willie International, the ultimate holding company of Yearwise having obtained the approval of its shareholders (as required by the Listing Rules) for the sale of the Convertible Note as contemplated under the Agreement;
- (iii) Equity Spin having completed and being satisfied with the results of the legal and financial due diligence on HMIL and its subsidiaries and as to status of compliance by HMIL with the terms of the Convertible Note; and
- (iv) all necessary approvals being obtained from the Securities and Futures Commission, the Stock Exchange, the Hong Kong Futures Exchange Limited and any other relevant authorities to the extent required under the relevant laws and regulations for the change in shareholding structure of Radland International Limited, CU Corporate Finance Limited, Chung Nam Commodities Limited and Chung Nam Securities Limited as a result of the purchase and conversion of the Convertible Note by Equity Spin.

If the conditions are not satisfied or waived (in the case of (iii) and (iv) above) on or before 5:00 p.m. on 17 July 2006 (or such later date as Equity Spin and Yearwise may agree) then the deposit shall be refunded without interest to Equity Spin and the Agreement shall terminate and the parties shall have no further claims against each other save for claims in respect of antecedent breaches.

Radland International Limited, CU Corporate Finance Limited, Chung Nam Commodities Limited and Chung Nam Securities Limited are all indirect wholly-owned subsidiaries of HMIL.

LETTER FROM THE BOARD

Completion: Completion shall take place on the third business day after the satisfaction or waiver of the Conditions (in the case of (iii) and (iv) above), or such other date as the parties may agree. If Completion does not take place in accordance with the Agreement, the deposit shall be refunded without interest to Equity Spin.

If Inner Mongolia waives the satisfaction of the condition set out in (iv) above and proceeds to Completion, it intends to hold the Convertible Note and exercise conversion rights thereunder after all necessary approvals from the regulatory authorities are obtained.

Terms of the Convertible Note

The terms of the Convertible Note are set out as follows:

Issuer

HMIL, currently held approximately 35.55% by Willie International as at the Latest Practicable Date.

Outstanding Principal amount of the Convertible Note

HK\$131 million

Issue Date

21 September 2005

Maturity

The Convertible Note will mature on the day immediately preceding the tenth anniversary from the date of issue. On maturity, to the extent that the Convertible Note is not redeemed or converted, HMIL will repay the Convertible Note.

Interest

The Convertible Note bears interest at 8% per annum, payable monthly.

Conversion

The outstanding principal amount of the Convertible Note may be converted into HMIL Shares by the holder of the Convertible Note in amounts or integral multiples of HK\$500,000 at any time from the date of issue up to seven days before (and excluding) the maturity date of the Convertible Note. There is no automatic conversion on maturity of the Convertible Note.

LETTER FROM THE BOARD

Conversion Price

The initial conversion price of the Convertible Note was HK\$0.25 per HMIL Share. In January 2006, the Conversion Price was adjusted to HK\$0.15 per HMIL Share as a result of an issue of HMIL Shares to third parties.

Early Redemption

The Convertible Note is redeemable at 100% of its outstanding principal amount together with accrued interest at any time from the date of issue up to seven days before (and excluding) the maturity date of the Convertible Note at the option of HMIL. To the extent that the Convertible Note is not redeemed or converted on maturity, HMIL will repay the Convertible Note.

Shares to be issued upon conversion

The HMIL Shares to be issued upon conversion of the Convertible Note will when issued rank equally in all respects among themselves and with the HMIL Shares in issue on the relevant date of conversion.

If the Convertible Note is converted in full at the Conversion Price of HK\$0.15 per HMIL Share, a total of 873,333,333 HMIL Shares will be issued. These HMIL Shares represent approximately 100.27% of the existing issued share capital of HMIL, and approximately 50.07% of the issued share capital of HMIL as enlarged by the new HMIL Shares to be issued upon conversion of the Convertible Note (assuming no further shares are issued by HMIL from the Latest Practicable Date till the date of conversion).

HMIL is indirectly held as to approximately 35.55% by Willie International and approximately 1.15% by the Company as at the Latest Practicable Date. The balance of the shareholdings in HMIL are indirectly held by eight other companies, the shares of each of which are listed on the main board of the Stock Exchange, one independent financial institution and two independent third parties.

Voting rights of holders of the Convertible Note

The holder of the Convertible Note does not have any right to attend or vote at any meetings of HMIL by virtue of it being the holder of the Convertible Note.

Transferability

The Convertible Note is transferable in authorised denominations of HK\$500,000.

LETTER FROM THE BOARD

CONVERSION OF CONVERTIBLE NOTE

Equity Spin will exercise its conversion rights in full under the Convertible Note to convert into shares in HMIL as soon as practicable after Completion subject to all necessary approvals from the regulatory authorities being obtained, to the extent required. Assuming no further shares are issued by HMIL from the Latest Practicable Date till the date of conversion and using the conversion price of HK\$0.15 per HMIL Share, the indirect shareholding of the Company in HMIL will be approximately in aggregate 50.64% of the issued share capital of HMIL as enlarged by the new HMIL shares to be issued upon conversion of the Convertible Note and HMIL will become a subsidiary of the Company. There is no restriction on the subsequent disposal of HMIL Shares by Equity Spin.

GENERAL INFORMATION

HMIL is the financial services group which the Company is considering to invest in as stated in its previous announcement dated 2 February 2006. HMIL through its subsidiaries is engaged in investment holding, provision of financial services including brokerage, commodity trading, money lending, margin financing and corporate finance advisory as well as proprietary trading and direct investment.

The shares of HMIL are not listed on any stock exchange.

The audited consolidated net losses of HMIL for the two financial years ended 31 December 2004 and 31 December 2005 were approximately HK\$421.2 million and HK\$222.6 million respectively. The net asset value of HMIL based on the unaudited management account for the period ended 28 February 2006 was approximately HK\$108.6 million. The audited net asset value of HMIL as at 31 December 2005 was approximately HK\$62.7 million.

Willie International, through various subsidiaries, is engaged in the businesses of property investments, investment in trading securities, provision of brokerage and financial services and investments in coke and related gas chemical business. Yearwise is a wholly-owned subsidiary of Willie International and an investment holding company.

The Company, through various subsidiaries, is engaged in trading of goods, provision of finance, trading of securities, property holding and investment activities. Equity Spin is a wholly-owned subsidiary of the Company and an investment holding company.

The consideration of HK\$100 million for the acquisition of the HK\$131 million Convertible Note was arrived at after arms length negotiation between Yearwise and Equity Spin and represents an effective conversion price of HK\$0.1145 per HMIL Share which represents (i) 13.37% premium to the audited net asset value per HMIL share of HK\$0.101 as at 31 December 2005; (ii) 8.4% discount to the unaudited net asset value per HMIL share of HK\$0.125 as at 28 February 2006; and (iii) 16.42% discount to the pro-forma net asset value per HMIL share of HK\$0.137 after Equity Spin fully converts the Convertible Note.

LETTER FROM THE BOARD

Based on the unaudited financial statements for the period ended 28 February 2006 of HMIL and upon the Conversion, HMIL will become a non wholly-owned subsidiary of the Company, the tangible assets of the Group will be increased by in HK\$496,823,000 the liabilities of the Group will be increased by HK\$257,191,000, and the minority interests of the Group will be increased by HK\$118,282,000.

REASONS OF AND BENEFITS FOR THE TRANSACTION

The Company is endeavouring to further develop the businesses of provision of finance, trading of securities and investment activities. The Transaction and the Conversion will enable the Company to integrate and strengthen its resources and enlarge its client base, with a view to the Company becoming a leading and sophisticated investment service advisor and finance provider in the market.

LISTING RULES IMPLICATION

The Transaction and the Conversion contemplated under the Agreement constitutes a major transaction of the Company under the Listing Rules and is therefore subject to the approval of Shareholders at the EGM.

PROCEDURES FOR DEMANDING A POLL BY SHAREHOLDERS

Article 76 of the Articles of the Company sets out the following procedure by which Shareholders may demand a poll.

At any general meeting a resolution put to the vote at the meeting shall be decided on a show of hands unless a poll is (before or on the declaration of the result of the show of hands) demanded:

- (i) by the Chairman; or
- (ii) by at least three members present in person or by proxy for the time being entitled to vote at the meeting; or
- (iii) by any member or members present in person or by proxy and representing not less than one-tenth of the total voting rights of all the members having the right to vote at the meeting; or
- (iv) by any member or members present in person or by proxy and holding shares in the Company conferring a right to vote at the meeting being shares on which an aggregate sum has been paid up equal to not less than one-tenth of the total sum paid up on all the shares conferring that right.

LETTER FROM THE BOARD

RECOMMENDATION

The Board is of the opinion that the terms of the Agreement are fair, reasonable and in the best interest of the Company and the Shareholders as a whole, and recommends you to vote in favour of the resolution to be proposed at the EGM to approve the Transaction and the Conversion.

Whether or not Shareholders are able to attend the EGM, Shareholders are requested to complete and return the enclosed form of proxy in accordance with the instructions printed thereon to the branch share registrar of the Company, Secretaries Limited, at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong as soon as possible but in any event not less than 48 hours before the time appointed for holding the EGM. Completion and return of the form of proxy will not preclude Shareholders from attending and voting in person at the EGM should Shareholders so wish.

Your attention is also drawn to the additional information set out in the appendices to this circular.

By order of the Board
Yau Shum Tek, Cindy
Chairman

1(a). Summary of Consolidated Financial Information For The Three Years Ended 31 March 2005

The following is a summary of the audited consolidated financial information of the Company for each of the three years ended 31 March 2003, 2004 and 2005 as extracted from the respective audited annual accounts of the Company.

RESULTS

	Year ended 31 March		
	2005	2004	2003
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Turnover	<u>72,238</u>	<u>23,305</u>	<u>51,493</u>
Profit (loss) before taxation	18,823	(17,054)	(43,684)
Taxation	<u>(2,504)</u>	<u>—</u>	<u>—</u>
Profit (loss) for the year	<u>16,319</u>	<u>(17,054)</u>	<u>(43,684)</u>
Attributable to			
Shareholders of the Company	16,319	(17,054)	(43,684)
Minority interests	<u>—</u>	<u>4,316</u>	<u>—</u>
	<u>16,319</u>	<u>(12,738)</u>	<u>(43,684)</u>

ASSETS AND LIABILITIES

	At 31 March		
	2005	2004	2003
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Total assets	509,986	469,230	503,438
Total liabilities	<u>(3,266)</u>	<u>(2,547)</u>	<u>(5,270)</u>
	506,720	466,683	498,168
Minority interests	<u>—</u>	<u>—</u>	<u>(37,736)</u>
Shareholders' funds	<u>506,720</u>	<u>466,683</u>	<u>460,432</u>

1(b). Audited Consolidated Financial Statements For The Year Ended 31 March 2005

The following audited financial statements of the Group are extracted from the Company's annual report for the year ended 31 March 2005.

CONSOLIDATED INCOME STATEMENT

For the year ended 31 March 2005

	<i>Notes</i>	2005 <i>HK\$'000</i>	2004 <i>HK\$'000</i>
Turnover	4	72,238	23,305
Cost of sales		<u>(41,618)</u>	<u>(2,423)</u>
Gross profit		30,620	20,882
Other operating income		244	839
Investment income	6	—	833
Administrative expenses		(12,522)	(16,718)
Other operating expenses	7	<u>(63)</u>	<u>(22,907)</u>
Profit (loss) from operations	8	18,279	(17,071)
Interest on bank overdrafts		—	(78)
Gain on disposal of subsidiaries		50	95
Share of results of an associate		<u>494</u>	<u>—</u>
Profit (loss) before taxation		18,823	(17,054)
Taxation	10	<u>(2,504)</u>	<u>—</u>
Profit (loss) before minority interests		16,319	(17,054)
Minority interests		<u>—</u>	<u>4,316</u>
Net profit (loss) for the year		<u><u>16,319</u></u>	<u><u>(12,738)</u></u>
Dividend	11	<u><u>—</u></u>	<u><u>—</u></u>
Earnings (loss) per share — basic	12	<u><u>HK0.44 cent</u></u>	<u><u>(HK0.40 cent)</u></u>

CONSOLIDATED BALANCE SHEET

At 31 March 2005

	<i>Notes</i>	2005 <i>HK\$'000</i>	2004 <i>HK\$'000</i>
Non-current assets			
Investment properties	13	5,700	5,700
Property, plant and equipment	14	606	412
Interest in an associate	16	3,614	—
Investments in securities	17	42,000	42,000
Long-term loans receivable	18	<u>212,000</u>	<u>165,616</u>
		<u>263,920</u>	<u>213,728</u>
Current assets			
Trade and other receivables	19	28,462	44,971
Short-term loans receivable	18	213,651	179,699
Deposit made on acquisition of a subsidiary	20	—	2,342
Investments in securities	17	209	272
Bank balances and cash		<u>3,744</u>	<u>28,218</u>
		<u>246,066</u>	<u>255,502</u>
Current liabilities			
Other payables		1,720	2,489
Tax payable		1,546	—
Bank overdrafts		<u>—</u>	<u>58</u>
		<u>3,266</u>	<u>2,547</u>
Net current assets		<u>242,800</u>	<u>252,955</u>
		<u>506,720</u>	<u>466,683</u>
Capital and reserves			
Share capital	23	40,211	34,811
Reserves		<u>466,509</u>	<u>431,872</u>
		<u>506,720</u>	<u>466,683</u>

BALANCE SHEET*At 31 March 2005*

	<i>Notes</i>	2005 <i>HK\$'000</i>	2004 <i>HK\$'000</i>
Non-current assets			
Property, plant and equipment	14	—	—
Interests in subsidiaries	15	<u>502,145</u>	<u>461,517</u>
		<u>502,145</u>	<u>461,517</u>
Current assets			
Other receivables		72	69
Bank balances and cash		<u>3,644</u>	<u>3,576</u>
		<u>3,716</u>	<u>3,645</u>
Current liabilities			
Other payables		1,168	1,108
Tax payable		1,495	—
Bank overdrafts		<u>—</u>	<u>58</u>
		<u>2,663</u>	<u>1,166</u>
Net current assets		<u>1,053</u>	<u>2,479</u>
Total assets less current liabilities		503,198	463,996
Non-current liability			
Amount due to a subsidiary	21	<u>903</u>	<u>904</u>
		<u>502,295</u>	<u>463,092</u>
Capital and reserves			
Share capital	23	40,211	34,811
Reserves	25	<u>462,084</u>	<u>428,281</u>
		<u>502,295</u>	<u>463,092</u>

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 March 2005

	Share capital	Share premium	Capital redemption reserve	Special reserve	Distributable reserve	Accumulated losses	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
				(note 25(a))	(note 25(c))		
THE GROUP							
At 1 April 2003	31,161	287,456	485	35,131	595,191	(488,992)	460,432
Issue of shares	3,650	15,995	—	—	—	—	19,645
Expenses incurred in connection with the issue of shares	—	(656)	—	—	—	—	(656)
Net loss for the year	—	—	—	—	—	(12,738)	(12,738)
At 31 March 2004	34,811	302,795	485	35,131	595,191	(501,730)	466,683
Issue of shares	5,400	19,080	—	—	—	—	24,480
Expenses incurred in connection with the issue of shares	—	(762)	—	—	—	—	(762)
Net profit for the year	—	—	—	—	—	16,319	16,319
At 31 March 2005	<u>40,211</u>	<u>321,113</u>	<u>485</u>	<u>35,131</u>	<u>595,191</u>	<u>(485,411)</u>	<u>506,720</u>

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 March 2005

	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
OPERATING ACTIVITIES		
Profit (loss) before taxation	18,823	(17,054)
Adjustments for:		
Investment income	—	(833)
Interest on bank overdrafts	—	78
Depreciation	186	638
Impairment loss recognised in respect of investment securities	—	11,000
Impairment loss recognised in respect of intangible asset	—	11,321
Allowance for other receivables	—	415
Allowance for amount due from an associate	—	2
Deficit arising on valuation of investment properties	—	100
(Gain) loss on disposal of property, plant and equipment	(12)	69
Unrealised loss (gain) on other investments	63	(43)
Gain on disposal of subsidiaries	(50)	(95)
Share of results of an associate	(494)	—
Operating cash flows before movements in working capital	18,516	5,598
(Increase) decrease in trade and other receivables	(26,491)	61,291
Increase in loans receivable	(80,336)	(122,416)
Decrease in investments in securities	—	2,290
(Decrease) increase in other payables	(769)	1,516
Cash used in operations	(89,080)	(51,721)
Interest paid on bank overdrafts	—	(78)
Interest received	—	833
Hong Kong Profits Tax paid	(958)	—
NET CASH USED IN OPERATING ACTIVITIES	<u>(90,038)</u>	<u>(50,966)</u>

	<i>Note</i>	2005 <i>HK\$'000</i>	2004 <i>HK\$'000</i>
INVESTING ACTIVITIES			
Settlement of proceeds from disposal of subsidiaries in prior year		43,000	—
Refund (place) of deposit made on acquisition of a subsidiary		2,342	(2,342)
Proceeds from disposal of property, plant and equipment		111	23
Proceeds from disposal of subsidiaries (net of cash and cash equivalents disposed of)	26	50	(32,222)
Amount advanced to an associate		(3,120)	(2)
Purchase of property, plant and equipment		<u>(479)</u>	<u>(131)</u>
NET CASH FROM (USED IN) INVESTING ACTIVITIES		<u>41,904</u>	<u>(34,674)</u>
FINANCING ACTIVITIES			
Issue of shares, net of expenses		23,718	18,989
Repayment of other borrowings		<u>—</u>	<u>(1,101)</u>
NET CASH FROM FINANCING ACTIVITIES		<u>23,718</u>	<u>17,888</u>
NET DECREASE IN CASH AND CASH EQUIVALENTS		(24,416)	(67,752)
CASH AND CASH EQUIVALENTS AT 1 APRIL		<u>28,160</u>	<u>95,912</u>
CASH AND CASH EQUIVALENTS AT 31 MARCH		<u>3,744</u>	<u>28,160</u>
Represented by:			
Bank balances and cash		3,744	28,218
Bank overdrafts		<u>—</u>	<u>(58)</u>
		<u>3,744</u>	<u>28,160</u>

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 March 2005

1. GENERAL

The Company is an exempted company incorporated in the Cayman Islands with limited liability. The shares of the Company are listed on The Stock Exchange of Hong Kong Limited (the “Stock Exchange”).

The Company is an investment holding company and provides corporate management services.

The activities of the Company’s principal subsidiaries are set out in note 31.

2. POTENTIAL IMPACT ARISING FROM THE RECENTLY ISSUED ACCOUNTING STANDARDS

In 2004, the Hong Kong Institute of Certified Public Accountants (the “HKICPA”) issued a number of new or revised Hong Kong Accounting Standards (“HKAS(s)”) and Hong Kong Financial Reporting Standards (“HKFRS(s)”) (hereinafter collectively referred to as “new HKFRSs”) which are effective for accounting periods beginning on or after 1 January 2005 except for HKFRS 3 “Business Combinations”. The Group has not early adopted these new HKFRSs in the financial statements for the year ended 31 March 2005.

HKFRS 3 is applicable to business combinations for which the agreement date is on or after 1 January 2005. The Group has not entered into any business combination for which the agreement date is on or after 1 January 2005. Therefore HKFRS 3 did not have any impact on the Group for the year ended 31 March 2005.

The Group has considered the potential impact of these new HKFRSs and the effect on how the results of operations and financial positions of the Group are prepared and presented as described below:

HKFRS 2 “Share-based Payment”

HKFRS 2 Share-based Payment which requires an expense to be recognised where the Group buys goods or obtains services in exchange for shares or rights over shares, or in exchange for other assets equivalent in value to a given number of shares or rights over shares. The principal impact of HKFRS 2 on the Group is in relation to the expensing of the fair value of directors’ and employees’ share options of the Company determined at the date of grant of the share options over the vesting period. Prior to the application of HKFRS 2, the Group did not recognise the financial effect of these share options until they were exercised.

*HKAS 32 “Financial Instruments: Disclosure and Presentation”**HKAS 39 “Financial Instruments: Recognition and Measurement”*

HKAS 39 requires all financial assets to be reclassified into held-to-maturity financial assets, available-for-sale financial assets, financial assets at fair value through profit or loss and loans and receivables. Available-for-sale financial assets and financial assets at fair value through profit or loss are carried at fair value, with changes in fair values recognised in equity and profit or loss respectively. Held-to-maturity financial assets and loans and receivables are measured at amortised cost using the effective interest method. Currently, the Group’s investments in securities are classified as investment securities or other investments which are measured at cost less impairment loss or at fair value respectively. The Group’s long-term and short-term loans receivables are carried at cost less impairment loss. An adjustment to the carrying amounts of these assets at 1 April 2004 is required to be made to the Group’s accumulated losses.

HKAS 40 “Investment Properties”

HKAS 40 requires all revaluation gains or losses of investment properties to be taken directly to the income statement. Investment property revaluation reserve brought forward should be transferred to retained earnings.

