YANTAI CHANGYU PIONEER WINE COMPANY LIMITED

1999 Annual Report

April , 18, 2000

YANTAI CHANGYU PIONEER WINE COMPANY LIMITED

(a joint stock limited company incorporated in the People's Republic of China with limited liability)

1999 Annual Report

I. BRIEF INTRODUCTION TO THE COMPANY

Yantai Changyu Pioneer Wine Company Limited (the "Company") is situated in Yantai, the region that produces the finest grapes and wine in the PRC.The predecessor of the Company is Yantai Changyu Pioneer Wine Company, the establishment of which dated back in 1892. With a history of 108 years, the Company is the first industrial winery in China.

1. Legal Name in Chinese: **烟台张裕葡萄酿酒股份有限公司**
2. Legal Name in English: Yantai Changyu Pioneer Wine Company Limited
   Legal Representative: Sun Li-qiang
3. Secretary to the Board of Directors: Qu Wei-min
   Contact Address: 174 Shihuiyao Road, Yantai City, Shandong Province, the PRC
   Telephone: 0535-6247214, 6647864
   Facsimile: 0535-6247214, 6244616
   E-Mail: quwm@changyu.com.cn
   Authorized Representative of the Securities Affairs: Lin Wen-bing
   Contact Address: 174 Shihuiyao Road, Yantai City, Shandong Province, the PRC
   Telephone: 0535-6648741
   Facsimile: 0535-6244616
4. Registered Address: 56 Dama Road, Yantai City, Shandong Province, the PRC
   Office Address: 174 Shihuiyao Road, Yantai City, Shandong Province, the PRC
   Postal Code: 264001
   Web Site: http://www.changyu.com.cn
   E-Mail: stock@changyu.com.cn
5. The newspapers on which the Company's information is disclosed: "China Securities Newspaper", "Securities Times" in the PRC and "Hong Kong Commercial Daily" outside the PRC.
   Web Site for carrying the report: http://www.cninfo.com.cn
   Annual Report kept at: Securities Department
   Telephone: 0535-6647864
   Location of listing of the B Shares: Shenzhen Stock Exchange
   Abbreviation of the B Shares: Changyu B
   Code Number of the B Shares: 2869

II. SUMMARY OF ACCOUNTING AND FINANCIAL INFORMATION

1. Summary of Financial Information for the Year Ended 31st December, 1999(the Reporting Period)

Item:	Amount RMB' 000
Profit before taxation	110,132
Profit after taxation	89,435
Net profit after irregular profit and loss	
Gross profit	322,412
Other income	2,041
Operation profits	107,300
Investment earnings	
Net of non-operating income and expenses	2,041
Subsidy income	
Net cash flows from operating activities	74,946
Net increase in cash and cash equivalents	-19,910

2. Differences in Net Profit under the PRC Accounting Standards and International Accounting Standards

The net profit of the Company of the Reporting Period was RMB 92,321,626 as audited by Arthur Andersen ▪ Hua Qiang Certified Public Accountants according to the PRC Accounting Standards and RMB89,434,626 after adjusted by Arthur Andersen & Co., according to the International Accounting Standards. Major differences in using the International Accounting Standards and the PRC Accounting Standards are as follows:

	RMB' 000
Net profit as stated under the PRC Accounting Standards	92,321,626
Impact to the net profit as stated under the International Accounting Standards:	
Adjustment on administrative expenses using accrual basis	
--Write-off of deemed input value added tax	500,000
--Deferred tax	(3,387,000)
Restated under the International Accounting Standards	89,434,626

3. Principal Accounting and Financial Information for the three Years ended 31st December, 1999

Items	1999.1-12	1998.1-12	1997.1-12
ales	583,175,000	530,208,000	375,811,000
Profit after taxation	89,435,000	84,431,000	76,736,000
Total assets	832,683,000	715,962,000	709,352,000
Total shareholders' equity	586,380,000	531,145,000	479,964,000
Earnings per Share (RMB)	0.39	0.37	0.34
Net assets value per Share (RMB)	2.57	2.33	2.11
Return on shareholders' equity (%)	15.3	15.9	16.0
Net assets value per Share after adjustment	2.44	2.19	2.08
Earnings per Share computed on weighted average basis (RMB)	0.39	0.37	0.36
Earnings per Share after irregular profit and loss			
Net cash flows per Share from operating activities	0.33	0.15	

Notes:

(1) The foregoing data and ratios are obtained based on the information contained in the consolidated financial statements.

(2) The share capital of the Company kept unchanged in the Reporting Period.

(3) Fully diluted method used for computation:

Earnings per Share = Net profit/Total number of Shares issued at period end

Net assets value per Share = Shareholders' equity at year end/Total number of Shares issued at year end

Return on shareholders' equity = Net profit/Year end shareholders' equity×100%

Net assets value per Share after adjustment = (Shareholders' equity at year end-Net accounts receivable over three years- Deferred and prepaid expenses-Net loss for non-disposed total assets-initial costs-Deferred and prepaid expenses for long term-balance (negative) for revolving funds for housing)/Total number of Shares issued at period end

Net cash flows per Share from operating activities = Net cash flows from operating activities/Total number of Shares issued at period end

(4) Weighted average method used for computation:

Earnings per share computed on weighted average basis = Profit after taxation in the Reporting Period ÷[Total number of Shares issued at period end÷(1+Ratio of rights issue)+Total number of Shares issued at period end÷(1+ Ratio of rights issue)×Ratio of rights issue×the amount of months from the next month of the last day of payment to the month of period end÷12]

Return on shareholders' equity computed on weighted average basis = Profit after taxation in the Reporting Period÷[(Net assets at period beginning + Net assets at period end)÷2 + Net assets from rights issue × (the amount of months from the next month of the last day of payment to the month of period end)÷12]

