

REPORT OF THE DIRECTORS

Board of Directors and Company Secretary of Founder (Hong Kong) Limited



Prof. Wang Xuan

Chairman

Prof. Cheung Yuk Fung

Executive Director



Mr. Cheung Shuen Lung

Executive Director
and President

Prof. Wu Shu Qing

Non-executive Director



Prof. Ren Yan Shen

Non-executive Director

Dr. Hu Hung Lick, Henry

Independent
Non-executive Director



Mr. Li Fat Chung

Independent
Non-executive Director

Mr. Chan Yiu Kwong

Company Secretary



REPORT OF THE DIRECTORS *(Continued)*

The directors herein present their report and the audited financial statements of the Company and the Group for the year ended 31 December 1998.

PRINCIPAL ACTIVITIES

The principal activities of the Company are investment holding, systems integration and the trading of computer products. The principal activities of the subsidiaries and jointly controlled entities are detailed in notes 14 and 15, respectively, to the financial statements. There were no changes in the nature of the Group's principal activities during the year.

SEGMENTED INFORMATION

An analysis of Group turnover and contribution to operating loss by principal activity and geographical area of operations for the year ended 31 December 1998 is as follows:

	Turnover HK\$'000	Contribution HK\$'000
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By principal activity:		
Software development and systems integration	1,096,929	239,757
Sales of computers and related products	1,062,745	23,706
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	<u>2,159,674</u>	263,463
General, administrative and financial expenses		425,848
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		(162,385)
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By geographical area:		
The People's Republic of China (the "PRC"):		
Hong Kong	207,580	23,253
Elsewhere	1,918,081	217,359
Others	34,013	22,851
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	<u>2,159,674</u>	263,463
General, administrative and financial expenses		425,848
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		(162,385)
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RESULTS AND DIVIDENDS

The Group's loss for the year ended 31 December 1998 and the state of affairs of the Company and the Group at that date are set out in the financial statements on pages 27 to 57.

The directors do not recommend the payment of any dividends in respect of the year.

SUMMARY OF FINANCIAL INFORMATION

A summary of the published results of the Group for the last five financial years, and of its assets and liabilities as at 30 June 1995 and 31 December 1995, 1996, 1997 and 1998 is set out below.

RESULTS

	Year ended 31 December				
	1998	1997	1996	1995	1994
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
TURNOVER	2,159,674	1,973,409	1,483,351	1,096,233	847,531
OPERATING PROFIT/(LOSS)	(162,385)	142,534	126,934	113,090	63,627
Share of losses of jointly controlled entities	(3,265)	—	—	—	—
PROFIT/(LOSS) BEFORE TAXATION	(165,650)	142,534	126,934	113,090	63,627
Taxation	(46)	757	(131)	(3,819)	(3,707)
NET PROFIT/(LOSS) ATTRIBUTABLE TO SHAREHOLDERS	(165,696)	143,291	126,803	109,271	59,920

ASSETS AND LIABILITIES

	31 December 1998	31 December 1997	31 December 1996	31 December 1995	30 June 1995
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
TOTAL ASSETS	1,163,392	1,362,704	1,241,511	1,030,461	609,967
TOTAL LIABILITIES	490,736	551,953	527,889	535,545	427,256
NET ASSETS	672,656	810,751	713,622	494,916	182,711

SUMMARY OF FINANCIAL INFORMATION (Continued)

Notes:

- (1) The combined results for the year ended 31 December 1994 have been extracted from the accountants' report included in the Company's prospectus dated 12 December 1995. The combined results for the year ended 31 December 1995 were prepared based on the Group's combined results for the six months ended 30 June 1995 as extracted from the same accountants' report, and the consolidated results for the six months ended 31 December 1995 as extracted from the Company's 1995 annual report. The combined results were prepared on a pro forma basis to reflect the Group reorganisation as set out in the accountants' report included in the Company's prospectus dated 12 December 1995.
- (2) The combined assets and liabilities of the Group at 30 June 1995 as stated above were prepared on a pro forma basis to reflect the Group reorganisation as set out in the accountants' report included in the Company's prospectus dated 12 December 1995.

ACCOUNTING POLICIES

The significant accounting policies of the Company and the Group are set out in note 1 to the financial statements.

FIXED ASSETS AND INVESTMENT PROPERTIES

Details of movements in the fixed assets and investment properties of the Company and the Group are set out in notes 11 and 12 to the financial statements, respectively.

SUBSIDIARIES

Particulars of the Company's subsidiaries are set out in note 14 to the financial statements.

JOINTLY CONTROLLED ENTITIES

Particulars of the Group's jointly controlled entities are set out in note 15 to the financial statements.

BORROWINGS

Details of the Company's and the Group's borrowings at 31 December 1998 are set out in notes 18 and 19 to the financial statements.

SHARE CAPITAL AND SHARE OPTIONS

Details of movements in the Company's share capital and share options during the year and the reasons for the issues are set out in note 20 to the financial statements.

RESERVES

Details of movements in the reserves of the Company and the Group during the year are set out in note 21 to the financial statements.

DIRECTORS

The directors of the Company during the year were:

Executive directors:

Wang Xuan

Cheung Shuen Lung

Zhang Zhao Dong

Zhao Wei

Xiao Jian Guo

Zhou Ning

Jiang Bi Jin (appointed on 25 May 1998)

Non-executive directors:

Wu Shu Qing

Ren Yan Shen

Hu Hung Lick, Henry*

Li Fat Chung*

** Independent non-executive directors*

Subsequent to the balance sheet date, on 15 April 1999, Zhang Zhao Dong, Zhao Wei, Xiao Jian Guo, Zhou Ning and Jiang Bi Jin resigned as directors of the Company. On the same date, Cheung Yuk Fung was appointed as a director of the Company.