Currently, investment properties are measured at open market values, with revaluation surplus or deficits credited or charged to investment property revaluation reserve unless the balance on this reserve was insufficient to cover a revaluation decrease, in which case the excess of the revaluation decrease over the balance on the investment property revaluation reserve was charged to the income statement. Where a decrease had previously been charged to the income statement and revaluation subsequently arose, that increase was credited to the income statement to the extent of the decrease previously charged. As the Group does not maintain any revaluation surplus at both 1 April 2004 and 2003, the adoption of HKAS 40 will not have any impact on the Group’s results and financial position.

In relation to other new HKFRSs, the Group does not expect that the adoption will have a material effect on how the results of operations and financial position of the Group are prepared and presented.

3. SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared under the historical cost convention, as modified for the revaluation of investment properties and certain investments in securities, and in accordance with accounting principles generally accepted in Hong Kong. The principal accounting policies adopted are as follows:

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries made up to 31 March each year.

The results of subsidiaries and associate acquired or disposed of during the year are included in the consolidated income statement from the effective dates of acquisition or up to the effective date of disposal, as appropriate.

All significant inter-company transactions and balances within the Group are eliminated on consolidation.

Investments in subsidiaries

Investments in subsidiaries are included in the Company’s balance sheet at cost less any identified impairment losses.

Interests in associates

The consolidated income statement includes the Group’s share of the post-acquisition results of its associates for the year. In the consolidated balance sheet, interests in associates are stated at the Group’s share of the net assets of the associates.

Investment properties

Investment properties are completed properties which are held for their investment potential, any rental income being negotiated at arm’s length.

Investment properties are stated at their open market value based on independent professional valuation at the balance sheet date. Any revaluation surplus or deficit arising on the revaluation of investment properties is credited or charged to the investment property revaluation reserve unless the balance on this reserve is insufficient to cover a

revaluation deficit on a portfolio basis, in which case the excess of the revaluation deficit over the balance on the investment property revaluation reserve is charged to the income statement. Where a deficit has previously been charged to the income statement and a revaluation surplus subsequently arises, this surplus is credited to the income statement to the extent of the deficit previously charged.

On disposal of an investment property, the balance on the investment property revaluation reserve attributable to that property is transferred to the income statement.

No depreciation is provided on investment properties except where the unexpired term of the relevant lease is twenty years or less.

Property, plant and equipment

Property, plant and equipment are stated at cost less depreciation and any accumulated impairment losses.

Depreciation is provided to write off the cost of items of property, plant and equipment over their estimated useful lives and after taking into account their estimated residual values, using the straight line method, at the following rates per annum:

Fixtures	15% or over the terms of the relevant lease, whichever is shorter
Computer equipment	33 $\frac{1}{3}$ %
Motor vehicles	30%
Others	15%

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sale proceeds and the carrying amount of the asset and is recognised in the income statement.

Investments in securities

Investments in securities are recognised on a trade date basis and are initially measured at cost.

Investments other than held-to-maturity debt securities are classified as investment securities and other investments.

Investment securities, which are securities held for an identified long-term strategic purpose, are measured at subsequent reporting dates at cost, as reduced by any impairment loss that is other than temporary.

Other investments are measured at fair value, with unrealised gains and losses included in net profit or loss for the period.

Revenue recognition

Sales of goods are recognised when goods are delivered and title has passed.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the interest rate applicable.

Sales of investments in securities are recognised on a trade date basis.

Dividend income from investments is recognised when the Group's rights to receive payment have been established.

Impairment

At each balance sheet date, the Group reviews the carrying amounts of its tangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately.

Operating leases

Rentals payable under operating leases are charged to the income statement on a straight line basis over the terms of the relevant leases.

Retirement benefit costs

The retirement benefit costs charged in the income statement represent the contributions payable in respect of the year to the Group's Mandatory Provident Fund ("MPF") scheme.

Foreign currencies

Transactions in foreign currencies are initially recorded at the rates of exchange prevailing on the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Profits and losses arising on exchange are included in the income statement.

On consolidation, the assets and liabilities of the Group's operations are translated at exchange rates prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the period. Exchange differences arising, if any, are classified as equity and transferred to the Group's translation reserve. Such translation differences are recognised as income or as expenses in the year in which the operation is disposed of.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years, and it further excludes items that are never taxable or deductible.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill (or negative goodwill) or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

4. TURNOVER

Turnover represents the net amounts received and receivable from sales of goods, sales of securities, interest income from provision of finance and dividend income during the year, and is analysed as follows:

	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
Sales of goods	40,018	—
Sales of securities	—	801
Interest income from provision of finance	32,219	22,475
Dividend income from investments in securities		
— Hong Kong listed shares	<u>1</u>	<u>29</u>
	<u>72,238</u>	<u>23,305</u>

5. BUSINESS AND GEOGRAPHICAL SEGMENT INFORMATION

During the year, the Group was organised into five (2004: four) main operating segments: sale of goods, provision of finance, trading of securities, property holding and investment and investment activities.

During the year, a wholly-owned subsidiary of the Company, Hansom Eastern International Trading (Group) Limited, is engaged in sale of electronic products and results in a new business segment for the year.

These divisions are the basis on which the Group reports its primary segment information.

Segment information about these businesses is presented below:

Business segments

	For the year ended 31 March 2005					
	Sale of goods	Provision of finance	Trading of securities	Property holding and investment	Investment activities	Consolidated
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
SEGMENT REVENUE	<u>40,018</u>	<u>32,219</u>	<u>1</u>	<u>—</u>	<u>—</u>	<u>72,238</u>
SEGMENT RESULTS	<u>358</u>	<u>29,996</u>	<u>(75)</u>	<u>(133)</u>	<u>(274)</u>	29,872
Unallocated corporate expenses						<u>(11,593)</u>
Profit from operations						18,279
Gain on disposal of subsidiaries						50
Share of results of an associate	—	—	—	—	494	<u>494</u>
Profit before taxation						18,823
Taxation						<u>(2,504)</u>
Net profit for the year						<u>16,319</u>

At 31 March 2005

	Sale of goods	Provision of finance	Trading of securities	Property holding and investment	Investment activities	Consolidated
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
ASSETS						
Segment assets	27,951	425,658	211	5,777	42,141	501,738
Interest in an associate	—	—	—	—	3,614	3,614
Unallocated corporate assets						4,634
Consolidated total assets						<u>509,986</u>
LIABILITIES						
Segment liabilities	76	30	5	329	5	445
Unallocated corporate liabilities						2,821
Consolidated total liabilities						<u>3,266</u>

For the year ended 31 March 2005

	Sale of goods	Provision of finance	Trading of securities	Property holding and investment	Investment activities	Consolidated
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
OTHER INFORMATION						
Unrealised loss on other investments	—	—	63	—	—	63

For the year ended 31 March 2004

	Provision of finance <i>HK\$'000</i>	Trading of securities <i>HK\$'000</i>	Property holding and investment <i>HK\$'000</i>	Investment activities <i>HK\$'000</i>	Consolidated <i>HK\$'000</i>
SEGMENT REVENUE	<u>22,475</u>	<u>830</u>	<u>—</u>	<u>—</u>	<u>23,305</u>
SEGMENT RESULTS	<u>21,898</u>	<u>(1,563)</u>	<u>(1,823)</u>	<u>(23,931)</u>	(5,419)
Unallocated corporate expenses					<u>(11,652)</u>
Loss from operations					(17,071)
Interest on bank overdrafts					(78)
Gain on disposal of subsidiaries					<u>95</u>
Loss before taxation					(17,054)
Taxation					<u>—</u>
Loss before minority interests					(17,054)
Minority interests					<u>4,316</u>
Net loss for the year					<u>(12,738)</u>

At 31 March 2004

	Provision of finance <i>HK\$'000</i>	Trading of securities <i>HK\$'000</i>	Property holding and investment <i>HK\$'000</i>	Investment activities <i>HK\$'000</i>	Consolidated <i>HK\$'000</i>
ASSETS					
Segment assets	369,443	426	6,827	87,624	464,320
Unallocated corporate assets					<u>4,910</u>
Consolidated total assets					<u>469,230</u>
LIABILITIES					
Segment liabilities	30	5	1,223	25	1,283
Unallocated corporate liabilities					<u>1,264</u>
Consolidated total liabilities					<u>2,547</u>

For the year ended 31 March 2004

	Provision of finance	Trading of securities	Property holding and investment	Investment activities	Consolidated
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
OTHER INFORMATION					
Allowance for other receivables	—	—	415	—	415
Capital additions	—	—	—	131	131
Depreciation	—	—	55	583	638
Deficit arising on valuation of investment properties	—	—	100	—	100
Impairment loss recognised in respect of intangible asset	—	—	—	11,321	11,321
Impairment loss recognised in respect of investment securities	—	—	—	11,000	11,000
	<u>—</u>	<u>—</u>	<u>—</u>	<u>11,000</u>	<u>11,000</u>

Geographical segments

The Group's operations are mainly located in Hong Kong and the People's Republic of China, other than Hong Kong (the "PRC"). Over 90% of the Group's sales are in Hong Kong. Accordingly, no geographical analysis of sales is presented.

The following is an analysis of the carrying amount of segment assets, and additions to property, plant and equipment, analysed by the geographical area in which the assets are located:

	Carrying amount of segment assets		Additions to property, plant and equipment	
	2005	2004	2005	2004
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Hong Kong	460,595	422,404	479	131
The PRC	<u>45,777</u>	<u>46,826</u>	<u>—</u>	<u>—</u>
	<u>506,372</u>	<u>469,230</u>	<u>479</u>	<u>131</u>

6. INVESTMENT INCOME

	2005	2004
	HK\$'000	HK\$'000
Interest income from:		
Banks	—	634
Others	<u>—</u>	<u>199</u>
	<u>—</u>	<u>833</u>

7. OTHER OPERATING EXPENSES

	2005 <i>HK\$'000</i>	2004 <i>HK\$'000</i>
Included in other operating expenses are:		
Impairment loss recognised in respect of intangible asset	—	11,321
Impairment loss recognised in respect of investment securities	—	11,000
Unrealised loss on other investments	63	—
Deficit arising on valuation of investment properties	—	100
Allowance for amount due from an associate	—	2
Allowance for other receivables	—	415
	<u> </u>	<u> </u>

8. PROFIT (LOSS) FROM OPERATIONS

	2005 <i>HK\$'000</i>	2004 <i>HK\$'000</i>
Profit (loss) from operations has been arrived at after charging:		
Staff costs, including directors' emoluments (<i>note 9(a)</i>):		
Salaries and other benefits	6,342	6,491
MPF contributions, net of forfeited contributions HK\$10,000 (2004: HK\$134,000)	<u>220</u>	<u>100</u>
	<u>6,562</u>	<u>6,591</u>
Auditors' remuneration:		
Current year	1,080	901
Underprovision in prior year	<u>120</u>	<u>—</u>
	<u>1,200</u>	<u>901</u>
Depreciation	186	638
Loss on disposal of property, plant and equipment	—	69
and after crediting:		
Gain on disposal of property, plant and equipment	12	—
Unrealised gain on other investments	<u>—</u>	<u>43</u>

9. EMOLUMENTS OF DIRECTORS AND FIVE HIGHEST PAID INDIVIDUALS

Particulars of the emoluments of the directors and the five highest paid individuals are as follows:

(a) Directors' emoluments

	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
Fees:		
Executive directors	—	—
Independent non-executive directors	<u>303</u>	<u>240</u>
	<u>303</u>	<u>240</u>
Other emoluments:		
Executive directors		
Salaries and other benefits	3,500	4,273
MPF contributions	136	137
Independent non-executive directors	<u>—</u>	<u>—</u>
	<u>3,636</u>	<u>4,410</u>
	<u><u>3,939</u></u>	<u><u>4,650</u></u>

The emoluments of the directors are within the following bands:

	Number of directors	
	2005	2004
Nil to HK\$1,000,000	4	4
HK\$1,000,001 to HK\$1,500,000	1	1
HK\$1,500,001 to HK\$2,000,000	—	1
HK\$2,000,001 to HK\$2,500,000	<u>1</u>	<u>—</u>

(b) **Emoluments of the five highest paid individuals**

The emoluments of the five highest paid individuals of the Group for the year included three (2004: four) directors of the Company, whose emoluments are included in (a) above. The aggregate emoluments of the remaining two individuals (2004: one) are as follows:

	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
Salaries and other benefits	722	300
MPF contributions	<u>16</u>	<u>15</u>
	<u>738</u>	<u>315</u>

During the year, no emoluments were paid by the Group to the five highest paid individuals, including directors, as an inducement to join or upon joining the Group or as compensation for loss of office. In addition, none of the directors has waived any emoluments during the year.

10. TAXATION

	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
The charge comprises:		
Hong Kong Profits Tax of the Company and its subsidiaries	<u>2,504</u>	<u>—</u>

Hong Kong Profits Tax is calculated at 17.5% of the estimated assessable profit for the year.

No provision for Hong Kong Profits Tax has been made for the year ended 31 March 2004, as neither the Company nor its subsidiaries has any assessable profits for that year.

Details of deferred taxation are set out in note 22.

The tax charge for the year can be reconciled to the profit (loss) per the income statement as follows:

	2005 <i>HK\$'000</i>	2004 <i>HK\$'000</i>
Profit (loss) before taxation	<u>18,823</u>	<u>(17,054)</u>
Tax at domestic income tax rate of 17.5%	3,294	(2,984)
Tax effect of expenses not deductible for tax purposes	17	4,524
Tax effect of income not taxable for tax purposes	(41)	(183)
Tax effect of results of an associate	(87)	—
Tax effect of tax losses not recognised	105	—
Tax effect of deferred tax assets not recognised	9	562
Utilisation of tax losses previously not recognised	<u>(793)</u>	<u>(1,919)</u>
Tax charge for the year	<u><u>2,504</u></u>	<u><u>—</u></u>

11. DIVIDEND

No dividend was proposed or paid by the Company for both years.

12. EARNINGS (LOSS) PER SHARE

The calculation of the basic earnings (loss) per share for the year is based on the net profit for the year of HK\$16,319,000 (2004: loss of HK\$12,738,000) and on the weighted average of 3,741,014,456 (2004: 3,186,028,417) ordinary shares in issue.

Diluted earnings per share for the year ended 31 March 2005 has not been presented as the exercise price of the Company's outstanding share options was higher than the average market price for shares.

Diluted loss per share for the year ended 31 March 2004 has not been presented as the exercise of the Company's outstanding share options would result in a reduction in loss per share.

13. INVESTMENT PROPERTIES

THE GROUP

HK\$'000

VALUATION

At 31 March 2004 and 31 March 2005

5,700

The Group's investment properties, which are to be rented out under operating leases, are held under long-term land use rights in the PRC.

The Group's investment properties were revalued at 31 March 2005 by RHL Appraisal Ltd., an independent firm of professional property valuers, on an open market value basis at HK\$5,700,000.

14. PROPERTY, PLANT AND EQUIPMENT

	THE GROUP				THE COMPANY
	Furniture, fixtures and equipment <i>HK\$'000</i>	Computer equipment <i>HK\$'000</i>	Motor vehicles <i>HK\$'000</i>	Total <i>HK\$'000</i>	Motor vehicles <i>HK\$'000</i>
COST					
At 1 April 2004	1,203	467	837	2,507	668
Additions	388	91	—	479	—
Disposals	(728)	(111)	(169)	(1,008)	—
At 31 March 2005	<u>863</u>	<u>447</u>	<u>668</u>	<u>1,978</u>	<u>668</u>
DEPRECIATION					
At 1 April 2004	860	445	790	2,095	668
Provided for the year	126	30	30	186	—
Eliminated on disposals	(649)	(108)	(152)	(909)	—
At 31 March 2005	<u>337</u>	<u>367</u>	<u>668</u>	<u>1,372</u>	<u>668</u>
NET BOOK VALUES					
At 31 March 2005	<u>526</u>	<u>80</u>	<u>—</u>	<u>606</u>	<u>—</u>
At 31 March 2004	<u>343</u>	<u>22</u>	<u>47</u>	<u>412</u>	<u>—</u>

15. INTERESTS IN SUBSIDIARIES

	2005 <i>HK\$'000</i>	2004 <i>HK\$'000</i>
Unlisted shares, at cost	—	—
Amounts due from subsidiaries, less allowances	<u>502,145</u>	<u>461,517</u>
	<u>502,145</u>	<u>461,517</u>

The amounts due from subsidiaries are unsecured and have no fixed terms of repayment. Out of the balance at 31 March 2005, an amount of HK\$426,336,000 (2004: HK\$369,413,000) bears interest at prevailing market rate and the remaining balance is interest-free. In the opinion of the directors, the amounts will not be repayable within twelve months from the balance sheet date and are therefore shown as non-current.

Details of the Company's principal subsidiaries at 31 March 2005 are set out in note 31.

16. INTEREST IN AN ASSOCIATE

	THE GROUP	
	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
Share of net assets	494	—
Amount due from associate, less allowances	<u>3,120</u>	<u>—</u>
	<u><u>3,614</u></u>	<u><u>—</u></u>

Details of the Group's associate at 31 March 2005, which is held indirectly by the Company, are as follows:

Name of associate	Form of business structure	Place of incorporation	Attributable equity interest %	Principal activity
Equity Concept Investments Limited	Incorporated	British Virgin Islands ("BVI")	40	Securities investment

17. INVESTMENTS IN SECURITIES

	THE GROUP	
	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
Non-current investments:		
Investment securities, at cost		
Overseas unlisted shares (<i>notes</i>)	90,000	135,000
Less: Impairment losses recognised	<u>(48,000)</u>	<u>(93,000)</u>
	<u><u>42,000</u></u>	<u><u>42,000</u></u>
Current investments:		
Other investments, at market value		
Hong Kong listed shares	<u>209</u>	<u>272</u>

Notes:

The directors of the Company consider that the investment securities are held for long-term strategic purposes. Out of the cost of HK\$90,000,000 at 31 March 2005:

- (a) an amount of HK\$50,000,000 represents the Group's investment in an investee company, Hennabun Management International Limited ("HMI") (formerly known as Hennabun Management Inc.). HMI acts as an investment holding company of companies engaged in the brokerage, commodity trading, margin financing, money lending, corporate finance advisory services and proprietary trading activities.

At 31 March 2005, an impairment loss of HK\$48,000,000 (2004: HK\$48,000,000) had been recognised in the Group's investment in HMI to restate the carrying value of the investment to its estimated recoverable amount.

- (b) the other amount of HK\$40,000,000 represents the Group's investment in Xi'an Yizhiliu Pharmaceutical Co., Ltd. (西安一枝刘制药有限公司) ("Xi'an Yizhiliu"), a company established in the PRC. The investment is a 22.5% holding of the registered capital of Xi'an Yizhiliu. Xi'an Yizhiliu is not regarded as an associate of the Group as the Group is not in a position to exercise significant influence over its affairs.

18. LOANS RECEIVABLE

	THE GROUP	
	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
The loans receivable comprise:		
Unsecured long-term loans receivable	212,000	165,616
Unsecured short-term loans receivable	<u>213,651</u>	<u>179,699</u>
	425,651	345,315
Less: Amount due within one year shown under current assets	<u>(213,651)</u>	<u>(179,699)</u>
Amount due over one year	<u><u>212,000</u></u>	<u><u>165,616</u></u>

The loans receivable bear interest at prevailing market rate.

The Group negotiates credit period with borrowers according to the credit of individual borrower.

19. TRADE AND OTHER RECEIVABLES

	THE GROUP	
	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
Trade receivables (<i>note i</i>)	21,907	—
Deposit paid	6,000	—
Proceeds from disposal of subsidiaries (<i>note ii</i>)	—	43,000
Other receivables	<u>555</u>	<u>1,971</u>
	<u><u>28,462</u></u>	<u><u>44,971</u></u>

Notes:

- i. The Group allows an average credit period of 30 days to its trade customers. At 31 March 2005, all trade receivables of the Group are aged within 30 days.
- ii. The amount was fully settled during the year.

20. DEPOSIT MADE ON ACQUISITION OF A SUBSIDIARY

In March 2004, the Group entered into an agreement to acquire the entire equity interest in 深圳市方達電子產品有限公司 from two independent third parties, for an aggregate consideration of RMB3,500,000 (equivalent to approximately HK\$3,285,000). A deposit of RMB2,500,000 (equivalent to approximately HK\$2,342,000) had been paid by the Group at 31st March, 2004.

During the year, the agreement was terminated and the deposit was fully refunded.

21. AMOUNT DUE TO A SUBSIDIARY

The amount due to a subsidiary of the Company is unsecured, interest-free and has no fixed terms of repayment. Having agreed with the subsidiary, the amount will not be repayable within twelve months from the balance sheet date and is therefore shown as non-current.

22. DEFERRED TAX

At 31 March 2005, the Group has unused tax losses of HK\$44,002,000 (2004: HK\$51,729,000) available for offset against future profits. At 31 March 2004, the Company had unused tax losses of HK\$3,563,000 available for offset against future profits and has been applied to set off against assessable profit for the current year. No deferred tax asset has been recognised in respect of the tax losses due to the unpredictability of future profit streams. The tax losses may be carried forward indefinitely.