4. Changes of Shareholders' Equity in the Reporting Period

Item	Share Capital	Capital Surplus	Surplus Reserve	Welfare Reserve	Retained Earnings	Total
	RMB' 000	RMB' 000	RMB' 000	RMB' 000	RMB' 000	RMB' 000
Amount at beginning of the reporting period	228,000	235,709	19,850	9,925	47,586	531,145
Increase during the reporting period			18,464	9,232	70,971	89,435
Decrease during the reporting period					34,200	34,200
Amount at the end of the reporting period	228,000	235,709	38,314	19,157	84,357	586,380
The reasons for variety			withdraw the profit after taxation	withdraw the profit after taxation	increase profit after taxation	

III. CHANGES IN SHARE CAPITAL AND SUBSTANTIAL SHAREHOLDERS

1. Changes in Share Capital

(1) During the Reporting Period, the Company didn't make any bonus Shares, converted Shares or rights issue, which would lead to change in share capital. The share capital structure of the Company as at 31st December, 1999 was set out below:

Unit: Share with par value of RMB 1 each

	Amount at beginning of the Reporting Period	Amount at end of the Reporting Period
Non-listed Shares		
Promoter's Shares including:		
--State Shares	140,000,000	140,000,000
--Shares held by domestic legal persons		
--Shares held by foreign legal persons		
--Others		
Shares offered to legal persons		
Shares offered to employees		
Preferred Shares or others		
Total non-listed Shares	140,000,000	140,000,000
Listed Shares		
A Shares listed in the PRC		
B Shares listed in the PRC	88,000,000	88,000,000
B Shares listed overseas		
Others		
Total listed Shares	88,000,000	88,000,000
Total number of Shares issued	228,000,000	228,000,000

(2) Issuing and Listing of Shares

On 1st September, 1999, Yantai Changyu Pioneer Wine Company Limited (the "Company") initially issued 88,000 B Shares with denomination of RMB1.00 per Share to overseas investors under the permission of the China Securities Regulatory Commission proved by document number (1997)52.. The issuing of Shares was fulfilled in scheduled period. The issuing price wasRMB3.48 per Share converted into HKD3.25 per Share. The Company's B Share was listed on the Shenzhen Stock Exchange on Sep.23,1997.

Since the initial issuing of 88,000,000 B Shares, the Company hasn't made any bonus shares, converted shares or rights issue which would lead to change in share capital and share composition.

2. Substantial Shareholders

The Company had 2,186 shareholders as at 31st December,1999, including one state shareholder. The State Shares held by Yantai Changyu Group Company Limited (the "Changyu Group Company") are entrusted by Yantai City's Administration Bureau of State-owned Assets. There were 2,185 shareholders with respect to B Shares listed in the PRC.

The respective shareholding of the top 10 shareholders of the Company as at 31st December, 1999 were as follows:

Name of Shareholders	Number of Shares held	Percentage of total Shares (%)
Yantai Changyu Group Company Limited	140,000,000	61.40
Xin Lian International Pty. Ltd.	4,100,000	1.80
China Everbright Assets Management Company Limited	2,500,400	1.10
Speedy Link Investment Limited	2,500,000	1.10
Wellplanned Limited	2,500,000	1.10
China Guo Tai Holdings Company Limited	2,492,600	1.09
Longbusy Investment Limited	2,446,600	1.07
China Everbright Financial Holdings Limited	2,435,000	1.07
Banque Paribas Crownble Enterprises Limited	2,033,912	0.89
Bony A/C Cmg Ch China Investments Limted	1,690,700	0.74

3. The only legal person holding more than 5% (including 5%) of the Company's Shares was Yantai Changyu Group Company Limited, the Parent Company, which held 61.40% of the Company's Shares. The legal

representative of Yantai Changyu Group Company Limited is Mr.Sun Li-qiang, its scope of business includes the management and administration to the authorized state assets, Chinese medicine, glass products, spirits producing and managing, hotel management, canteens serving the Company's employees, kindergartens, etc.. During the Reporting Period, the number of the Company's Shares held by Yantai Changyu Group Company Limited has not been changed and was not subject to any lien or frozen or under any legal disputes.

4. Among the top 10 shareholders, China Everbright Assets Management Company Limited and China Everbright Financial Holdings Limited are related parties, while the others are not.
5. In the Reporting Period, the Parent Company of the Company kept unchanged.

IV. BRIEF DESCRIPTION OF THE SHAREHOLDERS' MEETING

The Company convened the shareholders' meeting twice during the Reporting Period.

1. The Company's Shareholders' Meeting (the 1998 annual meeting) was convened at the conference room of the Company's Wine Culture Museum at 8:30 am on 28th MAY ,1999. The public notice regarding the meeting was published on 9th April, 1999 in the "China Securities Newspaper", "Securities Times " and " Hong Kong Commercial Daily". Six persons, including one domestic shareholder and five foreign shareholders and proxies, presented at the meeting, representing 144.905 million Shares or 63.56% of the total 228 million Shares issued in conformity with the stipulates in "the Law of Limited Company in the PRC" and "the Articles of Association of the Company". During the meeting, the relevant issues were discussed and the following resolutions were made by public ballot:

(1) Passed "the Work Report of the Board of Directors of 1998"
(2) Passed "the Work Report of the Board of Supervisors of 1998"
(3) Passed '"the Annual Report of 1998"
(4) Passed " the 1998 Financial Statement and the 1999 Financial Budget Report"
(5) Passed "the Profit Distribution Proposal of 1998"
(6) Passed "the Proposal of Continuing the Appointment to Certified Public Accountants"
(7) Passed "the Proposal of Leasing of the Related Property of Ynatai Changyu Group Company Limited"
(8) Passed "the Authorization to the Board of Directors for Investment Decision with Investment Amount of less than 10% of the Company's Total Net Assets".