In accordance with the Company's articles of association, Ren Yan Shen and Cheung Yuk Fung will retire and, being eligible, will offer themselves for re-election at the forthcoming annual general meeting.

DIRECTORS' SERVICE CONTRACTS

Each of the executive directors of the Company has entered into a service contract with the Company for an initial term of five years and thereafter, subject to re-election by the shareholders of the Company. The service contract can be terminated by either the director concerned or the Company giving to the other not less than one year's notice.

The service contracts with Zhang Zhao Dong, Zhao Wei, Xiao Jian Guo, Zhou Ning and Jiang Bi Jin were terminated as a consequence of the resignation as directors of the Company on 15 April 1999.

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

DIRECTORS' INTERESTS IN CONTRACTS

No director had a beneficial interest in any material contract to which the Company or any of its subsidiaries was a party during the year.

DIRECTORS' RIGHTS TO ACQUIRE SHARES

Pursuant to the Company's share option scheme, as further detailed in note 20 to the financial statements, in prior years the Company granted options in favour of the following directors:

Name of director	Number of share options at 31 December 1998
Wang Xuan	10,800,000
Cheung Shuen Lung	9,360,000
Zhang Zhao Dong	9,360,000
Zhao Wei	9,360,000
Xiao Jian Guo	9,360,000
Zhou Ning	9,360,000
	57,600,000

All the above share options are exercisable from 21 December 1998 to 6 December 2005 at an exercise price of HK\$1.397 per ordinary share. The exercise price is adjustable in accordance with the provisions of the share option scheme.

Apart from the foregoing, at no time during the year was the Company or any of its subsidiaries a party to any arrangement to enable the Company's directors, their respective spouse or children under 18 years of age of any such director or chief executive to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other related body corporate.

DIRECTORS' INTERESTS IN SHARES

At 31 December 1998, Mr Cheung Shuen Lung and his wife each had a 50% interest in the share capital of Swan-City International Group Limited which in turn held 25,346,058 shares of the Company. As defined by the Securities (Disclosure of Interests) Ordinance ("SDI Ordinance"), Mr Cheung Shuen Lung had corporate interests in these 25,346,058 shares of the Company.

DIRECTORS' INTERESTS IN SHARES (Continued)

In addition to the above, Mr Cheung Shuen Lung has non-beneficial personal equity interests in certain subsidiaries held for the benefit of the Company solely for the purpose of compliance with the minimum company membership requirements.

Save as disclosed above and as disclosed under the heading "Directors' rights to acquire shares", none of the directors or their associates had any personal, family, corporate or other interests in the securities of the Company or any of its associated corporations as defined in the SDI Ordinance and recorded in the register required to be maintained pursuant to Section 29 thereof.

SUBSTANTIAL SHAREHOLDERS

At 31 December 1998, the following interests of 10% or more of the share capital of the Company were recorded in the register of interests required to be kept by the Company pursuant to Section 16(1) of the SDI Ordinance:

Name of shareholder	Number of shares held
Peking University	369,527,609
Peking University Founder Group Corporation ("Peking Founder")	369,527,609

Note: Peking Founder is wholly-owned by Peking University. The interests disclosed under Peking University represent its deemed interests in the shares of the Company by virtue of its interest in Peking Founder.

DISTRIBUTABLE RESERVES

At 31 December 1998, the Company's reserves available for cash distribution calculated in accordance with the provisions of Section 79B of the Companies Ordinance amounted to HK\$26,853,000. The share premium of HK\$506,153,000 may be distributed in the form of fully paid bonus shares.

MAJOR SUPPLIERS AND CUSTOMERS

In the year under review, sales to the five largest customers accounted for less than 30% of total sales for the year.

Purchases from the five largest suppliers accounted for 36% (1997: 36%) of the total purchases for the year and purchases from the largest supplier included therein amounted to 15% (1997: 15%).

As far as the directors are aware, neither the directors, their associates, nor those shareholders which to the knowledge of the directors own more than 5% of the Company's share capital had any interest in the five largest customers and suppliers.

PENSION SCHEME

The Group has established defined contribution pension schemes for certain of its qualified employees. The assets of the schemes are held and managed by independent professional fund managers.

RELATED PARTY TRANSACTIONS

The related party transactions undertaken by the Group during the year are set out in note 10 to the financial statements.

The independent non-executive directors of the Company have reviewed and confirmed to the board of directors their opinion about the related party transactions as disclosed in note 10 to the financial statements were conducted in the ordinary and usual course of the Group's business and are fair and reasonable so far as the shareholders of the Company are concerned.

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES

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

COMPLIANCE WITH THE CODE OF BEST PRACTICE

In the opinion of the directors, the Company has complied with the Code of Best Practice as set out in Appendix 14 of the Listing Rules of The Stock Exchange of Hong Kong Limited throughout the accounting year covered by the annual report. Independent non-executive directors are not appointed for a specific term but are subject to retirement by rotation and re-election at the annual general meeting of the Company in accordance with the Company's articles of association.

REPORT OF THE DIRECTORS *(Continued)*

AUDITORS

Ernst & Young retire and a resolution for their reappointment as auditors of the Company will be proposed at the forthcoming annual general meeting.

ON BEHALF OF THE BOARD

Wang Xuan
Chairman

Hong Kong 15 April 1999