23. SHARE CAPITAL

	Number of ordinary shares	Amount HK\$'000
Ordinary shares of HK\$0.01 each		
Authorised:		
Balance at 1 April 2003, 31 March 2004 and 31 March 2005	<u>200,000,000,000</u>	<u>2,000,000</u>
Issued and fully paid:		
Balance at 1 April 2003	3,116,124,045	31,161
Issue of shares	<u>365,000,000</u>	<u>3,650</u>
Balance at 31 March 2004	3,481,124,045	34,811
Issue of shares	<u>540,000,000</u>	<u>5,400</u>
Balance at 31 March 2005	<u>4,021,124,045</u>	<u>40,211</u>

During both years, the following changes in the share capital of the Company took place:

- (i) Pursuant to a placing agreement entered into on 18 December 2003, the Company issued 215,000,000 ordinary shares of HK\$0.01 each at HK\$0.053 per share which represents a discount of approximately 7.02% to the closing price of HK\$0.057 per share on 18 December 2003 as quoted on the Stock Exchange. The net proceeds of the placement of HK\$11,034,000 was used for additional working capital of the Group.

- (ii) Pursuant to a placing agreement entered into on 30 January 2004, the Company issued 150,000,000 ordinary shares of HK\$0.01 each at HK\$0.055 per share which represents a discount of approximately 5.17% to the closing price of HK\$0.058 per share on 30 January 2004 as quoted on the Stock Exchange. The net proceeds of the placement of HK\$7,955,000 was used for additional working capital of the Group.
- (iii) Pursuant to a placing agreement entered into on 5 May 2004, the Company issued 240,000,000 ordinary shares of HK\$0.01 each at HK\$0.052 per share which represents a discount of approximately 1.89% to the closing price of HK\$0.053 per share on 5 May 2004 as quoted on the Stock Exchange. The net proceeds of the placement of HK\$12,093,000 was used for additional working capital of the Group.
- (iv) Pursuant to a placing agreement entered into on 7 January 2005, the Company issued 300,000,000 ordinary shares of HK\$0.01 each at HK\$0.040 per share which represents a discount of approximately 11.11% to the closing price of HK\$0.045 per share on 6 January 2005 as quoted on the Stock Exchange. The net proceeds of the placement of HK\$11,625,000 was used for additional working capital of the Group.

These new ordinary shares issued during the year rank *pari passu* with the then existing ordinary shares of the Company in all respects.

The new ordinary shares issued during the year were under the general mandates granted to the directors of the Company at the extraordinary general meeting held on 5 September 2003 and the annual general meeting held on 9 September 2004.

24. SHARE OPTION SCHEME

The share option scheme of the Company was approved and adopted by the shareholders at the extraordinary general meeting held on 23 August 2002 (the “2002 Scheme”). The 2002 Scheme shall be valid and effective for a period of 10 years commencing from 23 August 2002 (“the Adoption Date”). The primary purpose of the 2002 Scheme is to provide participants with the opportunity to acquire proprietary interests in the Company and to encourage participants to work towards enhancing the value of the Company and its shares for the benefit of the Company and its shareholders as a whole.

The categories of the participants under the 2002 Scheme are any directors (including executive directors, non-executive directors and independent non-executive directors) of the Company and its subsidiaries and employees of the Group and any advisors, consultants, distributors, contractors, suppliers, agents, customers, business partners, joint venture business partners, promoters, service providers to the Group who the Board of Directors of the Company (the “Board”) considers, in its sole discretion have contributed or will contribute to the Group.

The Board may, at its absolute discretion, made an offer to any participant to take up share options. An offer is deemed to have been accepted and a share option is deemed to have been granted and accepted and shall take effect when the duplicate of the offer letter comprising acceptance of the offer duly signed by the grantee and the remittance of HK\$1 by way of consideration for the grant thereof is received by the Company. Share options granted may be exercised during the period as notified by the Board to each grantee at the time of making the offer and shall be at any time from the date of grant to the tenth anniversary thereof.

The total number of shares which may be issued upon exercise of all share options granted under the 2002 Scheme and other share option scheme(s) of the Company (excluding share options lapsed) must not exceed 311,612,404 shares, being approximately 10% of the total number of the Company’s shares in issue on the Adoption Date, except with prior approvals from the Company’s shareholders. The maximum number of shares in respect of which share options may be granted to a specifically identified single grantee under the 2002 Scheme shall not (when aggregated with any shares subject to any other share option scheme(s) of the Company) in any 12-month period exceed 1% of the Company’s shares in issue. Any further grant of share options in excess of this limit is subject to shareholders’ approval in advance in a general meeting.

The subscription price for shares on the exercise of share options under the 2002 Scheme shall be determined by the Board in its absolute discretion but in any event shall not be less than the greatest of: (i) the closing price of the Company's shares as stated in the daily quotations sheets issued by the Stock Exchange on the date on which a share option is granted; (ii) the average closing price of the Company's shares as stated in the daily quotations sheets issued by the Stock Exchange for the five business days immediately preceding the date on which a share option is granted; and (iii) the nominal value of the Company's share.

The 2002 Scheme will expire on 22 August 2012.

At 31 March 2005, share options in respect of a total of 60,000,000 shares had been granted to the directors of the Company under the 2002 Scheme, representing approximately 1.49% of the issued share capital of the Company at that date and 22 July 2005, respectively. There were no share options granted to employees of the Group.

There were 60,000,000 outstanding share options as at 31 March 2004 and 31 March 2005 and all of them were granted to directors of the Company.

A summary of movements of share options held by the directors of the Company is as follows:

Date of grant	Exercisable period	Subscription price per share HK\$	Outstanding at 1.4.2003	Number of share options			
				Granted during the year	Outstanding at 31.3.2004	Granted during the year	Outstanding at 31.3.2005
16.1.2004	16.1.2004 to 15.1.2009	0.06*	—	60,000,000	60,000,000*	—	60,000,000*

* These share options were held by the relevant directors as beneficial owners.

During both years, no share options were exercised, cancelled or lapsed under the 2002 Scheme.

No charge was recognised in the income statement of the Company in respect of share options granted. Share options granted are not recognised in the financial statements until such options are exercised. Upon exercise of share options, the shares issued by the Company will be recorded as additional share capital at the nominal value of such shares and the excess of the subscription price over the nominal value of the shares issued is recorded in the Company's share premium account.

The total consideration received during the year ended 31 March 2004 for the share options granted was HK\$2.

25. RESERVES

	Share premium <i>HK\$'000</i>	Capital redemption reserve <i>HK\$'000</i>	Contributed surplus <i>HK\$'000</i> <i>(note b)</i>	Distributable reserve <i>HK\$'000</i> <i>(note c)</i>	Accumulated losses <i>HK\$'000</i>	Total <i>HK\$'000</i>
THE COMPANY						
At 1 April 2003	287,456	485	39,521	595,191	(493,421)	429,232
Issue of shares	15,995	—	—	—	—	15,995
Expenses incurred in connection with the issue of shares	(656)	—	—	—	—	(656)
Net loss for the year	—	—	—	—	(16,290)	(16,290)
At 31 March 2004	302,795	485	39,521	595,191	(509,711)	428,281
Issue of shares	19,080	—	—	—	—	19,080
Expenses incurred in connection with the issue of shares	(762)	—	—	—	—	(762)
Net profit for the year	—	—	—	—	15,485	15,485
At 31 March 2005	<u>321,113</u>	<u>485</u>	<u>39,521</u>	<u>595,191</u>	<u>(494,226)</u>	<u>462,084</u>

Notes:

- (a) The special reserve of the Group represents the difference between the aggregate amount of the share capital and share premium account of a company which was the former holding company of the Group and the nominal value of the Company's shares issued pursuant to the group reorganisation in 1992.
- (b) The contributed surplus of the Company represents the difference between the nominal value of the share capital issued by the Company and the underlying net tangible asset value net of pre-acquisition dividends and realised pre-acquisition investment property revaluation reserve of subsidiaries which were acquired by the Company pursuant to the group reorganisation in 1992.
- (c) The distributable reserve of the Group and the Company represents the aggregate of the credit arising from the following:
- (i) the reduction of nominal value of the shares from HK\$0.10 each to HK\$0.002 each by cancelling HK\$0.098 paid up on each issued share and the cancellation of share premium account as at 31 October 1998, after a transfer of HK\$607,193,000 towards the elimination of the accumulated losses of the Company at 31 October 1998; and
 - (ii) Capital reduction during the year ended 31 March 2002.

26. DISPOSAL OF SUBSIDIARIES

	2005 <i>HK\$'000</i>	2004 <i>HK\$'000</i>
Net assets disposed of:		
Property, plant and equipment	—	230
Intangible asset	—	22,641
Short-term loans receivable	—	23,949
Bank balances and cash	—	82,452
Other payables	—	(2,717)
Minority interests	—	(33,420)
	<u>—</u>	<u>(33,420)</u>
Net assets	—	93,135
Gain on disposal of subsidiaries	50	95
	<u>50</u>	<u>95</u>
	<u>50</u>	<u>93,230</u>
Satisfied by:		
Cash consideration received	50	50,230
Other receivables	—	43,000
	<u>50</u>	<u>93,230</u>
Analysis of net inflow (outflow) of cash and cash equivalents in connection with the disposal of subsidiaries:		
Cash consideration received	50	50,230
Bank balances and cash disposed of	—	(82,452)
	<u>50</u>	<u>(32,222)</u>
Net inflow (outflow) of cash and cash equivalents in connection with the disposal of subsidiaries	<u>50</u>	<u>(32,222)</u>

During the year, the Group's profit (loss) from operations included a loss of HK\$4,000 (2004: loss of HK\$12,655,000) in respect of the disposed subsidiaries up to their disposal date.

27. OPERATING LEASE COMMITMENTS

The Group as lessee

	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
Minimum lease payments paid by the Group under operating leases in respect of rented premises during the year	<u>692</u>	<u>818</u>

At the balance sheet date, the Group had commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
Within one year	256	612
In the second to fifth year inclusive	<u>404</u>	<u>—</u>
	<u>660</u>	<u>612</u>

Operating lease payments represent rentals payable by the Group for its office premises, a staff quarter and warehouse. Leases are negotiated for an average term of three years and rentals are fixed for an average of three years.

The Company did not have any significant operating lease commitments at the balance sheet date.

28. CAPITAL COMMITMENTS

	THE GROUP	
	2005	2004
	<i>HK\$'000</i>	<i>HK\$'000</i>
Capital expenditure contracted for but not provided in the financial statements in respect of acquisition of a subsidiary	<u>—</u>	<u>943</u>

The Company did not have any significant capital commitments at the balance sheet date.

29. PENSION SCHEME

The Group has operated a MPF scheme for all employees. Contributions are made based on a percentage of the employees' basic salaries and are charged to the income statement as they become payable in accordance with the rules of the scheme. The assets of the scheme are held separately from those of the Group in independently-administered funds. The Group's contributions are contributed into the scheme in accordance with the rules of the scheme.

30. POST BALANCE SHEET EVENTS

Subsequent to the balance sheet date, the following significant events took place:

- (i) On 13 June 2005, the Company put forward a share consolidation proposal pursuant to which every twenty existing shares in the issued and unissued ordinary share capital of the Company of HK\$0.01 each (the “Existing Share”) will be consolidated into one consolidated share of HK\$0.20 each (the “Consolidated Share”);
- (ii) On 13 June 2005, the Company entered into a first placing agreement with a placing agent (the “Placing Agent”) on a fully underwritten basis for the placing of 20,000,000 Consolidated Shares at a price of HK\$0.54 per share. The placing price per share represents a discount of approximately 6.9% to the closing price of HK\$0.029 per Existing Share on 3 June 2005 as quoted on the Stock Exchange (on the basis that every twenty Existing Shares is equivalent to one Consolidated Share);
- (iii) On 13 June 2005, the Company entered into a second placing agreement with the Placing Agent on a best efforts basis for the placing of 40,000,000 Consolidated Shares at a price of HK\$0.54 per share. The placing price per share represents a discount of approximately 6.9% to the closing price of HK\$0.029 per Existing Share on 3 June 2005 as quoted on the Stock Exchange (on the basis that every twenty Existing Shares is equivalent to one Consolidated Share);
- (iv) On 13 June 2005, the Company entered into a convertible notes placing agreement with the Placing Agent on a best efforts basis for the placing of convertibles notes of aggregate principal amount of up to HK\$48,000,000 at a conversion price of HK\$0.60 per Consolidated Share. The conversion price per share represents a premium of approximately 3.45% to the closing price of HK\$0.029 per Existing Share on 3 June 2005 as quoted on the Stock Exchange (on the basis that every twenty Existing Shares is equivalent to one Consolidated Share);
- (v) On 13 June 2005, the Company entered in to a conditional subscription agreement for the issue of 35,000,000 Consolidated Shares at a price of HK\$0.58 per share to Goodnews Resources Limited which is wholly-owned by Ms. Yau Shum Tek, Cindy, a director and a substantial shareholder of the Company. The subscription price per share is equal to the closing price of HK\$0.029 per Existing Share on 3 June 2005 as quoted on the Stock Exchange (on the basis that every twenty Existing Shares is equivalent to one Consolidated Share); and
- (vi) On 20 June 2005, the Company put forward a proposal to change its name from “HANSOM EASTERN (HOLDINGS) LIMITED 恒盛東方控股有限公司” to “INNER MONGOLIA DEVELOPMENT (HOLDINGS) LIMITED 內蒙發展(控股)有限公司”.

The estimated maximum net proceeds from (ii) to (v) above is approximately HK\$98,100,000 (assuming that all 40,000,000 Consolidated Shares in (iii) above and convertible notes of aggregate principal amount of HK\$48,000,000 in (iv) above are fully placed), the Company intends to utilize about half of the maximum net proceeds of approximately HK\$49,050,000 for investments and the remaining half for working capital.

All of the above events are subject to the passing of the relevant resolutions by the shareholders of the Company at the extraordinary general meeting of the Company to be held on 4 August 2005.

31. PRINCIPAL SUBSIDIARIES

Details of the Company's principal subsidiaries at 31 March 2005 are as follows:

Name of subsidiary	Place of incorporation/ registration	Nominal value of issued and fully paid ordinary share capital	Proportion of nominal value of issued share capital held by the Company		Principal activities
			Directly %	Indirectly %	
Asia Hunter Global Limited	BVI	US\$1	100	—	Investment holding
Eastern Sunny Limited	Hong Kong	HK\$2	—	100	Provision of management services
Equity Spin Investments Limited	BVI	US\$1	100	—	Investment holding
Far Hero Limited	Hong Kong	HK\$2	—	100	Property investment
Hansom Finance Limited	Hong Kong	HK\$2	—	100	Provision of finance
Longsun Ltd.	BVI	US\$1	100	—	Investment holding
Peking Bay Assets Limited	BVI	US\$1	—	100	Investment holding
Hansom Eastern International Trading (Group) Limited (formerly known as Progressive Company Limited)	Hong Kong	HK\$1,000	—	100	Sale of goods
Smart Jump Corporation	BVI	US\$1	—	100	Trading in securities
Win Advance Development Limited	Hong Kong	HK\$2	—	100	Property investment

None of the subsidiaries had any debt securities subsisting at the end of the year or at any time during the year.

The above table lists the subsidiaries of the Company which, in the opinion of the directors, principally affected the results or assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

2. STATEMENT OF INDEBTEDNESS

Borrowings

At the close of business on 30 April 2006, being the latest practicable date for the purpose of this indebtedness statement prior to the printing of this circular, the Enlarged Group had aggregate outstanding borrowings of approximately HK\$114,453,000, comprising the following:

- (i) unsecured bank overdraft of approximately HK\$776,000;
- (ii) secured bank overdraft of approximately HK\$22,967,000 (note 1);
- (iii) mortgage loan of approximately HK\$36,229,000 (note 2);
- (iv) secured margin financing provided by a financial institution of approximately HK\$1,918,000 (note 3); and
- (v) unsecured other loans of approximately HK\$52,563,000 (note 4).

Note:

- 1. The secured bank overdraft was secured by HMIL's margin clients stock.
- 2. The mortgage loan was secured by HMIL's properties.
- 3. The margin financing was secured by the Group's investment securities.
- 4. Unsecured other loans comprise of HK\$12,000,000 bearing an interest of prime rate minus 2% per annum and will mature in June 2006. HK\$40,000,000 bearing an interest of 12% per annum and will mature within twelve months from 24 March 2006 and the remaining amount of HK\$563,000 representing interest portion of the above two loans.

As at 30 April 2006, the outstanding principal amount and interest accrued on the accounts of HMIL in respect of the Convertible Note were HK\$131,000,000 and HK\$861,000 respectively. Such balance has not been separately set out above on the basis that a pro forma combined approach is adopted in the preparation of this indebtedness statement and taking into the fact that the Convertible Note will be fully converted into ordinary shares of HMIL upon Completion.

Save as aforesaid or otherwise disclosed herein, and apart from intra-group liabilities and normal trade payables, the Enlarged Group did not have any outstanding mortgages, charges, debentures or other loan capital, bank overdrafts, loans, debt securities or other similar indebtedness, liabilities under acceptances or acceptance credits, finance leases or hire purchase commitments, guarantees or other material contingent liabilities at the close of business on 30 April 2006.

Contingent liabilities

At the close of business on 30 April 2006, being the latest practicable date for the purpose of this indebtedness statement, the Enlarged Group had no material contingent liabilities.

No material changes

The directors have confirmed that there has not been any material change in the indebtedness and contingent liabilities of the Group since 30 April 2006.

3. FINANCIAL AND TRADING PROSPECTS OF THE ENLARGED GROUP

The Company, through various subsidiaries, is engaged in trading of goods, provision of finance, trading of securities, property holding and investment activities.

The Group's unaudited consolidated loss for the six months ended 30 September 2005 was HK\$546,000 and the unaudited net assets value of the Group as at 30 September 2005 was HK\$520,646,000.

As stated in the circular of the Company dated 16 February 2006, the Company is constantly reviewing its existing businesses and possible new business opportunities and has since the end of December 2005 been investigating a new investment opportunity in a financial service group which is in fact HMIL. The Company is endeavouring to further develop the businesses of provision of finance, trading of securities and investment activities. The Transaction and the Conversion will enable the Company to integrate and strengthen its resources and enlarge the client base, with a view to the Company becoming a leading and sophisticated investment service advisor and finance provider in the market.

HMIL through its subsidiaries is engaged in investment holding, provision of financial services including brokerage, commodity trading, money lending, margin financing and corporate finance advisory as well as proprietary trading and direct investment.

The audited consolidated net losses of HMIL for the two financial years ended 31 December 2004 and 31 December 2005 were approximately HK\$421.2 million and HK\$222.6 million respectively. The net asset value of HMIL based on the unaudited management account for the period ended 28 February 2006 was approximately HK\$108.6 million. The audited net asset value of HMIL as at 31 December 2005 was approximately HK\$62.7 million.

4. WORKING CAPITAL

The Directors are of the opinion that, taking into account the cash flows generated from the operating activities, the financial resources available to the Enlarged Group, including internally generated funds, the available credit facilities and the estimated net proceeds from the placings, the Enlarged Group has sufficient working capital for its present requirements, that is for at least the next 12 months from the date of this circular.

5. NO MATERIAL ADVERSE CHANGE

As at the Latest Practicable Date, the Directors are not aware of any material adverse change in the financial or trading position of the Group since 31 March 2005, the date to which the latest audited financial statements of the Company were made up.

The following sets out the text of a report received from Moores Rowland Mazars, certified public accountants, prepared for the sole purpose of inclusion in this circular.

Moores Rowland Mazars

摩斯倫·馬賽會計師事務所

24 May 2006

The Directors
Inner Mongolia Development (Holdings) Limited

Dear Sirs/ Madam,

We set out below our report on the financial information regarding Hennabun Management International Limited (“HMIL”) and its subsidiaries (hereinafter collectively referred to as the “HMIL Group”) for each of the three years ended 31 December 2003, 2004 and 2005 (the “Relevant Periods”) for inclusion in the circular of Inner Mongolia Development (Holdings) Limited (the “Company”) dated 24 May 2006 (the “Circular”) in connection with a major transaction for the proposed acquisition by the Company of a 8% convertible note issued by HMIL in the outstanding principal amount of HK\$131 million (the “Transaction”) from Willie International Holdings Limited (“Willie International”), and the Company’s intention to exercise the conversion rights of the convertible note in full to convert into shares in HMIL as soon as practicable after the completion of the Transaction.

HMIL was incorporated in the British Virgin Islands on 6 March 1996 under the name of Hennabun Management Inc. as a limited liability company. The current name of Hennabun Management International Limited was adopted on 5 January 2005 pursuant to directors’ resolution. HMIL was formerly a subsidiary of Willie International. Pursuant to various share issues to third parties during the year ended 31 December 2003, Willie International’s interests in HMIL were diluted from 93.04% to 47.6% and HMIL then became an associate of Willie International. The principal activities of HMIL Group include investment holding, the provision of brokerage and financial services.

We have audited in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”), the consolidated financial statements of the HMIL Group for the Relevant Periods, which have been prepared in accordance with the Hong Kong Financial Reporting Standard issued by HKICPA.

For the purpose of this report, we have carried out such additional procedures as are necessary in accordance with the Auditing Guideline 3.340 “Prospectuses and the Reporting Accountant” issued by the HKICPA.