The resolution announcement of this shareholders' meeting was published on 29th May, 1999 in the "China Securities Newspaper", "Securities Times" and "Hong Kong Commercial Daily".

2. The Company convened the first Extraordinary Shareholder's Meeting (the 1999 annual meeting) on 30th August, 1999. The public notice regarding the extraordinary meeting was published on 30th July, 1999 in the "China Securities Newspaper", "Securities Times" and "Hong Kong Commercial Daily". Two shareholders and proxies attended the meeting, represented 141.5 million Shares or 62.06% of the total Shares issued, among which there were 140 million domestic Shares represented 98.94% of the Shares holding by the shareholders and proxies in the meeting, 1.5 million foreign Share represented 1.06% of the total Shares holding by the shareholders and proxies in the meeting which were in fully conformity with the stipulates and regulations in "the Law of Limited Company in the PRC" and "the Articles of Association of the Company". During the meeting, the proposal of increasing capital to issue B Shares in domestic market was discussed and the following resolutions were made by public ballot:

1). To increase capital to issue 40 million B Shares in domestic market and the capital collected from this issuing of B Shares will mainly be used for importing the assembling line of low-alcohol wine, improving the ferment capacity by 10,000 tons, establishing subsidiary companies for distribution in 21 provincial capitals and key cities in the PRC, extending the vineyards by 20,000 mous, setting up the computer network systems of sales, transforming the Company's technology and scientific center to apply for obtaining the certificate of state level. The unused portion of the proceeds if any will be deposited in the Company's current capital

2) To fix the issuing price with 5% to10% discount on the price when issued on the second market oron final fixed price. The issuing price would not be lower than the net assets value per Share by the end of 1998.

3) To limit the issuing period to one year from the date of the resolution passed in this Extraordinary Shareholders' Meeting.

4) To authorize full power to the Board of Directors to settle subjects of issuing B Shares including the issuing time, issuing measures, issuing price, revising the articles of association of the Company, the programs of using capital collected from B Shares issued.

The resolution announcement of this Extraordinary Shareholders' Meeting was published on 31 th August, 1999 in the "China Securities Newspaper", "Securities Times" and "Hong Kong Commercial Daily".

V. BOARD OF DIRECTORS' REPORT

1. Principal Business

(1) The Company is a light industrial manufacturer of which the principal business is the distilling, producing and distributing of wine, brandy, health wine, sparkling wine and cider using grapes and apples as materials with major products including dry red wine, dry white wine, XO brandy, VSOP brandy, VO Brandy, VS brandy, Tzepao Sanpien Jiu, Special Quality Sanpien Jiu, Vermouth and sparkling wine. According to the investigation to the domestic wine market sponsored by the Commercial Information Center of the Trade Department of China in December of 1999, the composite market occupation of the Company's wine was 21.42%, and the market share of its sales volume reached 24.06%, the occupation for market scope achieved to 19.66% which all took the first place in domestic wine industry (Resource from The Commercial Information Center of The Trade Department of China).

(2) Scope of Principal Business and Operating Situation

During the Reporting Period, the Company's total sales reached RMB 583.18 million with 11% growth over that of the last year, among which the sales of wines was RMB367.40 million, taking 63% of the total sales, sales of brandy reached RMB134.13 million, taking 23% of the total sales and sales of health wine was RMB69.62 million, taking 12% of the total sales.

By the end of the Reporting Period, the Company's sales for exportation reached RMB20.13 million which took 3.5% of the total sales of the Company. The major products exported were health wine, and the main markets covered Hongkong, Japan, South-east Asia, some European and American countries.

(3) Problems, Difficulties and Measures Taken in Operation

In the year of 1999, the Chinese wine market has turned into period for steadily growth since developed at top speed for last two years. The product structure and market share of wine have been reconstructed. In order to cope with the changes of wine market for acceding to WTO in the near future, increase the strength in competition and expand the market share of products, the Company had made great effort on market developing, improved the market management and distribution system, effectively raised the distribution ability of products and expanded the percentage of market occupation, thus ensured the highest portion of its products in domestic wine market and laid a solid foundation for its future development. On the other hand, the management of marketing channels and the way to increase the efficiency of advertisement, especially how to assess the influence upon domestic wine market after acceding to WTO and the further preparation for handling with those changes, are still to be improved.

2. Financial Situation of the Company

In the year of 1999, the Company strengthened the supervision to accounts receivable, thus kept cash flows better. By the end of the Reporting Period, the net of cash flows from operating activities was RMB74.946 million, the net of cash flows per Share from operating activities was RMB0.33, the equity-debt ratio was 29.6%, the current ratio was 2.33 and the quick ratio was 1.35.

The total assets by the end of the Reporting Period was RMB832.683 million, with growth of 16.3% over that of the preceding year, which was mainly caused by the enlargement of the production and sales scale. The long-term loans of the Company of last year was RMB10 million, which was all long-term bank loans and same as that of last year. The shareholders' equity was RMB586.38 million, 10.4% growth over that of the preceding year, which was mainly caused by the increase of the net profit. The profit from principal business was RMB322.412 million, 20.3% growth over that of the preceding year, which was caused by the increase of the income of the principal business, the percentage growth for mid-high grade products and the increase for the total profit. The net profit was RMB 89,434,626, 5.9% growth over that of the preceding year, which was mainly caused by the increase of the total sales.

The expenses for operation and distribution of the Company in 1999 was 19.4% up of that in 1998, which was mainly caused by the increase of investment on resources of staff, materials and finance for construction of the sales network, distribution of the new products, expandation of the market occupation, increase of advertising costs. It is sure that, the increased advertising cost at a large scale which would influence the profits of the corresponding period, and bring about positive effects on improving the sales of the Company in 2000, especially on strengthening the ability in competition when acceding to WTO in the near future.