The directors of HMIL are responsible for the preparation of the financial information as set out in Section A to B below (“the Financial Information”). The Financial Information as set out in this report has been prepared by the directors of HMIL based on the audited financial statements of the

HMIL Group and on the basis set out in Section A to B below, after making such adjustments as are appropriate. In preparing the Financial Information and the financial statements that intends to give a true and fair view, it is fundamental that appropriate accounting policies are selected and applied consistently.

It is our responsibility to form an independent opinion on the Financial Information.

The audit opinions issued by us on the audited financial statements of the HMIL Group for the years ended 31 December 2003, 2004 and 2005 contained qualifications concerning limitation of audit scope. The audit qualifications that remain unresolved are summarised below.

<I> Limitation of audit scope — financial statements for the year ended 31 December 2003

- (1) Included in current assets as at 31 December 2003 were loans receivable amounting to HK\$46,556,000. These loans receivable were unsecured and some of them were covered by personal guarantees provided by third parties. Of the total amount, HK\$41,206,000 were not yet due for repayment at 31 December 2003 and had not been settled up to the date of the issue of the audit report for that year. We were unable to obtain adequate external evidence to our satisfaction about the financial strength of the borrowers and the guarantors to enable us to form a view on the recoverability of the loans receivable and hence the adequacy of the provision as of 31 December 2003. These loans receivable were not repaid subsequently and were fully provided for in the year 2004.
- (2) Included in non-current assets was interest in an associate and in income statement profit on deemed disposal of interest in an associate of HK\$401,888,000 and HK\$2,500,000 respectively in respect of an associate of the HMIL Group. Audited financial information of this associate was not available.

Because of the abovementioned matter, we were unable to form a view as to whether the HMIL Group's share of the associate's net assets at 31 December 2003 was fairly stated. Any adjustments relating to the above matter that might have been found to be necessary would have a significant consequential impact on the result of the HMIL Group for the year ended 31 December 2003, including the profit on deemed disposal of interest in the associate amounting to HK\$2,500,000, and on the HMIL Group's interest in the associate at 31 December 2003.

Any adjustments in respect of the matters mentioned in (1) and (2) above would have consequential effect on the carrying amounts of HMIL's interests in subsidiaries as recorded in the HMIL's own balance sheet as at 31 December 2003.

<II> Limitation of audit scope — financial statements for the year ended 31 December 2004

- (1) As mentioned in <I>(1) above, we had not been able to form a view in the previous year on the recoverability of loans receivable of HK\$41,206,000 as at 31 December 2003 because of scope limitation. The amount concerned has been fully provided for during the year 2004. Any adjustments to the loans receivable balance as at 31 December 2003 would have consequential effect on the loss of the HMIL Group for the year ended 31 December 2004.

- (2) As mentioned in <I>(2) above, we had not been able to form a view in the previous year on the underlying value of an interest in an associate of HK\$401,888,000 as at 31 December 2003. The HMIL Group disposed of its interest in the associate during the year 2004 and recorded a loss of HK\$21,598,000 on disposal and a bad debt provision of HK\$97,389,000 on the amount due from it. Any adjustments to the underlying value of an interest in the associate as at 31 December 2003 would have consequential effect on the loss of the HMIL Group for the year ended 31 December 2004.
- (3) Included in current assets as at 31 December 2004 were loan receivables amounting to HK\$291,620,000. Of the amount, HK\$200,000,000 was unsecured and had not been settled up to the date of the issue of the audit report for that year. A director of HMIL provided to the HMIL Group a personal guarantee of HK\$200,000,000 in respect of the recoverability of such loans receivable. However, we were unable to assess the financial strength of the director to enable us to form a view on the value of his personal guarantee.

Any adjustments in respect of the matters mentioned in (1) to (3) above would have consequential effect on the carrying amounts of HMIL's interests in subsidiaries as recorded in HMIL's own balance sheet as at 31 December 2004.

<III> Limitation of audit scope — financial statements for the year ended 31 December 2005

As mentioned in <II>(3) above, we were not able to form a view in the previous year on the financial strength of a director of HMIL who had provided a personal guarantee of HK\$200,000,000 to the HMIL Group in respect of the recoverability of loans receivable amounting to HK\$291,620,000 held by two subsidiaries (the "Subsidiaries") as at 31 December 2004.

During the year, the HMIL Group disposed of the Subsidiaries at a loss. Had we been able to form a view on the recoverability of the loans receivable held by the Subsidiaries as at 31 December 2004 as mentioned in <II>(3) above, impairment loss might have been recorded in 2004. Any adjustments to loans receivable as at 31 December 2004 would have consequential effect on the loss of the HMIL Group for the year ended 31 December 2005.

In our opinion, the Financial Information gives a true and fair view of the state of affairs of the HMIL Group as at 31 December 2005.

Because of the significance of the possible effects of the limitations in audit scope in respect of the foregoing matters during the audits of the financial statements for the year ended 31 December 2003 and 2004 and we have not been able to obtain further information during our review for the purpose of this report to determine the adjustments required with respect to the limitations, for the purpose of this report, we are unable to form an opinion as to whether the Financial Information gives a true and fair view of the state of affairs of the HMIL Group as at 31 December 2003 and 2004 and of the consolidated results and cash flows of the HMIL Group for the Relevant Periods.

ACCOUNTANTS' REPORT ON HMIL GROUP

A. FINANCIAL INFORMATION

CONSOLIDATED INCOME STATEMENTS

	Note	Year ended 31 December		
		2003 HK\$'000 <i>(As restated — note 19A)</i>	2004 HK\$'000	2005 HK\$'000
Turnover	3	54,946	35,870	33,606
Other revenue	4	6,463	82	991
Other net income (loss)	5	20,969	16,519	(6,780)
Net provision for bad and doubtful debts		(174,199)	(364,549)	(22,168)
Employee benefits expenses		(12,092)	(63,182)	(6,450)
Depreciation and amortisation expenses		(1,691)	(1,650)	(1,985)
Finance costs for provision of financial services	8	(7,028)	(4,890)	(6,433)
Other expenses		(19,559)	(13,354)	(11,930)
Other finance costs	8	(13,494)	(7,746)	(5,936)
Profit (Loss) on disposal of interests in subsidiaries		6,014	3,299	(195,482)
Profit on deemed disposal of interest in an associate		2,500	—	—
Loss on disposal of interest in an associate		—	(21,598)	—
Loss before taxation	7	(137,171)	(421,199)	(222,567)
Taxation	10	(4,200)	—	—
Loss for the year	11	<u>(141,371)</u>	<u>(421,199)</u>	<u>(222,567)</u>
Loss per share - Basic	12	<u>(80 cents)</u>	<u>(98 cents)</u>	<u>(38 cents)</u>

CONSOLIDATED BALANCE SHEETS

	Note	At 31 December		
		2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
ASSETS AND LIABILITIES				
Non-current assets				
Property, plant and equipment	14	2,595	1,273	87,979
Intangible assets	15	3,203	2,743	2,283
Other assets	16	2,053	1,976	2,140
Interest in an associate	18	401,888	—	—
		<u>409,739</u>	<u>5,992</u>	<u>92,402</u>
Current assets				
Investments held for trading	19	22,621	278	68
Loans receivable	20	46,556	291,620	45,534
Trade and other receivables	21	193,686	164,438	228,076
Pledged bank deposits		18,002	18,000	3,000
Bank balances and cash	22	25,552	48,009	71,589
		<u>306,417</u>	<u>522,345</u>	<u>348,267</u>
Current liabilities				
Trade and other payables		45,572	59,906	59,786
Due to shareholders	23	406	—	—
Due to a director	24	—	—	14,000
Due to related companies	25	148,121	8,020	998
Bank overdrafts	26	61,109	32,084	21,425
Interest-bearing borrowings	27	—	—	146,000
Taxation		4,720	4,798	4,798
		<u>259,928</u>	<u>104,808</u>	<u>247,007</u>
Net current assets		<u>46,489</u>	<u>417,537</u>	<u>101,260</u>
Total assets less current liabilities		<u>456,228</u>	<u>423,529</u>	<u>193,662</u>
Non-current liabilities				
Convertible notes	28	46,500	120,300	131,000
NET ASSETS		<u>409,728</u>	<u>303,229</u>	<u>62,662</u>
CAPITAL AND RESERVES				
Issued capital	30	241,124	463,268	48,433
Reserves	31	168,604	(160,039)	14,229
TOTAL EQUITY		<u>409,728</u>	<u>303,229</u>	<u>62,662</u>

BALANCE SHEET

		At 31 December		
	Note	2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
ASSETS AND LIABILITIES				
Non-current assets				
Property, plant and equipment	14	65	42	21
Interests in subsidiaries	17	<u>771,981</u>	<u>394,705</u>	<u>191,790</u>
		<u>772,046</u>	<u>394,747</u>	<u>191,811</u>
Current assets				
Loans receivables	20	—	—	5,424
Other receivables		16	13,713	14
Investments held for trading	19	15,950	—	—
Bank balances and cash		<u>35</u>	<u>125</u>	<u>31</u>
		<u>16,001</u>	<u>13,838</u>	<u>5,469</u>
Current liabilities				
Other payables		27,351	549	592
Due to shareholders	23	407	—	—
Due to related companies	25	148,019	8,020	998
Taxation		<u>4,200</u>	<u>4,200</u>	<u>4,200</u>
		<u>179,977</u>	<u>12,769</u>	<u>5,790</u>
Net current (liabilities) assets		<u>(163,976)</u>	<u>1,069</u>	<u>(321)</u>
Total assets less current liabilities		<u>608,070</u>	<u>395,816</u>	<u>191,490</u>
Non-current liabilities				
Convertible notes	28	<u>46,500</u>	<u>120,300</u>	<u>131,000</u>
NET ASSETS		<u>561,570</u>	<u>275,516</u>	<u>60,490</u>
CAPITAL AND RESERVES				
Issued capital	30	241,124	463,268	48,433
Reserves	31	<u>320,446</u>	<u>(187,752)</u>	<u>12,057</u>
TOTAL EQUITY		<u>561,570</u>	<u>275,516</u>	<u>60,490</u>

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

	Year ended 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
Opening balance — Total equity	346,144	409,728	303,229
Prior year adjustment (<i>note 19A</i>)	<u>(64,240)</u>	<u>—</u>	<u>—</u>
As restated	281,904	409,728	303,229
Investment revaluation deficit realised on disposal of other securities included in non-current assets	4,295	—	—
Net gains not recognised in the income statement	<u>(900)</u>	<u>—</u>	<u>—</u>
	<u>3,395</u>	<u>—</u>	<u>—</u>
Issue of share capital	265,800	314,700	17,320
Repurchases of shares	—	—	(40,000)
Conversion of convertible note	—	—	4,680
Loss for the year	<u>(141,371)</u>	<u>(421,199)</u>	<u>(222,567)</u>
Closing balance — Total equity	<u>409,728</u>	<u>303,229</u>	<u>62,662</u>

CONSOLIDATED CASH FLOW STATEMENT

	Year ended 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
	<i>(As restated — note 19A)</i>		
OPERATING ACTIVITIES			
Loss before taxation	(137,171)	(421,199)	(222,567)
Depreciation and amortisation expenses	1,691	1,650	1,985
Interest expenses	20,522	12,636	12,369
Directors' emoluments settled by issue of shares	—	55,000	—
Net gain on disposal of property, plant and equipment	—	(577)	—
Net provision for bad and doubtful debts	174,199	364,549	22,168
Net unrealised loss on investments held for trading	19,017	—	—
Loss on disposal of other securities	4,295	—	—
Gain on disposal of investments held for trading	—	(12,470)	—
(Profit) Loss on disposal of interests in subsidiaries	(6,014)	(3,299)	195,482
(Gain) Loss on disposal of interest in an associate	(2,500)	21,598	—
Changes in working capital:			
Due from the substantial shareholder	1,280	—	—
Loans, trade and other receivables	(400,732)	(173,415)	(169,725)
Investments held for trading	2,477	4,441	209
Trade and other payables	33,397	14,376	(2,687)
Due to related companies	(18,818)	67,877	—
Due to shareholders	406	(406)	—
Due to directors	—	—	14,000
Cash used in operations	(307,951)	(69,239)	(148,766)
Interest paid	(20,115)	(5,614)	(6,855)
Hong Kong Profits Tax refunded	121	78	—
Hong Kong Profits Tax paid	(58)	—	—
Net cash used in operating activities	(328,003)	(74,775)	(155,621)

CONSOLIDATED CASH FLOW STATEMENT (CONTINUED)

	Note	Year ended 31 December		
		2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
INVESTING ACTIVITIES				
Acquisition of subsidiaries	33	—	2	(49,871)
Disposal of subsidiaries	34	34,074	3,594	156,280
Proceeds from disposal of investments held for trading		19,103	28,420	—
Proceeds from disposal of property, plant and equipment		—	1,058	—
Deposit with SEHK		—	(3)	—
Proceeds from disposal of an associate		—	900	—
Purchase of property, plant and equipment		(285)	(1,296)	(3,085)
Contribution in cash to clearing house and exchange		—	(20)	(170)
Refund of deposit from clearing house and exchange		—	100	6
Increase in pledged bank deposit		18,174	—	—
Net advances from an associate		40,000	—	—
Net cash from investing activities		<u>111,066</u>	<u>32,755</u>	<u>103,160</u>
FINANCING ACTIVITIES				
Issue of shares for cash		178,300	140,000	7,000
Repayment to related companies		(14,124)	—	—
New other loans raised		—	—	175,000
Repayment of other loans		(12,615)	—	(65,000)
Issue of convertible notes		163,000	—	—
Repurchase of shares		—	—	(20,000)
Redemption of convertible notes		(29,000)	(46,500)	(25,300)
Net cash from financing activities		<u>285,561</u>	<u>93,500</u>	<u>71,700</u>
Net increase in cash and cash equivalents		68,624	51,480	19,239
Cash and cash equivalents at beginning of the year		<u>(86,179)</u>	<u>(17,555)</u>	<u>33,925</u>
Cash and cash equivalents at end of the year	22	<u>(17,555)</u>	<u>33,925</u>	<u>53,164</u>

B. NOTES TO THE FINANCIAL STATEMENTS**1. GENERAL INFORMATION**

HMIL is a limited liability company incorporated in the British Virgin Islands. HMIL's registered office is located at Sea Meadow House, Blackburne Highway, PO Box 116, Road Town, Tortola, British Virgin Islands. The principal activities of HMIL and its subsidiaries (the "HMIL Group") are described in note 3.

2. PRINCIPAL ACCOUNTING POLICIES

The Financial Information have been prepared in accordance with Hong Kong Financial Reporting Standards issued by the HKICPA as applicable to the last financial year included in the Relevant Periods.

Basis of preparation

The Financial Information has been based on consolidated financial statements that have been prepared on the historical cost basis, except for investments held for trading, which are measured at fair value as explained in the principal accounting policies set out below.

Basis of consolidation

The consolidated financial statements include the financial statements of HMIL and its subsidiaries made up to 31 December each year.

The results of subsidiaries 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 inter-company transactions and balances within the HMIL Group are eliminated on consolidation.

Subsidiaries

A subsidiary is an entity in which HMIL, directly or indirectly, has the power to govern the financial and operating policies so as to obtain benefits from its activities.

In HMIL's balance sheet, investments in subsidiaries are stated at cost less accumulated impairment losses. The carrying amount of the investment is reduced to its recoverable amount on an individual basis. The results of subsidiaries are accounted for by HMIL on the basis of dividends received and receivable.

Goodwill

Goodwill on acquisition is initially measured at cost, being the excess of the cost of the acquisition over HMIL's share of the fair value of the identifiable assets, liabilities and contingent liabilities. Goodwill on acquisition of subsidiaries is recognised as a separate asset. Goodwill is carried at cost less accumulated impairment losses. Goodwill is tested for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

An excess of HMIL's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities over the cost of acquisition, after reassessment, is recognised immediately in the income statement.

Intangible assets

Intangible assets, representing eligibility rights to trade on or through the Stock Exchange of Hong Kong Limited ("SEHK") and the Hong Kong Futures Exchange Limited ("HKFE"). They are stated at cost less accumulated amortisation and any accumulated impairment losses.

Amortisation is provided to write off the cost of intangible assets on the straight-line basis over their estimated useful lives.

Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses.

The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, only when it is probable that future economic benefits associated with the item will flow to the HMIL Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the year in which they are incurred.

The gain or loss arising from the retirement or disposal of property, plant and equipment is determined as the difference between the estimated net sales proceeds and the carrying amount of the assets and is recognised as income or expense in the income statement.

Depreciation is provided to write off the cost less accumulated impairment losses of property, plant and equipment over their estimated useful lives from the date on which they become fully operational and after taking into account of their estimated residual values, using the straight-line method, at the following rates per annum:

Leasehold land	Over the unexpired term of lease
Buildings	2%
Leasehold improvements	20%
Furniture and fixtures	20%
Office equipment	20%
Motor vehicles	20%

Financial instruments

Financial assets and financial liabilities are recognised in the balance sheet when the HMIL Group becomes a party to the contractual provisions of the instruments, and on a trade date basis.

Investments held for trading

Investments held for trading are measured at fair value at each reporting dates. Gains and losses arising from changes in fair value are included in income statement for the period.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and are not held for trading. They are measured at amortised cost using the effective interest method. Amortised cost is calculated by taking into account any discount or premium on acquisition, over the year to maturity. Any gains and losses arising when the loans and receivables are derecognised or impaired, as well as through the amortisation process are recognised in the income statement.

Trade receivables and payables

Trade receivables and payables are recognised at fair values, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the HMIL Group will not be able to collect all the amounts due according to the original terms of receivables. The amount of the provision is the difference between the assets' carrying amount and the present value of estimated future cash flow, discounted at the effective interest rate. The amount of provision is recognised in the income statement.

Convertible loan notes

On the issue of convertible notes, the proceeds are split into liability and equity components. The fair value of the liability component is determined using a market rate for an equivalent non-convertible notes; and this amount, net of transaction costs, is carried as a non-current liability on the amortised cost basis until extinguished on conversion or redemption.

The remainder of the proceeds is allocated to the conversion option and is recognised and included in shareholders' equity, net of transaction costs. The carrying amount of the conversion option is not remeasured in subsequent years.

Payables and short-term borrowings

Payables and short-term borrowings are initially recognised at cost, being the fair value of the consideration received, net of transaction costs incurred and are subsequently measured at amortised cost, using effective interest method.

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the HMIL Group and when the revenue and costs, if applicable, can be measured reliably and on the following bases.

Brokerage fees and commission income is recognised in the period when services are rendered.

Interest income is accrued on a time proportion basis on the principal outstanding and at the interest rate applicable.

Dividend income from investments is recognised when the HMIL Group's rights to receive payment have been established.

Consultancy services, administration services and securities handling income are recognised in the period when services are rendered

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Rentals payable under operating leases are charged to the income statement on a straight-line basis over the term of the relevant lease.

Impairment

At each balance sheet date, the HMIL Group reviews internal and external sources of information to determine whether the carrying amounts of its tangible and intangible assets have suffered an impairment loss or impairment loss previously recognised no longer exists or may be reduced. If any such indication exists, the recoverable amount of the asset is estimated, based on the higher of its fair value less costs to sell and value in use. Where it is not possible to estimate the recoverable amount of an individual asset, the HMIL Group estimates the recoverable amount of the smallest group of assets that generates cash flows independently (i.e. a cash-generating unit).

If the recoverable amount of an asset or a cash-generating unit is estimated to be less than its carrying amount, the carrying amount of the asset or cash-generating unit is reduced to its recoverable amount. Impairment losses are recognised as an expense immediately.

A reversal of impairment loss is limited to the carrying amount of the asset or cash-generating unit that would have been determined had no impairment loss been recognised in prior years. Reversal of impairment losses is recognised as income immediately.

Employee benefits*Defined contribution plans*

The obligations for contributions to defined contribution retirement scheme are recognised as an expense in the income statement as incurred. The assets of the scheme are held separately from those of the HMIL Group in an independently administered fund.

Long service payment

The HMIL Group's net obligation in respect of long service payment under the Employment Ordinance is the amount of future benefit that employees have earned in return for their service in the current and prior periods. The obligation is calculated using the projected unit credit method and is discounted to its present value and the fair value of any related assets, including retirement scheme benefit, is deducted.

Related parties

A party is related to the HMIL Group if (a) directly, or indirectly through one or more intermediaries, the party controls, is controlled by, or is under common control with, the HMIL Group; or has an interest in the HMIL Group that gives it significant influence over the HMIL Group; or has joint control over the HMIL Group; (b) the party is an associate of the HMIL Group; (c) the party is a joint venture in which the HMIL Group is a venturer; (d) the party is a member of the key management personnel of the HMIL Group or its parent; (e) the party is a close member of the family of any individual referred to in (a) or (d); (f) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or (g) the party is a post-employment benefit plan for the benefit of employees of the HMIL Group, or of any entity that is a related party of the HMIL Group.

Taxation

The charge for current income tax is based on the results for the year as adjusted for items that are non-assessable or disallowed. It is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is provided using the liability method, on all temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax liabilities or assets are measured at the tax rates that are expected to apply to the period when the asset is recovered or liability is settled, based on the tax rates and the tax laws that have been enacted or substantively enacted by the balance sheet date. Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the deductible temporary differences, tax losses and credits can be utilised.

Cash equivalents

For the purpose of cash flow statement, cash equivalents represent short-term highly liquid investments which are readily convertible into known amounts of cash and which are subject to an insignificant risk of change in value, net of bank overdrafts.

Critical accounting estimates and judgements

Allowance for bad and doubtful debts

The provisioning policy for bad and doubtful debts of the HMIL Group is based on management's judgment of collectability and ageing analysis of the loans and accounts receivables. At the balance sheet date, the loans and accounts receivables, net of provision, amounted to HK\$273,610,000 (2004: HK\$456,058,000; 2003: HK\$240,242,000). A considerable amount of judgment is required in assessing the ultimate realisation of these receivables, including the creditworthiness and the past collection history of each debtor. If the financial conditions of these debtors were to deteriorate, resulting in an impairment of their ability to make payments, additional allowance will be required.

Financial risk management objective and policies

The HMIL Group's major financial instruments include trade and other receivables and payables, loans receivable, short-term borrowings and convertible bonds. Details of these financial instruments are disclosed in the respective notes. The risks associated with these financial instruments and the policies applied by the HMIL Group to mitigate these risks are set out below. Management monitors these exposures to ensure appropriate measures are implemented in a timely and effective manner.

Interest rate risk

The HMIL Group's interest rates on its bank and other borrowings included in current liabilities are mainly based on at prime rate. The interest rates and terms of repayment have been disclosed in note 27.

Credit risk

The HMIL Group has no significant concentration of credit risk, with exposure spread over a number of customers.

Liquidity risk

The HMIL Group's policy is to regularly monitor current and expected liquidity requirements and its compliance with lending covenants, to ensure that it maintains sufficient reserves of cash and adequate committed lines of funding from major financial institutions to meet its liquidity requirements in the short and longer term.

Future changes in HKFRS

At the date of authorisation of these financial statements, the HKICPA has issued a number of new or revised accounting standards and interpretations that are not yet effective and the HMIL Group has not early adopted. The directors anticipate that the adoption of these new/revised HKFRS in the future accounting periods will have no material impact on the results of the HMIL Group.

3. TURNOVER

Turnover recognised from the principal activities of the HMIL Group during the year including investment holding, the provision of brokerage and financial services.

	Year ended 31 December		
	2003	2004	2005
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Commission and brokerage for securities	8,364	9,336	9,289
Underwriting and placing commission	738	1,384	4,544
Interest income on:			
Loans receivable	39,261	16,836	16,228
Deposits in authorised institutions	121	369	240
Consultancy fee income	2,958	2,105	350
Dividend income from listed investments	30	1	—
Securities handling fees	<u>3,474</u>	<u>5,839</u>	<u>2,955</u>
	<u><u>54,946</u></u>	<u><u>35,870</u></u>	<u><u>33,606</u></u>

4. OTHER REVENUE

	Year ended 31 December		
	2003	2004	2005
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Administration fee	841	10	—
Commission fee	4,291	—	—
Sundry income	<u>1,331</u>	<u>72</u>	<u>991</u>
	<u><u>6,463</u></u>	<u><u>82</u></u>	<u><u>991</u></u>

5. OTHER NET INCOME (LOSS)

	Year ended 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
	<i>(As restated — note 19A)</i>		
Waiver of loan interest payable	—	2,706	—
Gain on disposal of property, plant and equipment	—	583	—
Net realised gain (loss) on investments held for trading	41,176	13,403	(7,182)
Net realised (loss) gain on trading in futures contracts	(1,190)	(173)	402
Net unrealised loss on investment held for trading	<u>(19,017)</u>	<u>—</u>	<u>—</u>
	<u>20,969</u>	<u>16,519</u>	<u>(6,780)</u>

6. SEGMENT INFORMATION

In accordance with the HMIL Group's internal financial reporting, the HMIL Group determined that business segments are its primary reporting format which mainly comprised of provision of financial services and investment holdings and no geographical segments have been presented as the HMIL Group's operations and assets are located in Hong Kong for the years ended 31 December 2005, 2004 and 2003.

Business segments

Business segments of the HMIL Group comprise the following:

Provision of financial services	:	Provide securities brokerage services, financial advisory services and loan financing
Investment holding	:	Holding investments for dividend income and capital appreciation

The following tables show segment information for the Relevant Periods.

Year ended 31 December 2005

	Provision of financial services	Investment holding	Unallocated	Total
Segment revenue	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Turnover	33,606	—	—	33,606
Other revenue	—	—	991	991
Total revenue	<u>33,606</u>	<u>—</u>	<u>991</u>	<u>34,597</u>
Segment results	1,519	(15,767)	(468)	(14,716)
Loss on disposal of interests in subsidiaries		(195,482)		(195,482)
Finance cost	(6,433)		(5,936)	<u>(12,369)</u>
Loss for the year				<u>(222,567)</u>

Year ended 31 December 2004

	Provision of financial services	Investment holding	Unallocated	Total
Segment revenue	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Turnover	35,869	1	—	35,870
Other revenue	—	—	82	82
Total revenue	<u>35,869</u>	<u>1</u>	<u>82</u>	<u>35,952</u>
Segment results	(324,991)	(17,554)	(47,719)	(390,264)
Profit on disposal of interests in subsidiaries		3,299		3,299
Loss on disposal of interests in an associate		(21,598)		(21,598)
Finance cost	(4,890)		(7,746)	<u>(12,636)</u>
Loss for the year				<u>(421,199)</u>

Year ended 31 December 2003

	Provision of financial services <i>HK\$'000</i>	Investment holding <i>HK\$'000</i>	Unallocated <i>HK\$'000</i>	Total <i>HK\$'000</i>
Segment revenue				
Turnover	54,916	30	—	54,946
Other revenue	<u>—</u>	<u>—</u>	<u>6,463</u>	<u>6,463</u>
Total revenue	<u>54,916</u>	<u>30</u>	<u>6,463</u>	<u>61,409</u>
Segment results				
Profit on disposal of interests in subsidiaries	(185,914)	60,447	304	(125,163)
Profit on deemed disposal of interests in an associate		6,014		6,014
Finance costs	(7,028)	2,500	(13,494)	(20,522)
Taxation				<u>(4,200)</u>
Loss for the year				<u>(141,371)</u>

Assets and liabilities as at 31 December 2005

	Provision of financial services <i>HK\$'000</i>	Investment holding <i>HK\$'000</i>	Unallocated <i>HK\$'000</i>	Total <i>HK\$'000</i>
Assets				
Total assets	342,008	11,176	87,485	<u>440,669</u>
Liabilities				
Total liabilities	165,928	175,879	36,200	<u>378,007</u>

Assets and liabilities as at 31 December 2004

	Provision of financial services <i>HK\$'000</i>	Investment holding <i>HK\$'000</i>	Unallocated <i>HK\$'000</i>	Total <i>HK\$'000</i>
Assets				
Total assets	513,321	14,140	876	<u>528,337</u>
Liabilities				
Total liabilities	80,681	138,927	5,500	<u>225,108</u>

Assets and liabilities as at 31 December 2003

	Provision of financial services <i>HK\$'000</i>	Investment holding <i>HK\$'000</i>	Unallocated <i>HK\$'000</i>	Total <i>HK\$'000</i>
Assets				
Segment assets	314,103	165	—	314,268
Interest in associates	—	401,888	—	<u>401,888</u>
Total assets				<u>716,156</u>
Liabilities				
Total liabilities	82,209	223,558	661	<u>306,428</u>

7. LOSS BEFORE TAXATION

	Year ended 31 December		
	2003 <i>HK\$'000</i>	2004 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
This is stated after charging:			
Contributions to MPF Scheme	406	147	389
Auditors' remuneration	361	525	510
Operating lease charges in respect of office premises	3,506	1,445	1,232
Net realised loss on disposal of other securities	<u>4,295</u>	<u>—</u>	<u>—</u>

8. FINANCE COSTS

	Year ended 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
Bank loans, overdrafts and other loans wholly repayable within five years	17,755	5,614	6,433
Convertible notes	<u>2,767</u>	<u>7,022</u>	<u>5,936</u>
	20,522	12,636	12,369
Less: Amount attributable to provision of financial services	<u>(7,028)</u>	<u>(4,890)</u>	<u>(6,433)</u>
Other finance costs	<u><u>13,494</u></u>	<u><u>7,746</u></u>	<u><u>5,936</u></u>

9. DIRECTORS' EMOLUMENTS

The aggregate amount of emoluments received by HMIL's directors are as follows:

	Year ended 31 December 2005		
	Directors' fees	Salaries, allowances and benefits	Total
		in kind	
	HK\$'000	HK\$'000	HK\$'000
Chuang Eugene Yue-chien	—	—	—
Chan Shek Wah	—	150	150
Tong So Yuet	<u>—</u>	<u>227</u>	<u>227</u>
	<u><u>—</u></u>	<u><u>377</u></u>	<u><u>377</u></u>

	Year ended 31 December 2004		
	Directors' fees	Salaries, allowances and benefits	Total
		in kind	
	HK\$'000	HK\$'000	HK\$'000
Chuang Eugene Yue-chien	—	55,000	55,000
Chan Shek Wah	—	228	228
Tong So Yuet	<u>—</u>	<u>57</u>	<u>57</u>
	<u><u>—</u></u>	<u><u>55,285</u></u>	<u><u>55,285</u></u>

Year ended 31 December 2003

	Directors' fees <i>HK\$'000</i>	Salaries, allowances and benefits in kind <i>HK\$'000</i>	Total <i>HK\$'000</i>
Chuang Eugene Yue-chien	<u>—</u>	<u>—</u>	<u>—</u>

Employees' emoluments

The five highest paid employees of the HMIL Group during the Relevant Periods are as follows:

Year ended 31 December

	2003 <i>HK\$'000</i>	2004 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Other emoluments	<u>3,250</u>	<u>2,265</u>	<u>1,997</u>

The emoluments fell within the following bands:

Year ended 31 December

	2003 <i>HK\$'000</i>	2004 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Nil to HK\$1,000,000	4	5	5
HK\$1,000,001 to HK\$1,500,000	<u>1</u>	<u>—</u>	<u>—</u>
	<u>5</u>	<u>5</u>	<u>5</u>

10. TAXATION

Hong Kong Profits Tax has not been provided as the HMIL Group incurred losses for taxation purposes for the years ended 31 December 2005 and 2004. Hong Kong Profits Tax has been provided at the rate of 17.5% on the HMIL Group's estimated assessable profits for the year ended 31 December 2003.

Year ended 31 December

	2003 <i>HK\$'000</i>	2004 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
The charge comprises:			
Hong Kong Profits Tax	<u>4,200</u>	<u>—</u>	<u>—</u>

Details of unrecognised deferred taxation are set out in note 29 to the financial statements.

Reconciliation of tax expense

	Year ended 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
	<i>(As restated</i>		
	<i>— note 19A)</i>		
Loss before taxation	<u>(137,171)</u>	<u>(421,199)</u>	<u>(222,567)</u>
Income tax at applicable tax rate of 17.5%	(24,005)	(73,710)	(38,949)
Non-deductible expenses	24,181	62,709	16,082
Tax exempt revenue	(7,561)	(10,347)	(26,482)
Unrecognised tax losses	2,579	21,443	49,635
Utilisation of previously unrecognised tax losses	(239)	(270)	(36)
Unrecognised temporary differences	9,259	175	(8)
Tax loss not allowed	—	—	(242)
Others	<u>(14)</u>	<u>—</u>	<u>—</u>
Tax expense for the year	<u>4,200</u>	<u>—</u>	<u>—</u>

The applicable tax rate is the Hong Kong Profits Tax rate of 17.5% for the Relevant Periods.

11. LOSS FOR THE YEAR

Of the HMIL Group's loss for the year of HK\$222,567,000 (2004: loss of HK\$421,199,000; 2003: HK\$141,371,000 (restated)), a loss of HK\$197,026,000 (2004: loss of HK\$600,754,000; 2003: profit of HK\$6,934,000 (restated)) has been dealt with in the financial statements of HMIL.

12. LOSS PER SHARE

The calculation of the loss per share is based on the loss for the year of HK\$222,567,000 (2004: HK\$421,199,000; 2003: HK\$141,371,000 (restated)) and on the weighted average number of 580,459,360 shares (2004: 428,098,360 shares; 2003: 177,319,634 shares) in issue during the year.

No diluted loss per share is presented for the Relevant Periods as conversion of HMIL's outstanding convertible notes had an anti-dilutive effect.

13. INVESTMENT PROPERTIES — HMIL GROUP

	At 31 December		
	2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
Valuation			
At beginning of year	5,900	—	—
Disposal of subsidiaries	(5,900)	—	—
At balance sheet date	<u>—</u>	<u>—</u>	<u>—</u>

All investment properties were situated in Hong Kong and were held on long leases.

14. PROPERTY, PLANT AND EQUIPMENT

	Leasehold improvements HK\$'000	Leasehold land and building HK\$'000	Furniture and fixtures HK\$'000	Office equipment HK\$'000	Motor vehicles HK\$'000	Total HK\$'000
HMIL GROUP						
Reconciliation of carrying amount — year ended 31 December 2003						
At beginning of year	67	1,300	977	1,313	1,195	4,852
Additions	33	—	68	184	—	285
Disposals	—	(1,277)	(3)	(5)	—	(1,285)
Depreciation	(31)	(23)	(335)	(474)	(394)	(1,257)
At balance sheet date	<u>69</u>	<u>—</u>	<u>707</u>	<u>1,018</u>	<u>801</u>	<u>2,595</u>
Reconciliation of carrying amount — year ended 31 December 2004						
At beginning of year	69	—	707	1,018	801	2,595
Additions	361	—	92	401	442	1,296
Disposals	(361)	—	(50)	(100)	(917)	(1,428)
Depreciation	(32)	—	(343)	(540)	(275)	(1,190)
At balance sheet date	<u>37</u>	<u>—</u>	<u>406</u>	<u>779</u>	<u>51</u>	<u>1,273</u>
Reconciliation of carrying amount — year ended 31 December 2005						
At beginning of year	37	—	406	779	51	1,273
Additions	—	—	1,786	691	608	3,085
Acquisition of subsidiaries	4,926	80,220	—	—	—	85,146
Depreciation	(23)	—	(695)	(647)	(160)	(1,525)
At balance sheet date	<u>4,940</u>	<u>80,220</u>	<u>1,497</u>	<u>823</u>	<u>499</u>	<u>87,979</u>

	Leasehold improvements <i>HK\$'000</i>	Leasehold land and building <i>HK\$'000</i>	Furniture and fixtures <i>HK\$'000</i>	Office equipment <i>HK\$'000</i>	Motor vehicles <i>HK\$'000</i>	Total <i>HK\$'000</i>
HMIL GROUP						
At 1 January 2004						
Cost	161	—	1,919	4,347	1,970	8,397
Accumulated depreciation	<u>(92)</u>	<u>—</u>	<u>(1,212)</u>	<u>(3,329)</u>	<u>(1,169)</u>	<u>(5,802)</u>
	<u>69</u>	<u>—</u>	<u>707</u>	<u>1,018</u>	<u>801</u>	<u>2,595</u>
At 1 January 2005						
Cost	161	—	1,961	4,628	190	6,940
Accumulated depreciation	<u>(124)</u>	<u>—</u>	<u>(1,555)</u>	<u>(3,849)</u>	<u>(139)</u>	<u>(5,667)</u>
	<u>37</u>	<u>—</u>	<u>406</u>	<u>779</u>	<u>51</u>	<u>1,273</u>
At 31 December 2005						
Cost	5,087	80,220	3,747	5,319	798	95,171
Accumulated depreciation	<u>(147)</u>	<u>—</u>	<u>(2,250)</u>	<u>(4,496)</u>	<u>(299)</u>	<u>(7,192)</u>
	<u>4,940</u>	<u>80,220</u>	<u>1,497</u>	<u>823</u>	<u>499</u>	<u>87,979</u>

The leasehold improvements and leasehold land and buildings were acquired through business combination in December 2005, no depreciation charge was recognised for the year ended 31 December 2005 as the amount is immaterial to the HMIL Group.

The leasehold land and buildings with a net book value of HK\$80,220,000 as at 31 December 2005 (*2004 and 2003: HK\$ Nil*) are held by the HMIL Group under medium-term lease in Hong Kong.

Office equipment
HK\$'000**HMIL**Reconciliation of carrying amount
— year ended 31 December 2003

At beginning of year	52
Additions	36
Depreciation	<u>(23)</u>
At balance sheet date	<u>65</u>

Reconciliation of carrying amount
— year ended 31 December 2004

At beginning of year	65
Depreciation	<u>(23)</u>
At balance sheet date	<u>42</u>

Reconciliation of carrying amount
— year ended 31 December 2005

At beginning of year	42
Depreciation	<u>(21)</u>
At balance sheet date	<u>21</u>

At 1 January 2004

Cost	167
Accumulated depreciation	<u>(102)</u>
	<u>65</u>

At 1 January 2005

Cost	167
Accumulated depreciation	<u>(125)</u>
	<u>42</u>

At 31 December 2005

Cost	167
Accumulated depreciation	<u>(146)</u>
	<u>21</u>

15. INTANGIBLE ASSETS — HMIL GROUP

	Trading rights of SEHK <i>HK\$'000</i>	Trading right of HKFE <i>HK\$'000</i>	Total <i>HK\$'000</i>
Reconciliation of carrying amount — year ended 31 December 2003			
At beginning of year	2,250	1,387	3,637
Amortisation	<u>(300)</u>	<u>(134)</u>	<u>(434)</u>
At balance sheet date	<u>1,950</u>	<u>1,253</u>	<u>3,203</u>
Reconciliation of carrying amount — year ended 31 December 2004			
At beginning of year	1,950	1,253	3,203
Amortisation	<u>(300)</u>	<u>(160)</u>	<u>(460)</u>
At balance sheet date	<u>1,650</u>	<u>1,093</u>	<u>2,743</u>
Reconciliation of carrying amount — year ended 31 December 2005			
At beginning of year	1,650	1,093	2,743
Amortisation	<u>(300)</u>	<u>(160)</u>	<u>(460)</u>
At balance sheet date	<u>1,350</u>	<u>933</u>	<u>2,283</u>
At 1 January 2004			
Cost	3,000	1,600	4,600
Accumulated amortisation and impairment losses	<u>(1,050)</u>	<u>(347)</u>	<u>(1,397)</u>
	<u>1,950</u>	<u>1,253</u>	<u>3,203</u>
At 1 January 2005			
Cost	3,000	1,600	4,600
Accumulated amortisation and impairment losses	<u>(1,350)</u>	<u>(507)</u>	<u>(1,857)</u>
	<u>1,650</u>	<u>1,093</u>	<u>2,743</u>
At 31 December 2005			
Cost	3,000	1,600	4,600
Accumulated amortisation and impairment losses	<u>(1,650)</u>	<u>(667)</u>	<u>(2,317)</u>
	<u>1,350</u>	<u>933</u>	<u>2,283</u>

16. OTHER ASSETS — HMIL GROUP

	At 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
Deposits with HKFE Clearing Corporation Limited	1,500	1,500	1,500
Admission fee paid to Hong Kong Securities Clearing Company Limited	100	100	100
Contributions in cash to Central Clearing and Settlement System Guarantee Fund	100	120	290
Deposits with the SEHK	253	156	150
Statutory deposits	100	100	100
	<u>2,053</u>	<u>1,976</u>	<u>2,140</u>

17. INTERESTS IN SUBSIDIARIES — HMIL

	At 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
Unlisted shares, at cost	21,000	50,000	50,000
Impairment loss	<u>(10,332)</u>	<u>(50,000)</u>	<u>(50,000)</u>
	<u>10,668</u>	<u>—</u>	<u>—</u>
Due from subsidiaries	945,845	1,179,279	1,023,970
Provision for doubtful debts	<u>(183,402)</u>	<u>(681,752)</u>	<u>(803,286)</u>
	<u>762,443</u>	<u>497,527</u>	<u>220,684</u>
Due to subsidiaries	<u>(1,130)</u>	<u>(102,822)</u>	<u>(28,894)</u>
	<u>771,981</u>	<u>394,705</u>	<u>191,790</u>

The amounts due from (to) subsidiaries are unsecured, interest-free and have no fixed repayments terms for the year ended 31 December 2005 and 2004.

The amounts due from subsidiaries for the year ended 31 December 2003 were unsecured, interest-free and had no fixed repayment terms, except that amounts due from subsidiaries of HK\$184,084,000 were interest-bearing at 8% to 8.5% per annum.