3. Investment of the Company

During the Reporting Period, the Company neither raised a fund nor made any foreign investment. The Company made an initial offer (the "offering") of 88 million B Shares listed in the PRC in September of 1997 with net proceeds amounted to HK$264.023 million. The Company had invested in those projects as disclosed in the Prospectus and finished the investment completely by the end of Reporting Period. The operational situations of investment projects finished and refinished to the end of the Reporting Period are set out below:

Unit: RMB' 000

Projects as disclosed in the Prospectus and actual Investment	Committed investme amount	Investment amount in 1998	Investment amount in 1999	Accumulatedtotal investment amount
-Additional 28 thousand tons mid-to high-end wine "shuang- jia" technology remodification	10,778	3,780	2,480	9,403(finished)
-Project for the development of vineyards	2,211	1,575	150	1,975(finished)

The uses of proceeds and the operational situation are stated below:

(1) Additional 28 Thousand Ton Mid-to High-end Wine "Shuangjia" Technology Remodification Project.

A total investment amount of RMB107.78 million was planned for this project, including RMB86 million for investment in fixed assets. The construction period of this project was estimated to be 2.5 years. Upon completion, the project was anticipated to increase net profit by RMB35.98 million. To date, the accumulative investment in this project amounted to RMB94.03 million, among which RMB24.80 million invested during the Reporting Period, which was used for projects below: **A**. To proceed with establishing the ferment factory for raw material wine with ferment capacity of 20,000 tons. This investment had been completed and put into operation in the grapes harvest season by the end of August, 1999, therefore the project offered the Company with sufficient raw materials for selling, manufacturing and stocking of wine in 2000. **B.** To undertake technology transform of Sparkling Wine Branch. RMB 11million had been invested in the project during the Reporting Period with budget investment of RMB 15million. The reconstruction of factory buildings, installation and adjustment of assembling line were to be nearly fulfilled by the end of Reporting Period. With the annual production capacity of 10,000 tons, the assembling line which was for filling wine and sparkling wine, would be put into operation by the end of January of 2000,

(2) Project for the Development of Vineyards

The Company had committed to invest RMB22.11 million in this project, and the accumulative investment by the end of 1999 reached RMB19.75 million while the Company invested RMB 1.5 million for the vineyards construction during the Reporting Period. The total area of vineyards had reached 50,000 mous on the basis of increase of 26,000 mous . The increased vineyards had started to provide the Company with grapes gradually since Autumn of 1999.

4. Influence of WTO upon the Future Operation of the Company

The Board of Directors considered the negative influence upon the Company's operation in the future after acceding to WTO as follows: The customs tariff would be minified and that was favorable for foreign wine company to swarm into Chinese market. Thus the domestic wine market would be impacted in a short time with more violent competition. On the other hand, the opening of the market would also further promote the exchange and cooperation of technology between the Chinese and foreign companies, and the Company would response to accelerating research and development of new products, increasing the competitive ability. Therefore, the Board of Directors confirmed that the Company should still keep on emphasizing on principal business, absorb the advanced technology and experience of management of foreign companies, enhance the Company's advantage of brand and technology, promote the sales network systems, further develop new products, and therefore the Company would be ensured to strengthen the ability in competition, raise the Company's position in domestic wine market, and finally obtain better and faster development.

5. Business Development Plan of the Company in 2000

(1) Business Development Plan in 2000

I f no irresistible situation occurs, the Chinese wine market will continue to develop steadily along with improving of the domestic financial situation and the increases of income per capita. The competition in the wine market will be enhanced, the concentration percentage of brand will also be raised. To adapt the aforesaid situations, ensure the steady increasing of sales income and total profit in 2000, the following measures will be adopted by the Company:

-To strengthen further construction of sales network, to promote the transformation of sales system leading into competition, increase the occupation percentage in wine market.

- To speed up technological innovation, advantage the composition of products, to accelerate the research of new products, strengthen the production and distribution of mid-high level products.

-To advantage the structure of grape variety, promote the construction of vineyards in order to ensure the supply of high-quality raw material, and to cater the Company's demands of distributing and adjusting of the structure of products.

-To enhance the reformation and innovation of the Company, promote the transformation of internal management, perfect the system for labor supply and wage distribution, to establish the circulating, opening and competitive system of labor supply.

-To emphasize the normative management, improve the quality of staff, keep focus on strength for engaging and training of high-quality technicians and managers, raise the level of policy determination and management.

(2) Investment Plan in 2000

During the year of 2000, the company will prepare to increase capitals to issue B Shares, make good preparation for the projects which are to be put into construction as follows:

A. To set up exclusive companies of distribution the Company's products in provincial capitals and key cities, develop and enhance the construction of the sales network.

B. To import the assembling line of wine cooler with the annual production capacity of 20,000 tons, increase the output of wine cooler of the Company.

C. To increase the ferment capacity of raw material wine by 10,000 tons, and also increase the vineyards by 20,000 mous.

D. To establish the network system for computer management, reconstruct the Company's technical and scientific center, apply for building up a technical and scientific center of State level.

The Board of Directors confirms that the investments mentioned above are profitable for the Company's development in the future and also beneficial for raising the requital to the shareholders. The Company will consider the financial situation before making preparations for the construction of relevant projects on the schedule settled according to the importance and urgency of the projects.

6. Matters on the Work of Board of Directors

The Company had convened the Board of Directors' meeting three times during the Reporting Period. The forth meeting of the first Board of Directors was held at the Company's Wine Culture Museum on 5th April, 1999, while seven directors should attend and genuinely attended at the meeting with all the senior management presented and all the supervisors attended as observers. Following resolutions were discussed and passed: **A.** "the Work Report for the Board of Directors of 1998", **B.** "the Work Report for the General Manager of 1998", **C.** "the Annual Report of 1998 and the Summary for the Report", **D.** "the Financial Statement of 1998", **E.** "the Profit Distribution Proposal of 1998", **F.** "the Financial Budget Report of 1999", **G.** "the Proposal of Leasing the Related Property of Yantai Changyu Group Company Limited", **H.** "the Proposal of Continuing to Engage Certified Public Accountants", **I.** "the Submission to the Meeting for Authorization to the Board of Directors for Investment Decision with Investment Volume of less than 10% of the Company's Total Net Assets", **J.** "the Relevant Subjects of Holding the Shareholders Meeting of 1998".