Details of the principal subsidiaries at the date of this report are as follows:

Name of subsidiary	Place of incorporation/ operation	Particulars of issued ordinary and paid up capital	Proportion of nominal value of issued capital held by HMIL		Principal activities
			Directly	Indirectly	
Apex Novel Limited	British Virgin Islands	1 share of US\$1 each	—	100%	Investment holding
Chung Nam Commodities Limited	Hong Kong	150,000 shares of HK\$100 each	—	100%	Commodities dealer
Chung Nam Finance Limited	Hong Kong	410,000,000 shares of HK\$1 each	—	100%	Securities financing and money lending
Chung Nam Holdings Limited	Hong Kong	17,200,000 shares of HK\$1 each	—	100%	Investment holding
Chung Nam Nominees Limited	Hong Kong	10,000 shares of HK\$1 each	—	100%	Nominees
Chung Nam Securities Limited	Hong Kong	302,000,000 shares of HK\$1 each	—	100%	Securities brokerage and financial services
CU Corporate Finance Limited	Hong Kong	10,000,000 shares of HK\$1 each	—	100%	Investment advisor
CU Investment (Holdings) Limited	Hong Kong	2 shares of HK\$1 each and 2 non-voting deferred shares of HK\$1 each	100%	—	Investment holding
Moonlightt Capital Management Limited	British Virgin Islands	101 shares of US\$1 each	100%	—	Investment holding and securities investment
Hennabun Investments Limited	British Virgin Islands	1 share of US\$1 each	100%	—	Investment holding
Radland International Limited	Hong Kong	23,400,000 shares of HK\$1 each	—	100%	Securities brokerage and financial services

Details of the principal subsidiaries at the date of this report are as follows:

Name of subsidiary	Place of incorporation/ operation	Particulars of issued ordinary and paid up capital	Proportion of nominal value of issued capital held by HMIL		Principal activities
			Directly	Indirectly	
Kam Kwong Investments Limited	Hong Kong	10,000 shares of HK\$1 each	—	100%	Investment holding
Quail-Trade Investments Limited	British Virgin Islands	4,980,000 shares of US\$1 each	100%	—	Investment holding
Sun Chung Nam Finance Limited	Hong Kong	1,000,000 shares of HK\$1 each	—	100%	Money lending

18. INTEREST IN AN ASSOCIATE — HMIL GROUP

	Note	At 31 December		
		2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
Share of net assets	18(a)	22,499	—	—
Due from an associate	18(b)	379,389	—	—
		<u>401,888</u>	<u>—</u>	<u>—</u>

(a) Investment in an associate represented 45% of the issued ordinary share capital of the associate, Parco Development Limited, which was disposed of during the year ended 31 December 2004 at a cash consideration of HK\$900,000 resulting in a loss on disposal of HK\$21,598,000.

(b) The amount due was unsecured, interest-free and had no fixed repayment term. During the year ended 31 December 2004, on disposal of the associate an amount of HK\$282,000,000 due from the associate was assigned to the purchaser. The remaining balance of HK\$97,389,000 was fully provided for.

19. INVESTMENTS HELD FOR TRADING

HMIL GROUP	At 31 December		
	2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
Equity securities:			
— Listed investments in Hong Kong (Note 19A)	21,765	278	68
— Listed investments outside Hong Kong	856	—	—
	<u>22,621</u>	<u>278</u>	<u>68</u>

	At 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
HMIL			
Equity securities:			
— Listed investments in Hong Kong (<i>Note 19A</i>)	<u>15,950</u>	<u>—</u>	<u>—</u>

19A. PRIOR YEAR ADJUSTMENT

At 31 December 2002, the HMIL Group held 290,000,000 shares in Radford Capital Investment Limited (“Radford Capital”), a company incorporated in the Cayman Islands with limited liability. Radford Capital is principally engaged in investments in listed and unlisted enterprises established and/or conducting business in Hong Kong and/or the People’s Republic of China and is an investment company listed under Chapter 21 of the Listing Rules of the SEHK. Although the HMIL Group’s investment in Radford Capital accounted for 23.44% issued ordinary shares of Radford Capital, the HMIL Group did not regard Radford Capital as an associate because it intended to hold the investment in Radford Capital for trading purpose. The shares of Radford Capital were thinly traded and the percentage of issued shares of Radford Capital held by the HMIL Group was substantial.

The shares were previously carried at HK\$114,000,000, which represented a discount of 20% on the quoted market price of Radford Capital as at 31 December 2002. The previous auditors qualified their report with regard to this valuation method. After taking further advice, it is considered that the net asset value of Radford Capital at 31 December 2002 is a better reflection of the fair value of the shares. Accordingly, a prior year adjustment has been effected to restate the previous carrying value to reflect the net asset value of Radford Capital. This has resulted in an increase of the accumulated loss at 1 January 2003 by HK\$64,240,000 and a reduction of the loss for the year ended 31 December 2003 by the same amount.

At 31 December 2003, the quoted market price of Radford Capital was lower than the net asset value. The sole director of HMIL considered the quoted market price at 31 December 2003, without any discount, was the fair value of Radford Capital at that date because the quoted market price which was lower than the net asset value and that the quoted market price better reflected the realisable value of the shares of Radford Capital, which were held with the intention of an orderly disposal in the stock market. Realised gain on partial disposal and unrealised holding loss of Radford Capital shares recognised during the year ended 31 December 2003 amounted to HK\$15,928,000 and HK\$58,312,000 respectively.

20. LOANS RECEIVABLE

HMIL GROUP	Note	At 31 December		
		2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
Third parties		68,992	514,004	52,990
Related companies	20(a)	8,214	31,990	—
A director of HMIL	20(b)	—	3,067	—
A director of subsidiaries		244	—	—
A director of the investor of HMIL		106	—	—
		<u>77,556</u>	<u>549,061</u>	<u>52,990</u>
Provision for bad and doubtful debts		<u>(31,000)</u>	<u>(257,441)</u>	<u>(7,456)</u>
Balance due within one year included in current assets		<u>46,556</u>	<u>291,620</u>	<u>45,534</u>

HMIL	At 31 December		
	2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
Third parties	<u>—</u>	<u>—</u>	<u>5,424</u>

An aging analysis of loans receivable (before provision for bad and doubtful debts) as at the balance sheet date is set out below:

HMIL GROUP	At 31 December		
	2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
Within maturity dates	65,524	479,683	49,140
Balances overdue for repayment:			
1-3 months	250	30,561	169
4-6 months	7,922	106	—
7-12 months	—	27,427	—
Over 12 months	<u>3,860</u>	<u>11,284</u>	<u>3,681</u>
	<u>77,556</u>	<u>549,061</u>	<u>52,990</u>

HMIL	At 31 December		
	2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
Within maturity dates	<u>—</u>	<u>—</u>	<u>5,424</u>

20(a) LOANS RECEIVABLE FROM RELATED COMPANIES

Name of related company	Connected director	Balance at 31.12.2003 <i>HK\$'000</i>	Balance at 31.12.2004 <i>HK\$'000</i>	Balance at 31.12.2005 <i>HK\$'000</i>
Sunderland Properties Limited	Chuang Eugene Yue-chien	—	23,776	—
Bo Wai Limited	Chuang Eugene Yue-chien	<u>8,214</u>	<u>8,214</u>	<u>—</u>
		<u>8,214</u>	<u>31,990</u>	<u>—</u>

Maximum debit amount outstanding
during the year

Name of related company	Connected director	2003 <i>HK\$'000</i>	2004 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Sunderland Properties Limited	Chuang Eugene Yue-chien	—	23,776	—
Bo Wai Limited	Chuang Eugene Yue-chien	<u>20,440</u>	<u>8,214</u>	<u>8,214</u>

The above loans were unsecured and interest-bearing at 7% per annum or at prime rate plus 2% per annum. The amounts due from Sunderland Properties Limited and Bo Wai Limited had been fully provided in the years 2004 and 2003 respectively and they were disposed upon the disposal of subsidiaries during the year ended 31 December 2005.

20(b) LOANS RECEIVABLE FROM A DIRECTOR OF HMIL

Name of the director	Balance at 31.12.2003 <i>HK\$'000</i>	Balance at 31.12.2004 <i>HK\$'000</i>	Balance at 31.12.2005 <i>HK\$'000</i>
Chuang Eugene Yue-chien	<u>—</u>	<u>3,067</u>	<u>—</u>

Maximum debit amount outstanding
during the year

Name of the director	2003 <i>HK\$'000</i>	2004 <i>HK\$'000</i>	2005 <i>HK\$'000</i>
Chuang Eugene Yue-chien	<u>—</u>	<u>3,067</u>	<u>3,067</u>

The above loan was unsecured, interest-bearing at 7% per annum and it was disposed of upon the disposal of subsidiaries during the year ended 31 December 2005.

At the balance sheet date, there was no interest due but unpaid and no provision had been made for non-repayment of the advance or interest.

21(b) TRADE RECEIVABLE FROM A RELATED COMPANY

The amount due represents securities margin loans secured by marketable securities. Details of the amount due are as follows:

Name	Connected director	Interest rate per annum	Balance at 31.12.2003 HK\$'000	Balance at 31.12.2004 HK\$'000	Balance at 31.12.2005 HK\$'000
Capital Union Inc.	Chuang Eugene Yue-chien	5% - 7.5%	<u>1,466</u>	<u>120</u>	<u>1,701</u>

Name of related company	Connected director	Maximum debit amount outstanding during the year		
		2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
Capital Union Inc.	Chuang Eugene Yue-chien	<u>20,440</u>	<u>8,214</u>	<u>8,214</u>

As at 31 December 2005, 2004 and 2003, there was no interest due but unpaid and no provision had been made for non-repayment of the advances or interest.

21(c) TRADE RECEIVABLES FROM OTHER RELATED PARTIES

The amount due represents securities margin loans secured by marketable securities. Details of amounts due are as follows:

Name	Interest rate per annum	Balance at 31.12.2003 HK\$'000	Balance at 31.12.2004 HK\$'000	Balance at 31.12.2005 HK\$'000
<i>Director of the substantial shareholder</i>				
Lo Kan Sun	5%-7.5%	19	—	—
Wong Ying Seung, Asiong	5%-7.5%	442	—	6,011
King, Phillip	5%-7.5%	—	—	264
<i>Directors of HMIL's subsidiaries</i>				
	5%-7.5%	<u>167</u>	<u>203</u>	<u>60</u>
		<u>628</u>	<u>203</u>	<u>6,335</u>

Name of directors of a substantial shareholder	Maximum debit amount outstanding during the year		
	2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
<i>Director of the substantial shareholder</i>			
Lo Kan Sun	411	136	—
Wong Ying Seung, Asiong	482	4,646	6,011
King, Phillip	—	—	561
<i>Directors of HMIL's subsidiaries</i>	<u>167</u>	<u>203</u>	<u>204</u>

21(d) OTHER RECEIVABLES

Included in other receivables as at 31 December 2004 was an amount of HK\$13,700,000 being the balance of consideration paid for the acquisition of two wholly-owned subsidiaries of a related company, a director of which was also a director of HMIL.

In April 2005, the related company re-acquired these two companies at a cash consideration of HK\$5,000,000. A loss on disposal of HK\$8,700,000 was recognised in the income statement during the year ended 31 December 2005.

22. CASH AND CASH EQUIVALENTS — HMIL GROUP

	At 31 December		
	2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
Bank balances and cash	25,552	48,009	71,589
Pledged bank deposits	18,002	18,000	3,000
Bank overdrafts	<u>(61,109)</u>	<u>(32,084)</u>	<u>(21,425)</u>
As stated in the cash flow statement	<u>(17,555)</u>	<u>33,925</u>	<u>53,164</u>

23. DUE TO SHAREHOLDERS — HMIL GROUP & HMIL

The amount due represented interest payable on the outstanding principal amount of the convertible notes prior to the exercise of the conversion.

24. DUE TO A DIRECTOR — HMIL GROUP

The amount due was unsecured, interest-free and had no fixed repayment term.

25. DUE TO RELATED COMPANIES

HMIL GROUP	Note	At 31 December		
		2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
Due to a related company with common director	(i)	1,101	998	998
Due to other related company	(ii)	<u>147,020</u>	<u>7,022</u>	<u>—</u>
		<u>148,121</u>	<u>8,020</u>	<u>998</u>

HMIL	Note	At 31 December		
		2003 HK\$'000	2004 HK\$'000	2005 HK\$'000
Due to a related company with common director	(i)	998	998	998
Due to other related company	(ii)	<u>147,021</u>	<u>7,022</u>	<u>—</u>
		<u>148,019</u>	<u>8,020</u>	<u>998</u>

Notes:

- (i) Related company with a common director

The amount due was unsecured, interest-free and had no fixed repayment term.

- (ii) Other related company

The other related company was Willie International Holdings Limited ("Willie International"), the substantial shareholder of HMIL, and the amount due as at 31 December 2004 represented interest payable on the convertible notes and such amount of interest payable was cancelled pursuant to an agreement dated 3 August 2005, details of which are provided in note 28(ii) below.

The amounts due as at 31 December 2003 represented loan advances which were unsecured, interest-bearing at prime rate plus 1% per annum and had no fixed repayment terms. The amounts were due to wholly-owned subsidiaries of the substantial shareholder and the loan advanced together with interest accrued were converted into convertible notes and ordinary shares of HMIL during the year ended 31 December 2004 as detailed in note 28(v) and 30(iv).

26. BANK OVERDRAFTS — HMIL GROUP

	At 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
Bank overdrafts:			
Secured	60,915	31,590	21,425
Unsecured	<u>194</u>	<u>494</u>	<u>—</u>
	<u>61,109</u>	<u>32,084</u>	<u>21,425</u>

27. INTEREST-BEARING BORROWINGS — HMIL GROUP

	At 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
Secured bank loan	—	—	36,000
Unsecured other loans	<u>—</u>	<u>—</u>	<u>110,000</u>
	<u>—</u>	<u>—</u>	<u>146,000</u>

Notes:

- (i) The maturities of the above borrowings are all within one year.
- (ii) Bank loan carried interest on prime rate minus 0.5% for the year of 2005. Other unsecured loans carried interest ranging from prime rate plus 1% to 2% and 7.5% per month for the year of 2005.

28. CONVERTIBLE NOTES — HMIL GROUP & HMIL

	At 31 December					
	2003		2004		2005	
	Note	HK\$'000	Note	HK\$'000	Note	HK\$'000
At beginning of year		—		46,500		120,300
Issuance during the year	(viii)	163,000	(v)	150,000	(i)(a)&(b)	146,000
Cancellation		—		—	(i)(b)	(95,000)
Redemption	(ix)	(29,000)	(vi)	(46,500)	(ii)	(25,300)
Conversion		<u>(87,500)</u>	(vii)	<u>(29,700)</u>	(iii)	<u>(15,000)</u>
At balance sheet date		<u>46,500</u>		<u>120,300</u>		<u>131,000</u>

2005

Notes:

- (i) During the year, HMIL entered into an agreement dated 3 August 2005 with its substantial shareholder, Willie International Holdings Limited ("Willie"), whereby:
- (a) HMIL acquired 100% of the equity shares in a wholly-owned subsidiary from Willie which principal assets were loans receivable of HK\$41 million. The acquisition was satisfied by the issue of a convertible note by HMIL in the principal amount of HK\$41 million ("First New Note");
- (b) the 6% convertible note issued by HMIL on January 2004 together with the outstanding principal amount of HK\$95 million and accrued interest of approximately HK\$10 million were cancelled in exchange for new convertible note issued by HMIL in the principal amount of HK\$105 million ("Second New Note");
- (c) the New Convertible Notes (the First New Note and Second New Note) bear interest at 8% per annum, payable monthly and will mature in ten years from the date of issue. They can be converted into shares of HMIL at a conversion price of HK\$0.25 per ordinary share at any time after the date of issue of the convertible note and before its maturity date; and
- (d) HMIL, or its subsidiaries or independent parties, provides an unsecured standby credit facility in the amount of HK\$50 million to Willie at prime rate and any drawdown of the facility is repayable on demand. Willie had not utilised such standby credit facility during the year ended 31 December 2005.
- (ii) Convertible note with principal sum of HK\$25,300,000 was redeemed by HMIL during the year.
- (iii) Of the New Convertible Notes with principal sum of HK\$146,000,000, principal amount of HK\$15,000,000 was converted into 60,000,000 ordinary shares of US\$0.01 each of HMIL at a conversion price of HK\$0.25 per share.
- (iv) The fair value of the liability component and the equity conversion component were determined at issuance of the New Convertible Notes. The fair value of the liability component, included in interest-bearing borrowings, was calculated using a market interest rate for an equivalent non-convertible note. The residual amount, representing the value of the equity conversion component was determined to be immaterial.

2004

Notes:

- (v) As mentioned in note 25(ii), for the year ended 31 December 2004, HMIL issued convertible notes with principal sum of HK\$150,000,000 to a wholly-owned subsidiary of Willie International. Details of the notes issued are as follows:

Interest	Maturity date	Conversion price per share
6% per annum	28 January 2007	HK\$1.5 per share

The note holders could convert the whole or part of the outstanding principal amount of the notes at any time after the date of issue and before the maturity date, in such number of conversion shares of the HMIL to be determined by dividing the principal amount of the notes or such part thereof to be converted by the conversion price.

HMIL might, at any time after the issue of the notes up to the date immediately prior to the maturity date, redeem the entirety or any part of the notes by payment to the note holders in cash of an amount equal to that part of the principal amount of the notes.

- (vi) The whole amount of the convertible note with principal sum of HK\$46,500,000 was redeemed by the HMIL for the year ended 31 December 2004.
- (vii) Of the convertible note with principal sum of HK\$150,000,000, principal amounting to HK\$29,700,000 was converted into 19,800,000 ordinary shares of US\$0.1 each of HMIL at a conversion price of HK\$1.50 per share.

2003

Notes:

- (viii) During the year ended 31 December 2003, HMIL issued convertible notes with principal sum of HK\$163,000,000 to third parties. Details of the notes issued are as follows:

Principal of notes	Interest	Maturity date	Conversion price per share
HK\$88,000,000	5% per annum	14 April 2005	HK\$2.00 and HK\$1.50
HK\$60,000,000	7.5% per annum	29 November 2006	HK\$1.50
HK\$15,000,000	7.5% per annum	1 December 2006	HK\$1.50

The note holders could convert the whole or part of the outstanding principal amount of the notes at any time after the date of issue and before the maturity date, in such number of conversion shares of HMIL to be determined by dividing the principal amount of the notes or such part thereof to be converted by the conversion price.

HMIL might, at any time after the issue of the notes up to the date immediately prior to the maturity date, redeem the entirety or any part of the notes by payment to the note holders in cash of an amount equal to that part of the principal amount of the notes.

Of the convertible note with principal sum of HK\$88,000,000, principal amounting to HK\$29,000,000 was redeemed by HMIL, and principals amounting to HK\$44,000,000 and HK\$15,000,000 were converted into 22,000,000 ordinary shares and 10,000,000 ordinary shares of US\$0.1 each of HMIL at a conversion price of HK\$2.00 and HK\$1.50 per share respectively. According to the terms of the convertible note with principal sum of HK\$88,000,000, the conversion price was HK\$2.00 per share but the note holder and HMIL mutually agreed that principal of HK\$15,000,000 was to be converted to HMIL's shares at HK\$1.50 per share. Of the convertible note with principal sum of HK\$60,000,000, principal amounting to HK\$28,500,000 was converted into 19,000,000 ordinary shares of US\$0.1 each of HMIL.

29. DEFERRED TAXATION

Unrecognised deferred tax assets arising from

	At 31 December		
	2003	2004	2005
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
HMIL GROUP			
Deductible temporary differences	80,141	21,551	6,568
Tax losses	<u>59,356</u>	<u>134,976</u>	<u>142,973</u>
At balance sheet date	<u><u>139,497</u></u>	<u><u>156,527</u></u>	<u><u>149,541</u></u>
	At 31 December		
	2003	2004	2005
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
HMIL			
Deductible temporary differences	14,689	—	—
Tax losses	<u>—</u>	<u>48,360</u>	<u>54,234</u>
At balance sheet date	<u><u>14,689</u></u>	<u><u>48,360</u></u>	<u><u>54,234</u></u>

Both the tax losses and the deductible temporary differences have no expiry date under current tax legislation.

30. ISSUED CAPITAL

	<i>Notes</i>	Number of ordinary shares of US\$0.1 each	Number of ordinary shares of US\$0.01 each	Nominal value HK\$'000
Authorised:				
At 1 January 2003		300,000,000	—	234,000
Increase during the year	(vi)	<u>450,000,000</u>	<u>—</u>	<u>351,000</u>
At 31 December 2003, 1 January 2004, 31 December 2004 and 1 January 2005		750,000,000	—	585,000
Subdivision of shares	(iii)	<u>(750,000,000)</u>	<u>7,500,000,000</u>	<u>—</u>
At 31 December 2005		<u>—</u>	<u>7,500,000,000</u>	<u>585,000</u>
Issued and fully paid:				
At 1 January 2003		158,133,333	—	123,344
New shares issued	(v)(vii)	100,000,000	—	78,000
Conversion of convertible notes	(viii)	<u>51,000,000</u>	<u>—</u>	<u>39,780</u>
At 31 December 2003 and 1 January 2004		309,133,333	—	241,124
New shares issued	(iv)	265,000,000	—	206,700
Conversion of convertible notes	27(vi) (vii)	<u>19,800,000</u>	<u>—</u>	<u>15,444</u>
At 31 December 2004 and 1 January 2005		593,933,333	—	463,268
New shares issued	(i)	7,000,000	—	5,460
Share repurchase	(ii)	(40,000,000)	—	(31,200)
Capital reduction	(iii)	<u>(560,933,333)</u>	<u>560,933,333</u>	<u>(393,775)</u>
		—	560,933,333	43,753
Conversion of convertible notes (<i>Note 28 iii</i>)		<u>—</u>	<u>60,000,000</u>	<u>4,680</u>
At 31 December 2005		<u>—</u>	<u>620,933,333</u>	<u>48,433</u>

2005*Notes*

- (i) By an ordinary resolution of the board of directors passed on 4 January 2005, 3,000,000 ordinary shares of US\$0.1 each were issued for total cash consideration of HK\$3,000,000. These shares rank pari passu with the existing shares in all respects.