The fifth meeting of the first Board of Directors was held at the conference room of the Company's Wine Culture Museum on 29th July,1999, with all the directors presented and all the supervisors attended as observers. The meeting was chaired by Mr.Sun Li-qiang, the chairman to the Board of Directors.

The following resolutions were discussed and passed: **A** "the Proposal for Increasing Capital to issue 40 million B Shares", **B.** "the Proposal on Projects Using the Capital Collected from 40 million B Shares issued", **C.** "the proposal of Holding the First Extraordinary Meeting of Shareholders' of 1999".

The sixth meeting of the first Board of Directors was held at the Company's Wine Culture Museum on 15th August,1999. Seven directors should attend while six directors genuinely attended the meeting with all the supervisors attended as observers. Mr. Tian Fu-yong, vice-chairman to the Board of Directors, chaired the meeting entrusted by Mr. Sun Li-qiang, the chairman to the Board of Directors. "The Interim Report of 1999" was discussed and passed at the meeting, and the Company decided neither to distribute profit nor transfer capital reserve to share capital for the middle of 1999.

7. Senior Management and Staff

(1) Brief Introduction to the Directors and Supervisors of the Company

During the Reporting Period, the directors and supervisors of the Company kept unchanged. Brief introduction is as follows:

NAME	AGE	PROFESSIONAL TITLE	POST
Mr. Sun Li-qiang	53	senior economist	Chairman to the Board of Directors & General Manager
Mr. Tian Fu-yong	61	senior politician	Vice Chairman to the Board of Directors
Mr. Wang Guo-zhu	56	senior economist	Director
Mr. Fu Shi-yong	53	senior economist	Director & Vice-General Manager
Mr. Fu Ming-zhi	47	senior economist	Director & Vice-General Manager
Mr. Li Hong-chen	56	senior accountant	Director & Chief Accountant
Mr. Qu Wei-min	43	senior economist	Director &Vice-General Manager and Secretary to the Board of Directors
Mr. Wang Shi-liang,	52	politician	Chairman for Board of Supervisors
Mrs. Zhang Hong-xia	44	accountant	Supervisor
Mr. Shi Shi-chun	36	engineer	Supervisor

All the above-introduced Directors and Supervisors have three years term office from 18th September, 1997 to 18th September,2000.

(2) Senior Management

In addition to the information of **Mr. Sun Li-qiang**, the General Manager, Mr. **Fu Shi-yong**, **Fu Ming-zhi** and **Qu Wei-min**, the Vice-General Managers, and Mr. **Li Hong-chen**, the Chief Accountant, set out above, the information of other members of the senior management is set out as follows:

Mr. Sun Mao-jian, aged 40, is a senior economist. He is currently a Vice-General Manager of the Company and the manager of the Sparkling Wine and Cider Division.

Mr. Yang Ming, aged 42, is a senior engineer. He is currently a Vice-General Manager of the Company and the Manager of the Health Spirits Division.

Mr. Zhou Hong-jiang, aged 35, is an engineer. He is currently a Vice-General Manager of the Company and the Manager of the Sales Division.

Mr. Wang Gong-tang, aged 61, is a senior engineer and a consultant of the Company.

Mr. Xu Zi-heng, aged 58, is a senior engineer and a consultant of the Company.

Mr. Lin Wen-bing, aged 65, is a senior engineer and a consultant of the Company.

During the Reporting Period, none of the above members of the senior management had left his post. All the directors, supervisors and senior management didn't hold any Shares of the Company and they all got the regular reward from the Company. Two persons got the total reward of RMB60,000 to 70,000 in1999, while ten persons received RMB40,000 to 50,000, and four persons gained RMB30,000 to 40,000.

(3). Staff of the Company

As to 31st December, 1999, the number of the staff of the Company was 1945, including 821 productive workers, 382 sales persons, 532 technicians, 98 financial members, 112 administrative persons. Among the staff members, there were 229 university graduates, 142 college graduates, 249 graduates of professional schools and 1,325 graduates of lower than senior middle schools.

8. Company's Profit Distribution Plan of 1999

The net profit of 1999 was RMB89,434,626 based on the audit performed by Arthur Andersen & Co. according to the International Accounting Standards, and RMB92,321,626 based on the audit performed by Arthur Andersen · Hua Qiang Certified Public Accountants according to the PRC Accounting Standards.

In accordance with the regulations of "Enforcement Detailed Rules on the Domestic-listed B Shares of Limited Company" and "the Articles of the Association of the Company", the appropriate of dividend of the B Shares listed Company should be based on the lower of the Company's retained earnings as reported in the financial statement drawn up according to the PRC Accounting Standards", on "the Audited Financial Statement according to the PRC Accounting Standards", and that adjusted by the International Accounting Standards.

On the basis of the net profit of RMB 92,321,626 in 1999, after allocating 10% of such amount, i.e. RMB 9,232,163, to the statutory common reserve, and 10% of such amount, i.e.RMB9,232,162, to the statutory common welfare fund, and plus RMB24,084,244 of the profit undistributed at the beginning of the Reporting Period, the amount available for distribution in 1999 was RMB 97,941,545.

Upon considering the Company's requirements for fund on technology innovation and new projects in 2000, and the earnings for shareholders in corresponding year, the 1999 profit distribution plan was decided as follows: RMB 34,200,000 was proposed to be appropriated by cash dividend to shareholders of all 228 million Shares on 31st December, 1999 in the ratio of RMB1.5 for every 10 Shares. The remaining of RMB 63,741,545 will be carried forward to the next year for distribution.

The cash dividend distributed to the foreign shareholders will be paid in HK Dollars converted from RMB by the middle ratio announced by the People's Bank of China on the first working day after the resolution date of the General Shareholders' Meeting.

The Company wouldn't transfer capital reserve to share capital in 1999.

The above profit distribution plan is subject to be considered and approved by the 1999 Shareholders' Meeting.

VI. BOARD OF SUPERVISORS' REPORT

1. Meeting of the Board of Supervisors

The Company had convened the Board of Supervisors' Meeting twice during the Reporting Period. The meeting of Board of Supervisors of 1998 was convened on 5th April, 1999. In the meeting, "the 1998 Annual Report to the Board of Directors", "the Financial Statement of 1998" and "the Profit Distribution Plan of 1998" were discussed and passed. The fourth meeting of the first Board of Supervisors was convened on 12th August , 1999 with "the Interim Report of 1999"discussed and Passed.

2. Report of the Board of Supervisors

During the Reporting Period, the Board of Supervisors summed up the following points on the basis of supervising and examining:

(1) During the Reporting Period, the Company was operated strictly in accordance with the stipulates and regulates in "the Securities Law", "the Law of Limited Company in the PRC", "the Articles of Association of the Company". The Company set up complete regulations and rules for management as "the Regulations for Examination on Bad Debts", "the Regulations for the Audit of the Company" and "the Regulations for the Audit of Investment Items". All the directors and senior management made great effort to work. They did not take any action which was in violation of any law, regulations, articles of association or which would jeopardize the Company's interest while performing their duties.

(2) It was true and normative for the Company's accounting documents, accounting statements and other accounting articles. The audit department executed an effective auditing on the annual operating benefits, costs and achievement targets to every branch, and further enhanced the management level, increased the responsibility for management.

(3) Proceeds from the offering in 1997 were invested in the projects same as previously disclosed in the Prospectus. The use of the offering was audited by Arthur Andersen · Hua Qiang Certified Public Accountants and the corresponding individual audit report has been presented.

(4) The Board of Supervisors considered all the connected transactions that took place were fair and reasonable strictly in accordance with market principle, and no action capable of hurting the interests of the Company had occurred.

(5) Arthur Andersen & Co. and Arthur Andersen · Hua Qiang Certified Public Accountants individually audited the Company's Financial Statements of 1999 according to the International Accounting Standard and the PRC Accounting Standard respectively, and expressed an unqualified opinion, which stated the Company's financial position was true and fair.

Ⅶ. MATERIAL EVENTS

1. Material Litigation and Arbitration

The Company had not experienced any material litigation and arbitration during the Reporting Period. With regard to the two lawsuits filed by the Company's promoter, Yantai Changyu Group Company Limited as disclosed in " the 1998 Annual Report ", of which rights and obligations should be assumed by the Company, the progress and judgement results are as follows by end of reporting period:

(1) The case regarding the payment dispute with Shandong Foodstuff Import/Export Company, the amount involved was RMB 4,022,839.80. The case was trying completely by the Mid-level People's Court of Yantai City and didn't close by the end of reporting period.

(2) The case regarding the payment dispute with Yantai City Foreign Lianghua Real Property Company, the amount involved was RMB 133,971.60. The case was ended after the People's Court of Yantai City Zhifu District took part in the mediation. The defendant was required to repay full amount, including the delayed payment, and the verdict is now being carried out.

2. During the Reporting Period, the Company and any of the directors, senior management hadn't been punished by the state supervising administration.

3. During the Reporting Period, there wasn't any changes of the holding shareholder and the proportion of Shares they hold, and there wasn't any reelection for the directors, while none of the directors left his duty and there wasn't any dismissal or reemployment for the general manager and the secretary to the Board of Directors.

4. Material Related Party Transactions

(1) In the Reporting Period, the Company and the Parent Company, Yantai Changyu Group Co., Ltd (the "Group Company ") signed " the Lease Agreement" on the Company leasing the relative assets of the associated company—Yantai Traditional Medicine Factory on 28th April, 1999. The main terms and conditions of the agreement were as follows:

① The Group Company shall lease the workshop of 7,353 square meters, production equipment with the original book value of RMB15.68 million, ground of 22,000 square meters for health wine production, existing office building and office facilities of its associated company, Yantai Traditional Medicine Factory to the Company at the rental rate settled in the light of the rental rate for the same properties in the Yantai Lease Market by the end of 1998; the Company shall carry out production by using the properties leased, while the steam will be supplied by the Group Company, with the payment of the steam fee at the cost price according to the actual usage.

② The Group Company shall no longer produce or operate health wine products from the execution date of the "Lease Agreement".

③ The rental for leasing the workshop shall be RMB0.5 per square meter per day, there are totally 7,353 square meters, the total rental of the workshop for one year shall be RMB1.34 million on the basis of 365 days a year. The rental of the ground shall be RMB10 per year per square meter, there are totally 22,000 square meters, the total rental for one year shall be RMB220 thousand. The rental for the production equipment for one year shall be 6 percent of its original book value, that is RMB940 thousand. The rental of the existing office building for one year shall be RMB300 thousand, the rental of the trade mark " Zhong Ya " for one year shall be RMB600 thousand.

④ The total rental of all the above properties for one year shall be RMB3.4 million. The rental, together with the steam fee shall be paid by the Company to the Group Company within ten working days after the end of the accounting year, for overdue payment, interest shall be paid according to the bank interest rate for current deposit in the corresponding period.

⑤ The Company shall have the responsibility of ensuring the completeness of the properties leased, unless the completeness of the above properties is damaged due to the causes of force majeure when the Company shall not make any compensation, the Company shall make compensation according to the replacement price of the properties damaged.