By an ordinary resolution of the board of directors passed on 7 January 2005, 4,000,000 ordinary shares of US\$0.1 each were issued for total cash consideration of HK\$4,000,000. These shares rank pari passu with the existing shares in all respects.

- (ii) By an ordinary resolution of the board of directors passed on 29 June 2005, 40,000,000 ordinary shares of US\$0.1 each were repurchased at a consideration of HK\$40,000,000 which was satisfied by a cash consideration of HK\$20,000,000 and loan payable amounted to HK\$20,000,000 due to such shareholder.
- (iii) By ordinary resolutions of the board of directors passed on 15 July 2005, the authorised capital was made up of one class and one series of shares divided into 7,500,000,000 shares of US\$0.01 par value with one vote for each share. It was further resolved that the par value of all of the share capital of HMIL both issued and unissued were reduced from US\$0.1 to US\$0.01 and accordingly a capital reduction of HK\$393,775,000 was recognised and transferred to the contributed surplus subject to the provisions in the Memorandum and Articles of Association of HMIL.

2004*Notes*

- (iv) Pursuant to a share subscription agreement dated 4 March 2004, 80,000,000 ordinary shares of US\$0.1 each were issued for total cash consideration of HK\$100,000,000. These shares rank pari passu with the existing shares in all respects.

By an ordinary resolution of the sole director passed on 9 July 2004, 10,000,000 ordinary shares of US\$0.1 each were issued for total cash consideration of HK\$10,000,000. These shares rank pari passu with the existing shares in all respects.

By an ordinary resolution of the sole director passed on 7 September 2004, 17,000,000 ordinary shares of US\$0.1 each were issued for total cash consideration of HK\$17,000,000. These shares rank pari passu with the existing shares in all respects.

By an ordinary resolution of the sole director passed on 4 October 2004, 65,000,000 ordinary shares of US\$0.1 each were issued for total cash consideration of HK\$65,000,000 which was used to settle part of the amount due to a related company as mentioned in note 21(d). These shares rank pari passu with the existing shares in all respects.

By an ordinary resolution of the board of directors passed on 11 October 2004, 55,000,000 ordinary shares of US\$0.1 each were issued for total consideration of HK\$55,000,000. These shares rank pari passu with the existing shares in all respects. The consideration of HK\$55,000,000 was the emoluments of the services rendered since 1996 by a director of HMIL and thus it was included in income statement as staff costs for the year ended 31 December 2004.

By an ordinary resolution written resolution of the board of directors passed on 27 October 2004, 25,000,000 ordinary shares of US\$0.1 each were issued as consideration to acquire the interests in two subsidiaries. These shares rank pari passu with the existing shares in all respects.

By an ordinary resolution of the directors passed on 20 December 2004, 10,000,000 ordinary shares of US\$0.1 each were issued for total cash consideration of HK\$10,000,000. These shares rank pari passu with the existing shares in all respects.

By an ordinary resolution of the directors passed on 23 December 2004, 3,000,000 ordinary shares of US\$0.1 each were issued for total cash consideration of HK\$3,000,000. These shares rank pari passu with the existing shares in all respects.

2003

- (v) Pursuant to a share subscription agreement dated 26 June 2003, 10,000,000 ordinary shares of US\$0.1 each were issued for total cash consideration of HK\$20,000,000. These shares rank pari passu with the existing shares in all respects.

Pursuant to a share subscription agreement dated 10 October 2003 entered between HMIL and a third party, a total of 40,000,000 ordinary shares of US\$0.1 each were issued for total cash consideration of HK\$83,300,000. These shares rank pari passu with the existing shares in all respects.

- (vi) By a written resolution of the sole director passed on 12 December 2003, the authorised share capital of HMIL was increased to HK\$585,000,000 by the creation of an additional 450,000,000 shares of US\$0.1 each.
- (vii) By a written resolution of the sole director passed on 15 December 2003, 50,000,000 ordinary shares of US\$0.1 each were issued for total cash consideration of HK\$75,000,000. These shares rank pari passu with the existing shares in all respects.
- (viii) During the year ended 31 December 2003, an aggregate of 51,000,000 ordinary shares of US\$0.1 each of HMIL were issued to certain convertible note holders upon the conversion of convertible notes at cash subscription prices as detailed in note 28(viii).

31. RESERVES

	Share premium <i>HK\$'000</i>	Capital reserve <i>HK\$'000</i>	Investment revaluation reserve <i>HK\$'000</i>	Contributed surplus <i>HK\$'000</i>	Investment properties revaluation reserve <i>HK\$'000</i>	Accumulated losses <i>HK\$'000</i>	Total <i>HK\$'000</i>
HMIL GROUP							
At 1 January 2003	242,923	2,553	(4,295)	98,619	900	(117,900)	222,800
Prior year adjustment (note 19A)	—	—	—	—	—	(64,240)	(64,240)
Derecognition of negative goodwill upon adoption of HKFRS 3	—	(2,553)	—	—	—	2,553	—
As restated	242,923	—	(4,295)	98,619	900	(179,587)	158,560
Premium on issue of shares	148,020	—	—	—	—	—	148,020
Released upon disposal	—	—	4,295	—	(900)	—	3,395
Loss for the year	—	—	—	—	—	(141,371)	(141,371)
At 31 December 2003 and 1 January 2004	390,943	—	—	98,619	—	(320,958)	168,604
Premium on issue of shares	92,556	—	—	—	—	—	92,556
Loss for the year	—	—	—	—	—	(421,199)	(421,199)
At 31 December 2004 and 1 January 2005	483,499	—	—	98,619	—	(742,157)	(160,039)
Premium on issue of shares	11,860	—	—	—	—	—	11,860
Share repurchase	(8,800)	—	—	—	—	—	(8,800)
Capital reduction	—	—	—	393,775	—	—	393,775
Loss for the year	—	—	—	—	—	(222,567)	(222,567)
At 31 December 2005	486,559	—	—	492,394	—	(964,724)	14,229

	Share premium HK\$'000	Capital reserve HK\$'000	Investment revaluation reserve HK\$'000	Contributed surplus HK\$'000	Accumulated losses HK\$'000	Total HK\$'000
HMIL						
At 1 January 2003	242,923	—	—	98,619	(111,810)	229,732
Prior year adjustment (<i>note 19A</i>)	—	—	—	—	(64,240)	(64,240)
As restated	242,923	—	—	98,619	(176,050)	165,492
Premium on issue of shares	148,020	—	—	—	—	148,020
Profit for the year	—	—	—	—	6,934	6,934
At 31 December 2003 and 1 January 2004	390,943	—	—	98,619	(169,116)	320,446
Premium on issue of shares	92,556	—	—	—	—	92,556
Loss for the year	—	—	—	—	(600,754)	(600,754)
At 31 December 2004 and 1 January 2005	483,499	—	—	98,619	(769,870)	(187,752)
Premium on issue of shares	11,860	—	—	—	—	11,860
Share repurchase	(8,800)	—	—	—	—	(8,800)
Capital reduction	—	—	—	393,775	—	393,775
Loss for the year	—	—	—	—	(197,026)	(197,026)
At 31 December 2005	486,559	—	—	492,394	(966,896)	12,057

Share premium represents the excess of consideration received over the par value of shares issued.

Contributed surplus represents amount transferred from share capital pursuant to capital reduction made in current and prior years.

32. MAJOR NON-CASH TRANSACTIONS

Major non-cash transactions during the year ended 31 December 2005 have been disclosed in notes 25(ii), 28(i) and (iii), 30(ii) and (iii).

33. ACQUISITION OF SUBSIDIARIES

On 19 January 2005, the HMIL Group acquired the entire share capital of Total Capital Limited for a consideration of HK\$0.6 million. The amount of goodwill as a result of the acquisition was HK\$0.9 million.

On 21 September 2005, the HMIL Group acquired the entire share capital of Supercapital Investment Limited which principal assets were loans receivable with fair value that approximated their carrying amount of HK\$41 million.

On 21 December 2005, the HMIL Group acquired the 100% equity interest of Apex Novel Limited through the acquisition of the entire share capital of Collier Assets Limited at the aggregate consideration of approximately HK\$49 million, which was based on the fair values of the leasehold property and bank loan of approximately HK\$85 million and HK\$36 million respectively at the date of acquisition.

The fair values of the identifiable assets and liabilities of the subsidiaries acquired during the year have no significant differences from their respective carrying amounts. The net assets acquired in the transactions, and the goodwill arising, are as follows:

	Year ended 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
Net assets acquired:			
Property, plant and equipment	—	—	85,146
Loan receivable	—	—	41,000
Other receivable	—	—	77
Bank balances and cash	—	2	6
Creditors and accrued charges	—	—	(297)
Bank loan	—	—	(36,000)
Due to parent company	—	(3,945)	—
	<u>—</u>	<u>(3,943)</u>	<u>89,932</u>
Goodwill arising on acquisition	—	3,943	945
	<u>—</u>	<u>3,943</u>	<u>945</u>
Total consideration	<u>—</u>	<u>—</u>	<u>90,877</u>
Satisfied by:			
Cash consideration	—	—	49,877
Issue of First New Note (note 28(i))	—	—	41,000
	<u>—</u>	<u>—</u>	<u>90,877</u>
Cash consideration	<u>—</u>	<u>—</u>	<u>90,877</u>

The acquired subsidiaries did not contribute any turnover or revenue to the HMIL Group for the year between the date of acquisition and the balance sheet date. There would have been no significant impacts to the HMIL Group's turnover and revenue had the acquisitions been completed on 1 January 2005.

The subsidiaries acquired during the year ended 31 December 2004 did not contribute significantly to the HMIL Group's cash flows or operating results for that year.

Analysis of outflow of cash and cash equivalents in respect of acquisition of subsidiaries

	Year ended 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
Cash paid	—	—	(49,877)
Bank balances and cash acquired	<u>—</u>	<u>2</u>	<u>6</u>
Net inflow (outflow) of cash and cash equivalents	<u>—</u>	<u>2</u>	<u>(49,871)</u>

34. DISPOSAL OF SUBSIDIARIES

	Year ended 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
Net assets disposed of:			
Investment properties	5,900	—	—
Property, plant and equipment	1,285	948	—
Investment in securities	—	717	—
Trade and other receivables	35,311	469	—
Loans receivable	464,389	—	351,082
Trading securities	—	1,233	—
Deposit	—	350	—
Bank balances and cash	118	406	—
Creditors and accrued charges	(5,515)	(5,365)	(266)
Due to a related company	(2,722)	—	—
Due to the sole director	(300)	—	—
Due to group companies	(419,389)	—	—
Dividends payable to the HMIL Group	<u>(30,000)</u>	<u>—</u>	<u>—</u>
	49,077	(1,242)	350,816
Goodwill on acquisition realised (note 33)	—	3,943	945
Investment properties revaluation reserve realised upon disposal of subsidiaries	(900)	—	—
Gain (Loss) on disposal of subsidiaries	<u>6,014</u>	<u>3,299</u>	<u>(195,481)</u>
Total consideration	<u>54,191</u>	<u>6,000</u>	<u>156,280</u>
Satisfied by:			
Cash received	34,192	4,000	156,280
Other receivable	—	2,000	—
Reclassification to interest in an associate	<u>19,999</u>	<u>—</u>	<u>—</u>
	<u>54,191</u>	<u>6,000</u>	<u>156,280</u>

Analysis of inflow of cash and cash equivalents in respect of disposal of subsidiaries:

	Year ended 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
Cash received	34,192	4,000	156,280
Bank balances and cash disposed of	<u>(118)</u>	<u>(406)</u>	<u>—</u>
Net inflow of cash and cash equivalents	<u>34,074</u>	<u>3,594</u>	<u>156,280</u>

The subsidiaries disposed of during the year had no contribution to turnover during the year ended 31 December 2005 (2004: loss of HK\$792,000; 2003: profit of HK\$43,236,000) for the period between the last balance sheet date and the date of disposal.

35. COMMITMENTS UNDER OPERATING LEASES

As at 31 December 2005, 2004 and 2003, the HMIL Group had total future minimum lease payments under non-cancellable operating leases in respect of office premises and equipment, which are payable as follows:

	At 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
Within one year	1,577	479	2,150
In the second to fifth year inclusive	<u>2,853</u>	<u>368</u>	<u>92</u>
	<u>4,430</u>	<u>847</u>	<u>2,242</u>

36. GENERAL BANKING FACILITIES

As at 31 December 2005, the HMIL did not have any contingent liabilities not provided for in the financial statements in respect of guarantee (2004: HK\$45,000,000; 2003: HK\$75,000,000) for banking facilities granted to subsidiaries, which were utilised by subsidiaries to the extent of approximately HK\$21,093,000 and HK\$60,915,000 in the years of 2004 and 2003 respectively.

37. PLEDGE OF ASSETS

As at 31 December 2005, 2004 and 2003, certain assets of the HMIL Group with the following carrying values have been pledged to secure general banking facilities granted to the HMIL Group:

	At 31 December		
	2003	2004	2005
	HK\$'000	HK\$'000	HK\$'000
Investments held for trading	15,950	228	—
Bank deposits	18,002	18,000	3,000
Leasehold land and buildings	—	—	80,220
	<u>33,952</u>	<u>18,228</u>	<u>83,220</u>

38. RELATED PARTY TRANSACTIONS

During the Relevant Periods, the following related party transactions were carried out:-

- (a) The HMIL Group granted unsecured loans to certain related companies in which the sole director of HMIL is also a director. During the year ended 31 December 2003, these loans were assigned from subsidiaries granting the loans to another subsidiary which became associate of the HMIL Group. As at 31 December 2003, the outstanding loans amounted to HK\$193,272,000 carried interest at a range of 6%-7% per annum or at prime rate plus 1%-3% per annum. Provision of HK\$38,311,000 had been made for non-repayment of the loans and related interest.
- (b) HMIL entered into an agreement with Willie International on 2 December 2003 to dispose 200,000,000 shares of Radford Capital to Willie International at a total consideration of HK\$24,000,000. At 31 December 2003, an amount of HK\$24,000,000 had been received from Willie International as deposit and included in creditors and accrued charges. The disposal was completed in January 2004.
- (c) The HMIL Group paid office rental amounting to HK\$2,078,000 to the wholly-owned subsidiaries of the then ultimate holding company, China United Holdings Limited ("CU Bermuda")/ Willie International, during the year ended 31 December 2003.
- (d) On 30 June 2003, HMIL, Willie International and CU Bermuda entered into an agreement under which approximately 18.68% of interest in HMIL and 48.53% interest in another company were transferred from CU Bermuda to Willie International in consideration of nominal cash and perpetual entitlement as detailed below. Under the agreement, Willie International made covenant that it and/or its subsidiaries would remain as the controlling shareholder of HMIL. In addition, under the agreement, CU Bermuda enjoyed a perpetual entitlement of 22% in the distribution of dividends, capital and assets by HMIL. HMIL was obliged to pay such distribution to CU Bermuda from the relevant portion of the distribution attributable to Willie International. Willie International made guarantee to CU Bermuda that if HMIL, for whatever reasons, failed to pay 22% of any distribution declared by HMIL to CU Bermuda, Willie International would compensate CU Bermuda with the equivalent amount. The covenants made by Willie International were perpetual in nature and binding on Willie International, whether or not Willie International or its subsidiaries held any interest in HMIL. During the year ended 31 December 2004, CU Bermuda confirmed in writing that the agreement had been cancelled and the guarantee made by Willie International as mentioned above was released accordingly.
- (e) As at 31 December 2005, 2004 and 2003, the HMIL Group's credit facilities to the extent of HK\$30,000,000 (2004: HK\$75,000,000; 2003: HK\$125,000,000) and HK\$66,000,000 (2004: HK\$30,000,000; 2003: HK\$50,000,000) were guaranteed by the substantial shareholder and a director of HMIL respectively.

- (f) During the year ended 31 December 2005 HMIL incurred interest expenses amounted to HK\$5,936,000 (2004: HK\$7,022,000; 2003: HK\$13,346,000) for convertible notes paid to the wholly-owned subsidiaries of the major shareholder.
- (g) During the year ended 31 December 2005, the HMIL Group received placing commission of HK\$690,000 (2004: HK\$825,000; 2003: HK\$ Nil) and financial advisory fee of HK\$38,000 (2004: HK\$400,000; 2003: HK\$ Nil) from the substantial shareholder.
- (h) The HMIL Group had granted securities margin loans to the directors of subsidiaries and the directors of the substantial shareholders as detailed in note 21 to the financial statements. The loans carried interest at 5% to 7.5% per annum and were repayable on demand.
- (i) During the year ended 31 December 2005 the Group paid short-term employee benefits of HK\$3,652,000 (2004: HK\$4,377,000; 2003: HK\$3,928,000) to key management personnel including directors.

39. POST BALANCE SHEET EVENTS

Other than disclosed elsewhere in the Financial Information, the HMIL Group entered into the following significant post balance sheet events:

- a) Subsequent to 31 December 2005, HMIL issued 250,000,000 ordinary shares at a price of HK\$0.2 per share to third parties and received total cash consideration of HK\$50,000,000. All shares ranked pari passu in all respects with the existing ordinary shares of HMIL.
- b) Subsequent to 31 December 2005, two staff members of a wholly-owned subsidiary of HMIL, which is a securities dealer, surrendered themselves to the police admitting that they had misappropriated clients' securities. An investigation is currently being conducted on this matter. The loss is covered by insurance and having taken appropriate legal advice, the directors estimate that the maximum loss, based on information unveiled to date, the Group is expected to bear under the insurance policy would be immaterial.

Moores Rowland Mazars
Chartered Accountants
Certified Public Accountants
Hong Kong

For illustrative purpose only, set out below is the unaudited pro forma statement of assets and liabilities of the Group after the completion of Transaction (the “Enlarged Group”). The pro forma statement of assets and liabilities is prepared in accordance with paragraph 4.29 of the Listing Rules for the purpose of providing investors with information to illustrate the effect of the Transaction on the financial position of the Group.

1. UNAUDITED PRO FORMA STATEMENT OF ASSETS AND LIABILITIES OF THE ENLARGED GROUP

The following is a summary of the unaudited pro forma statement of assets and liabilities of the Enlarged Group. It is based on the unaudited consolidated balance sheet of the Group as at 30 September 2005 extracted from the interim report of the Group for the six months ended 30 September 2005 and that of the HMIL as at 31 December 2005 extracted from the Accountants’ Report of HMIL Group set out in Appendix II and after making certain proforma adjustments resulting from the Transaction, assuming that the Transaction and the subsequent conversion of the Convertible Note into shares of HMIL have been completed as at 30 September 2005 for the purpose of illustrating how the Transaction might have affected the financial position of the Group as at 30 September 2005. As it is prepared for illustrative purpose only, and because of its nature, it may not give a true picture of the financial position of the Group as at 30 September 2005 or any future date.

The Hong Kong Institute of Certified Public Accountants has recently issued a number of new and revised Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards, and Interpretation (herein-after collectively referred to as the “new HKFRSs”), which are effective for accounting periods beginning on or after 1 January 2005. The Group has adopted these new HKFRSs in the interim financial statements for the six months ended 30 September 2005. Accordingly, the unaudited pro forma statement of assets and liabilities is prepared in accordance with the new HKFRSs and using accounting policies which are consistent with those adopted by the Group during the six months ended 30 September 2005.

The unaudited pro forma statement of assets and liabilities of the Enlarged Group should be read in conjunction with the audited financial information of the Group for the year ended 31 March 2005, the unaudited financial information of the Group for the six months ended 30 September 2005, and other financial information as set out in Appendix I to this circular.