⑥ The Company shall manage independently the properties leased from the Group Company, while the Group Company shall not make any interference.

⑦ The " Lease Agreement " had been reviewed and approved by the 1998 General Shareholders' Meeting convened on 28th May, 1999, when it went into effect and the term of validity should be 5 years from the date when it went into effect.

The purpose for which the Company lease the property is to avoid the competitions in the same trade between the Group Company and the Company, to seek unity in the health wine production and sales in both domestic and foreign market, and to build good foundation for the steady profit growth increment from the health wine products. On the other hand, the Company may make full use of the production workshop, advanced equipment, corresponding ground and supporting facilities owned by the Group Company, and enlarge the health wine annual production capacity from 3000 tons to 6000 tons to meet the market needs of the products.

This agreement had been approved by the 4th meeting of the first Board of Directors and passed after being reviewed by the 1998 General Shareholders' Meeting. The public notice about the related matters on the lease was published on 30th April, 1999 in the "China Securities Newspapers", "Securities Times" and "Hong Kong Commercial Daily"

(2) Others

Other connected transactions were detailed in the 18th clause in the notes to the consolidated financial statements.

5. Three Separations of Person, Property and Finance of Listed Company and Holding Shareholder

(1) Separation of Senior Management

At present, the chairman to the Board of Directors simultaneously holds the post of legal representative of the holding shareholder, and the General Manager of the Company simultaneously holds the post of the General Manager of the holding shareholder's company. Since The China Securities Regulatory Commission put forward the policy of "Three Separations" for listed Company and holding Shareholder's company, the Company engaged actively in settling the problems of multiple and pluralistic post for senior management, the chairman to the Board of Directors and the General Manager of the Company, together with relevant departments of Yantai City. And now the Company has gone into concrete action for the settling. Before the accomplishment of post settlement, the Company will strictly define the duty for senior management, firmly stop the irregular material related party transactions with the Group Company, ensure the independent operation system and guarantee the legal rights and interests of investors.

The holding of post of other directors, supervisors and senior management in the Company is in entirely accordance with the laws, regulations and the Company's constitutions.

(2) The Separation for Property

The Company separate with the holding Shareholder-the Group Company on subject of industrial rights and non-proprietary technology. At the beginning of establishment, the legal alteration formalities of the property the Group Company invested to the Company had been finished in 1998. As one independent corporation with full property right, the Company undertakes its operation individually, and engages independently in purchasing raw materials, producing and distributing products without any activities of entrusting the Group Company to purchase or distribute. There isn't any unnecessary competition in same trade between the Company and the Group Company. All related transactions with the Group Company were signed up with corresponding agreements and passed by the Shareholders' meeting. The Company haven't used its property to stand any guarantee for any debts of shareholders', personals, other body corporate or nature person.

(3) The Separation of Finance

The Company set up separately financial department with independent and standard financial calculating system. There isn't any problem of interference in financial staff and calculating system with the Group Company. The subsidiary companies of the Company also established individual calculating system and bank accounts as individual tax bearer. The Company draw up the financial statements to report the financial situations and changes of the Parent Company and its subsidiaries according to stipulates of the State Financial Ministry.

6. Lease of Other Property

To avoid unnecessary competition in same trade, the Company signed leasing agreements with its Parent Company- the Group Company on 10th march, 1998 and 28th April , 1999, concerning rental of relevant property from Yantai Fushan Winery, Yantai Second Distillery of and Yantai Traditional Chinese Medicine Factory. The agreements were still effective during the Reporting Period. The announcement for property leasing was published in "Chinese Securities Newspaper", " Securities Times" and "Hong Kong Commercial Daily" on 9th Aril,1998 and 30th April,1999.

7. Engagement Certified Public Accountants

The Company convened 1998 Shareholders' Meeting on 28th May, 1999, and determined to engage continually in 1999 Arthur Andersen & Co., as the Company's international auditor, and Arthur Andersen • Hua Qiang as the certified public auditor. The period of appointment is 1 year.

8. During the Reporting Period, there wasn't any events of securities or mortgages of contracts, occurred in the Company.

9. During the Reporting Period, the name of the Company and the abbreviation of the B Shares were both unchanged.

10. Other Material Events

According to the documents of "The Notice for Printing and Releasing of Supplementary Stipulates to Settle the Accounts Problem for Limited Company" with number of Caikuaizi no.35 (1999), the limited company should withdraw four provisions, which had been already carried out by the Company in accordance with the stipulates, thus the financial situation and operation will not be influenced.

VIII. FINANCIAL REPORT

AUDITORS' REPORT

TO THE SHAREHOLDERS OF YANTAI CHANGYU PIONEER WINE COMPANY LIMITED:

Arthur Andersen & Co. (hereinafter referred to as "We") have audited the accompanying consolidated balance sheets of Yantai Changyu Pioneer Wine Company Limited and its subsidiaries (hereinafter referred to as the "Group") as of December 31, 1999 and 1998 and the related consolidated statements of income, changes in equity and cash flows for the years ended December 31, 1999 and 1998. These financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with International Standards on Auditing issued by the International Federation of Accountants. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as of December 31, 1999 and 1998 and the results of its operations and its cash flows for the years ended December 31, 1999 and 1998 in accordance with International Accounting Standards issued by the International Accounting Standards Committee.

ARTHUR ANDERSEN & CO.