UNAUDITED PRO FORMA STATEMENT OF ASSETS AND LIABILITIES

	The Group as at 30 September 2005 HK\$'000	HMIL as at 31 December 2005 HK\$'000	Pro forma Adjustments for the Transaction HK\$'000	<i>Notes</i>	Unaudited Pro forma assets and liabilities of the Enlarged Group after the Transaction HK\$'000
Non-current assets					
Investment properties	5,700	—			5,700
Property, plant and equipment	977	87,979			88,956
Goodwill	—	—	3,034	4	3,034
Intangible assets	—	2,283			2,283
Other assets	—	2,140			2,140
Interest in an associate	14	—			14
Available-for-sale investments	36,000	—	(2,000)	3	34,000
Long-term loans receivable	<u>205,000</u>	<u>—</u>			<u>205,000</u>
Total non-current assets	<u>247,691</u>	<u>92,402</u>			<u>341,127</u>
Current assets					
Trade and other receivables	235,064	228,076			463,140
Short-term loans receivable	42,926	45,534			88,460
Investments held for trading	289	68			357
Pledged bank deposits	—	3,000			3,000
Bank balances and cash	<u>5,839</u>	<u>71,589</u>	(100,000)	1	<u>(22,572)</u>
Total current assets	<u>284,118</u>	<u>348,267</u>			<u>532,385</u>

	The Group as at 30 September 2005 <i>HK\$'000</i>	HMIL as at 31 December 2005 <i>HK\$'000</i>	Pro forma Adjustments for the Transaction <i>HK\$'000</i>	<i>Notes</i>	Unaudited Pro forma assets and liabilities of the Enlarged Group after the Transaction <i>HK\$'000</i>
Current liabilities					
Trade and other payables	8,708	59,786			68,494
Due to a director	—	14,000			14,000
Due to related companies	—	998			998
Bank overdrafts	—	21,425			21,425
Interest-bearing borrowings	—	146,000			146,000
Tax payable	<u>2,455</u>	<u>4,798</u>			<u>7,253</u>
Total current liabilities	<u>11,163</u>	<u>247,007</u>			<u>258,170</u>
Net current assets	<u>272,955</u>	<u>101,260</u>			<u>274,215</u>
Total assets less current liabilities	<u>520,646</u>	<u>193,662</u>			<u>615,342</u>
Non-current liabilities					
Convertible notes	<u>—</u>	<u>131,000</u>	(131,000)	2	<u>—</u>
NET ASSETS	<u><u>520,646</u></u>	<u><u>62,662</u></u>			<u><u>615,342</u></u>

Notes:

- (1) This represents the adjustment in relation to the total consideration of HK\$100 million for the acquisition of HK\$131 million convertible note issued by HMIL which will be satisfied by cash. Since the cash and bank balances of the Group as at 30 September 2005 were HK\$5,839,000 and the consideration payable under the Transaction is HK\$100 million, the adjustment results in a negative cash and bank balances position for the Enlarged Group. It should be noted that this is merely a pro forma statement and does not represent the actual financial position of the Enlarged Group after completion of the Transaction. The balance of the consideration will be settled by the Group upon completion using the then available internal resources of the Group, including but not limited to proceeds from the placings completed on 24 April 2006 and 22 May 2006 respectively.
- (2) This represents the conversion of the convertible note into approximately 50.07% HMIL's shares.

- (3) This represents of the Company's existing investment in HMIL in the sum of HK\$2 million being reclassified from Available-for-sale investments to Interest in subsidiaries.
- (4) HMIL will become subsidiaries of the Group upon conversion of Convertible Note into shares of HMIL. The pro forma adjustments reflect the recognition of estimated goodwill of approximately HK\$3,034,000 arising from completion of the Transaction and the subsequent conversion of the Convertible Note into shares of HMIL (see Note (5) below) on the basis that no impairment charges concerning the above estimated goodwill is considered necessary.
- (5) Under Generally Accepted Accounting Principles in Hong Kong, the Group will apply the purchase method to account for the conversion of the Convertible Note into the shares of HMIL ("the Conversion"). In applying the purchase method, the identifiable assets and liabilities of HMIL would be recorded in the unaudited pro forma statement of assets and liabilities of the Enlarged Group at their fair values at the date of completion. Any goodwill or fair value adjustment arising on the Conversion will be determined as the excess or deficit of the purchase consideration deemed to be incurred by the Group over the Group's interests in the net fair value of the identifiable assets and liabilities of HMIL at the date of completion of the Conversion.

For the purpose of preparing the unaudited pro forma statement of assets and liabilities of the Enlarged Group after the Conversion, the net book value of the identifiable assets and liabilities of HMIL, as extracted from the accountants report on HMIL set forth in Appendix II to this Circular, is applied in the calculation of the estimated fair value adjustment arising from the Conversion. The actual fair value adjustment arising at the date of completion of the Conversion may be different from the estimated fair value adjustment as shown in Note (4) above because the fair value of the assets and liabilities of HMIL at the date of completion of the Conversion may be substantially different from those used in the preparation of the unaudited pro forma statement of assets and liabilities of the Enlarged Group contained herein.

**2. REPORT ON THE UNAUDITED PRO FORMA STATEMENT OF ASSETS AND
LIABILITIES OF THE ENLARGED GROUP**

Set forth below is the text of the report, prepared for the sole purpose of incorporation in this circular received by the Directors from K.S. Liu & Company, CPA Limited, Certified Public Accountants, Hong Kong, in connection with the unaudited pro forma statement of assets and liabilities of the Enlarged Group set out in Appendix III to this circular:

**K.S. Liu & Company, CPA Limited***Certified Public Accountants*

廖廣生會計師事務所有限公司

Unit 1003, 10/F.,
Rightful Centre,
12 Tak Hing Street,
Tsim Sha Tsui, Kowloon,
Hong Kong

24 May 2006

The Directors
Inner Mongolia Development (Holdings) Limited
31/F., China United Centre,
28 Marble Road,
North Point,
Hong Kong.

Dear Sirs

**Inner Mongolia Development (Holdings) Limited (the “Company”) and its subsidiaries
(collectively the “Group”) and Hennabun Management International Limited and its
subsidiaries (collectively the “Enlarged Group”)**

We report on the unaudited pro forma statement of assets and liabilities of the Enlarged Group (the “Pro Forma Statement”) set out on pages 94 and 99 under the heading of “Unaudited pro forma statement of assets and liabilities of the Enlarged Group” in Appendix III of the Company’s circular dated 24 May 2006 (the “Circular”) in connection with the Company’s proposed purchase of the Convertible Note pursuant to the Conditional Agreement dated 21 April 2006 for the sale and purchase of a convertible note issued by Hennabun Management International Limited (the “Transaction”), which has been prepared by the directors of the Company, for illustrative purposes only, to provide information about how the Transaction might have affected the relevant financial information presented.

Respective Responsibilities of Directors of the Company and Reporting Accountants

It is the responsibility solely of the directors of the Company to prepare the Pro Forma Statement in accordance with paragraph 4.29 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”) and with reference to Accounting Guideline 7 “Preparation of Pro Forma Financial Information for Inclusion in Investment Circulars” issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”).

It is our responsibility to form an opinion, as required by paragraph 4.29(7) of the Listing Rules, on the Pro Forma Statement and to report our opinion to you. We do not accept any responsibility for any reports previously given by us on any financial information used in the compilation of the Pro Forma Statement beyond that owed to those to whom those reports were addressed by us at the dates of their issue.

Basis of opinion

We conducted our engagement in accordance with the Hong Kong Standard on Investment Circular Reporting Engagements 300 “Accountants’ Reports” on Pro Forma Financial Information in Investment Circulars” issued by the HKICPA. Our work consisted primarily of comparing the unadjusted financial information with source documents, considering the evidence supporting the adjustments and discussing the Pro Forma Statement with the directors of the Company. This engagement did not involve independent examination of any of the underlying financial information.

We planned and performed our work so as to obtain the information and explanations we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Pro Forma Statement has been properly compiled by the directors of the Company on the basis stated, that such basis is consistent with the accounting policies of the Group and that the adjustments are appropriate for the purposes of the Pro Forma Statement as disclosed pursuant to paragraph 4.29(1) of the Listing Rules.

The Pro Forma Statement is for illustrative purposes only, based on the adjustments and assumptions of the directors of the Company, and, because of its hypothetical nature, does not provide any assurance or indication that any event will take place in the future and may not be indicative of the financial position of the Group as at 30 September 2005 or any future date.

Opinion

In our opinion:

- a. the Pro Forma Statement has been properly compiled by the directors of the Company on the basis stated;
- b. such basis is consistent with the accounting policies of the Group; and
- c. the adjustments are appropriate for the purposes of the Pro Forma Statement as disclosed pursuant to paragraph 4.29(1) of the Listing Rules.

Yours faithfully
K.S. Liu & Company, CPA Limited
Certified Public Accountants
Hong Kong
Liu Kwong Sang
FCCA (Practising) P01586

1. RESPONSIBILITY STATEMENT

This circular includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Group. The Directors collectively and individually accept full responsibility for the accuracy of the information contained in this circular and confirm, having made all reasonable enquiries, that to the best of their knowledge and belief, there are no other facts not contained herein the omission of which would make any statement contained in this circular misleading.

2. DISCLOSURE OF INTERESTS

(a) Interests of Directors

As at the Latest Practicable Date, the interests and short positions of the Directors and chief executives of the Company in the Shares, underlying Shares and debentures of the Company or any associated corporation (within the meaning of Part XV of the SFO) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they are taken or deemed to have under such provisions of the SFO), the Model Code for Securities Transactions by Directors of Listed Issuers contained in Appendix 10 of the Listing Rules and which were required to be entered into the register required to be kept under section 352 of the SFO were as follows:

Long positions in Shares

Name of director	Capacity	Number of Shares	Approximate % of shareholding
Yau Shum Tek, Cindy	Interest of controlled corporation	26,730,000 (Note)	2.73%

Note: As at the Latest Practicable Date, Ms Yau Shum Tek, Cindy, the Chairman of the Company, wholly-owns and controls Red China Holdings Limited and Capital Sun Industries Limited. Capital Sun Industries Limited wholly-owns Future Star Group Limited. Each of Red China Holdings Limited and Future Star Group Limited holds 50% of the issued share capital of Mainland Talent Developments Limited. Mainland Talent Developments Limited wholly owns Hastings Gold Limited which in turn wholly owns Pacific Rim Investment Management Enterprises Limited. Pacific Rim Investment Management Enterprises Limited holds 26,730,000 shares of the Company.

Interests in equity derivatives of the Company

Name of director	Date of grant	Exercisable period	Subscription price per share HK\$	Number of share options and underlying shares	Percentage of the Company's issued share capital at Latest Practicable Date
Kwong Wai Tim, William	16.1.2004	16.1.2004 to 15.1.2009	1.2	1,500,000	0.15%
Lai Ming Wai	16.1.2004	16.1.2004 to 15.1.2009	1.2	1,500,000	0.15%
				<u>3,000,000</u>	<u>0.30%</u>

Note: These share options were held by the relevant directors as beneficial owners.

Save as disclosed above, as at the Latest Practicable Date, none of the Directors or chief executives of the Company had any interests and short positions in the Shares, underlying Shares and debentures of the Company or any associated corporation (within the meaning of Part XV of the SFO) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they are taken or deemed to have under such provisions of the SFO), the Model Code for Securities Transactions by Directors of Listed Companies and which were required to be entered into the register required to be kept under section 352 of the SFO.

(b) **Interests of Shareholders**

As at the Latest Practicable Date, so far as is known to the Directors and the chief executives of the Company, there are no Shareholders (other than a Director or chief executive of the Company) who had an interest or short position in the Shares and underlying Shares which fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or who are, directly or indirectly interested in 10 per cent. or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at a general meeting of any member of the Enlarged Group.

(i) *The Group*

Name of Shareholder	Capacity	Number of Shares	Approximate % of shareholding
Chuang Eugene Yue-chien	Beneficiary of a trust	87,300,000	8.94%
Moon Light Investments Group Limited	Interest of controlled corporation	87,300,000	8.94%
Sunderland Properties Limited	Beneficial owner	87,300,000	8.94%
Heritage International Holdings Limited	Interest of controlled corporation	65,500,000	6.70%
Coupeville Limited	Interest of controlled corporation	65,500,000	6.70%
Dollar Group Limited	Beneficial owner	65,500,000	6.70%

(ii) *HMIL Group*

(a) Name of Shareholder	Number of Shares	Approximate % of shareholding
Grand Wishes Limited (<i>Note 1</i>)	309,633,334	35.55
Bloom Glory Limited	150,000,000	17.22
Au Shuk Yee, Sue	100,000,000	11.48

Note 1: A wholly-owned subsidiary of Willie International Holdings Limited

- (b) Chung Nam Nominees Limited, an indirect wholly-owned subsidiary of HMIL, holds 40% of Chung Nam Commodities Limited (an indirect 60% held subsidiary of HMIL).

Save as disclosed above, the Directors and the chief executives of the Company are not aware that there is any person (other than a Director or chief executive of the Company) who, as at the Latest Practicable Date, had an interest or short position in the Shares and underlying Shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or who is, directly or indirectly, interested in 10 per cent. or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at a general meeting of any other member of the Enlarged Group.

As at the Latest Practicable Date:-

- (i) none of the Directors had any direct or indirect interests in any assets which have since 31 March 2005 (being the date to which the latest published audited accounts of the Group were made up) been acquired or disposed of by or leased to any members of the Enlarged Group, or are proposed to be acquired or disposed of by or leased to any members of the Enlarged Group;
- (ii) none of the Directors was materially interested in any contracts or arrangements entered into by any members of the Enlarged Group subsisting as at the Latest Practicable Date which is significant in relation to the business of the Enlarged Group.

3. EXPERTS AND CONSENTS

The following is the qualification of the experts who have given opinion or advice which are contained in this circular:

Name	Qualification
K.S. Liu & Company, CPA Limited (“K.S. Liu”)	certified public accountants in Hong Kong
Moore Rowland Mazars (“Moore”)	certified public accountants in Hong Kong

As at the Latest Practicable Date, K.S. Liu and Moore did not have:-

- (a) any direct or indirect interest in any assets which have since 31 March 2005 (being the date to which the latest published audited accounts of the Company were made up) been acquired or disposed of by or leased to any member of the Enlarged Group, or are proposed to be acquired or disposed of by or leased to any member of the Enlarged Group; and
- (b) any shareholding in any member of the Enlarged Group or the right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in any member of the Enlarged Group.

K.S. Liu and Moores have given and have not withdrawn their consent to the issue of this circular with the inclusion of their reports or letters, as the case may be, and reference to their names in the form and context in which they respectively appear.

4. SERVICE CONTRACTS

As at the Latest Practicable Date, none of the Directors had entered into any service agreement with any members of the Group.

5. LITIGATION

As at the Latest Practicable Date, no member of the Enlarged Group was engaged in any litigation or arbitration proceedings of material importance and there was no litigation or claim of material importance known to the Directors to be pending or threatened against any member of the Enlarged Group.

6. COMPETING INTERESTS

As at the Latest Practicable Date, none of the Directors and his/her respective associates was considered to have an interest in a business which competes or is likely to compete, either directly or indirectly, with the business of the Group other than those businesses to which the Directors and his/her associates were appointed to represent the interests of the Company and/or the Group.

7. MATERIAL CONTRACTS

The following contracts (not being contracts entered into in the ordinary course of business) have been entered into by members of the Enlarged Group within the two years preceding the date of this circular and is or may be material.

- (i) a placing agreement dated 7 January 2005 entered into between the Company and Uni-Alpha Securities Limited relating to the placing of 300,000,000 shares of the Company;
- (ii) a placing agreement dated 13 June 2005 and termination deed dated 6 January 2006 entered into between the Company and Uni-Alpha Securities Limited relating to the placing of convertible notes by the Company;
- (iii) an agreement dated 13 June 2005 and supplemental agreement dated 24 August 2005 and termination deed dated 1 February 2006 entered into between Goodnews Resources Limited and the Company relating to the subscription of 35,000,000 shares in the capital of the Company;

- (iv) a placing agreement dated 13 June 2005 and supplemental agreement dated 17 October 2005 and termination deed dated 6 January 2006 entered into between the Company and Uni-Alpha Securities Limited relating to a placing of 40,000,000 new shares in the capital of the Company;
- (v) an underwriting agreement dated 13 June 2005 entered into between the Company and Uni-Alpha Securities Limited relating to 20,000,000 new shares in the capital of the Company;
- (vi) an underwritten agreement dated 1 December 2005 entered into between the Company and Chung Nam Securities Limited relating to 44,000,000 new shares in the capital of the Company;
- (vii) an underwritten agreement dated 30 December 2005 entered into between the Company, Get Nice Investment Limited and Kingston Securities Limited relating to 250,000,000 new shares in the Company;
- (viii) a placing agreement dated 30 December 2005 entered into between the Company and Get Nice Investment Limited relating to 750,000,000 new shares in the capital of the Company;
- (ix) a conditional agreement dated 10 April 2006 entered into between Willie International Holdings Limited and Freeman China Limited, a wholly-owned subsidiary of the Company, relating to the sale and purchase of the entire issued share capital of Leapfly Limited; and
- (x) the Agreement; and
- (xi) the Convertible Note.

8. GENERAL

- (i) The secretary of the Company is Mr Ken Chan, who is a member of the Hong Kong Institute of Chartered Secretaries.
- (ii) The qualified accountant of the Company is Mr Wong Kwok Tai, who is a fellow member of the Hong Kong Institute of Certified Public Accountants.
- (iii) The share registrar and transfer office of the Company in Hong Kong is Secretaries Limited, of 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong.
- (iv) The English version of this circular shall prevail over the Chinese text.

9. DOCUMENTS AVAILABLE FOR INSPECTION

Copies of the following documents are available for inspection at the principal place of business of the Company in Hong Kong at 31st Floor, China United Centre, 28 Marble Road, North Point, Hong Kong up to and including the date of the EGM:

- (i) the memorandum and articles of association of the Company;
- (ii) the material contracts as disclosed in paragraph 7 of this Appendix II;
- (iii) the Annual Reports of the Company for the years ended 31 March 2004 and 31 March 2005;
- (iv) (a) circular dated 4 July 2005 in relation to the placing of new consolidated shares, placing of convertible notes, subscription of new consolidated shares, proposed share consolidation and proposed change of company name;
- (b) circular dated 13 September 2005 in relation to the connected transaction and extension of the completion date in relation to the subscription of new shares;
- (c) circular dated 16 February 2006 in relation to the placing of new shares and refreshment of the issue mandate;
- (d) circular dated 18 April 2006 in relation to the proposed change of name, proposed capital reorganisation and discloseable transaction; and
- (e) circular dated 24 April 2006 in relation to discloseable transactions.
- (v) the accountants' report from Moores dated 24 May 2006, the text of which is set out in Appendix II to this circular;
- (vi) the report from K.S. Liu on the unaudited pro forma statement of assets and liabilities of the enlarged Group dated 24 May 2006, the text of which is set out in Appendix III to this circular; and
- (vii) the letters of consent referred to in the paragraph headed "Experts and consents" in this Appendix.



INNER MONGOLIA DEVELOPMENT (HOLDINGS) LIMITED

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 279)

NOTICE IS HEREBY GIVEN that an extraordinary general meeting of Inner Mongolia Development (Holdings) Limited (the “Company”) will be held at 30th Floor, China United Centre, 28 Marble Road, North Point, Hong Kong at 9:00 a.m. on Friday, 9 June 2006 for the purpose of considering and, if thought fit, passing the following resolution which will be proposed as an ordinary resolution:-

ORDINARY RESOLUTION

1. **“THAT:**

- (a) the entering into of the conditional agreement (“Agreement”) dated 21 April 2006 and supplemental agreement dated 2 May 2006 between Yearwise Finance Limited (“Yearwise”) and Equity Spin Investments Limited (“Equity Spin”), a wholly-owned subsidiary of the Company pursuant to which Equity Spin agreed to purchase from Yearwise all Yearwise’s rights, title and interests in the convertible note (“Convertible Note”) issued by Hennabun Management International Limited in the principal amount of HK\$131,000,000 due on 20 September 2015 for a consideration of HK\$100,000,000 (a copy of the Agreement has been produced to this meeting marked “A” and initialled by the chairman of the meeting for identification purpose) be and is hereby approved, ratified and confirmed and the transactions contemplated thereunder be and are hereby approved and the directors of the Company be and are hereby authorised to implement the transactions referred to in the Agreement and to do all such acts and things and sign such documents as they shall in the absolute discretion and consider necessary or desirable to give effect to the Agreement and the arrangements contemplated thereunder; and
- (b) the exercise of conversion rights under the Convertible Note in full by Equity Spin as soon as practicable after completion of the Agreement, subject to all necessary approvals from the regulatory authorities to the extent required being obtained, be and is hereby approved and the directors of the Company be and are hereby authorised to do all such acts and things and sign such documents as they shall in the absolute discretion and consider necessary or desirable to give effect to the conversion of the Convertible Note and the arrangements contemplated thereunder.”

By order of the Board
Yau Shum Tek, Cindy
Chairman

Dated 24 May 2006

NOTICE OF EXTRAORDINARY GENERAL MEETING

Notes:

1. To be valid, the instrument appointing a proxy must be in writing under the hand of the appointor or of his attorney authorised in writing or if the appointor is a corporation, either under seal or under the hand of an officer or attorney duly authorised.
2. Any member of the Company entitled to attend and vote at the meeting shall be entitled to appoint another person as his proxy to attend and vote instead of him. A proxy duly appointed pursuant to the articles of association of the Company is entitled to vote on a show of hands at the meeting. On a poll votes may be given either personally or by proxy. A proxy need not be a member of the Company. A member may appoint more than one proxy to attend on the same occasion.
3. The instrument appointing a proxy and the power of attorney or other authority, if any, under which it is signed or a notarially certified copy of that power or authority must be deposited at the Company's share registrar in Hong Kong, Secretaries Limited, at 26th Floor, Tesbury Centre, 28 Queen's Road East, Hong Kong not less than 48 hours before the time for holding the meeting or the adjourned meeting or poll (as the case may be) at which the person named in such instrument proposes to vote, and in default the instrument of proxy shall not be treated as valid.
4. Where there are joint registered holders of any share, any one of such persons may vote at the meeting, either personally or by proxy, in respect of such share as if he were solely entitled thereto; but if more than one of such joint holders be present at the meeting personally or by proxy, that one of the said persons so present whose name stands first on the register of members in respect of such share shall alone be entitled to vote in respect thereof.