Hong Kong
March 7, 2000

YANTAI CHANGYU PIONEER WINE COMPANY LIMITED AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME FOR THE YEARS ENDED DECEMBER 31, 1999 AND 1998

(Expressed in thousands of Renminbi Yuan except earnings per share data)

	Note	1999	1998 (Note 19)
Revenue		583,175	530,208
Cost of sales		(260,763)	(262,190)
Gross profit		322,412	268,018
Other operating income		3,613	9,378
Selling and administrative expenses	4	(217,153)	(181,796)
Other operating expenses		(1,572)	(2,965)
Profit from operations		107,300	92,635
Finance income, net	5	2,832	3,032
Profit before taxation		110,132	95,667
Income tax	6	(20,697)	(11,236)
Net profit for the year		89,435	84,431
Retained earnings, beginning of year		47,586	6,226
Dividends	7	(34,200)	(29,640)
Appropriation to statutory reserves	14	(18,464)	(13,431)
Retained earnings, end of year		84,357	47,586
Earnings per share	8	RMB0.39	RMB0.37

The accompanying notes form an integral part of these financial statements.

YANTAI CHANGYU PIONEER WINE COMPANY LIMITED
AND ITS SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
AS OF DECEMBER 31, 1999 AND 1998

(Expressed in thousands of Renminbi Yuan)

	Note	1999	1998 (Note 19)
ASSETS			
Non-current assets			
Fixed assets, net	9	248,093	195,318
Construction-in-process		17,002	15,514
Investment in associates		703	703
Deferred tax assets	10	11,765	5,439
		277,563	216,974
Current assets			
Inventories	11	232,692	168,503
Accounts receivable, net	12	76,053	129,011
Prepayments and other receivables		75,892	49,227
Due from Changyu Group Company	17	57,578	19,432
Cash and cash equivalents		112,905	132,815
		555,120	498,988
Total assets		832,683	715,962
EQUITY AND LIABILITIES			
Capital and reserves			
Share capital	13	228,000	228,000
Capital reserve		235,709	235,709
Revenue reserves	14	38,314	19,850
Retained earnings		84,357	47,586
		586,380	531,145
Non-current liabilities			
Long-term bank loans	15	10,000	10,000
Deferred tax liabilities	10	19,340	9,627
		29,340	19,627
Current liabilities			
Accounts payable		46,387	53,871
Dividends payable	7	13,200	11,440
Short-term bank loans	15	20,000	12,200
Salaries payable		39,580	27,201
Taxes payable		44,923	28,149
Other payables and accrued liabilities		52,873	32,329
		216,963	165,190
Total equity and liabilities		832,683	715,962

The accompanying notes form an integral part of these financial statements.

YANTAI CHANGYU PIONEER WINE COMPANY LIMITED AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY FOR THE YEARS ENDED DECEMBER 31, 1999 AND 1998

(Expressed in thousands of Renminbi Yuan)

		Reserves				
	Share capital	Capital reserve	Statutory Surplus reserve fund	Statutory public welfare fund	Retained earnings	Total
Balances at January 1, 1998	228,000	235,709	3,210	3,209	6,226	476,354
Net profit for the year	-	-	-	-	84,431	84,431
Dividends	-	-	-	-	(29,640)	(29,640)
Appropriation from retained earnings	-	-	6,715	6,716	(13,431)	-
Balances at January 1, 1999	228,000	235,709	9,925	9,925	47,586	531,145
Net profit for the year	-	-	-	-	89,435	89,435
Dividends	-	-	-	-	(34,200)	(34,200)
Appropriation from retained earnings	-	-	9,232	9,232	(18,464)	-
Balances at December 31, 1999	228,000	235,709	19,157	19,157	84,357	586,380

The accompanying notes form an integral part of these financial statements.

YANTAI CHANGYU PIONEER WINE COMPANY LIMITED AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 1999 AND 1998

(Expressed in thousands of Renminbi Yuan)

	1999	1998 (Note 19)
CASH FLOWS FROM OPERATING ACTIVITIES		
Profit before taxation	110,132	95,667
Adjustments for:		
Loss on disposal of fixed assets	3,490	1,042
Depreciation	19,267	13,653
Interest expense	1,172	2,205
Interest income	(4,004)	(5,237)
Operating profit before changes in working capital	130,057	107,330
Increase in inventories	(64,189)	(2,100)
Decrease (Increase) in accounts receivable, net	52,958	(37,753)
Increase in prepayments and other receivables	(26,665)	(18,467)
Increase in due from Changyu Group Company	(40,946)	(26,181)
Decrease in accounts payable	(7,484)	(2,378)
Increase in salaries payable	12,379	16,480
Increase in other payables and accrued liabilities	20,544	13,575
	76,654	50,506
Interest paid	(1,172)	(2,205)
Taxes paid	(536)	(14,554)
Net cash flows from operating activities	74,946	33,747
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of fixed assets	(75,532)	(291)
Proceeds from sale of equipment	-	1,939
Increase in construction-in-progress	(1,488)	(30,671)
Interest received	4,004	5,237
Net cash used in investing activities	(73,016)	(23,786)
CASH FLOWS FROM FINANCING ACTIVITIES		
Increase (Decrease) in short-term bank loans	7,800	(60,340)
Decrease in long-term bank loans	-	(29,079)
Dividends paid	(29,640)	-
Net cash flows used in financing activities	(21,840)	(89,419)
Decrease in cash and cash equivalents balances	(19,910)	(79,458)
Cash and cash equivalents balances, beginning of year	132,815	212,273
Cash and cash equivalents balances, end of year	112,905	132,815

The accompanying notes form an integral part of these financial statements.

YANTAI CHANGYU PIONEER WINE COMPANY LIMITED AND ITS SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

AS OF DECEMBER 31, 1999 AND 1998

(Amounts expressed in Renminbi unless otherwise stated)

1. ORGANIZATION AND OPERATIONS

Yantai Changyu Pioneer Wine Company Limited (the "Company") was incorporated as a joint stock limited company in accordance with the Company Law of the People's Republic of China (the "PRC") on September 18, 1997. As part of the establishment plan, the Company issued 88,000,000 domestically listed foreign investment shares ("B Shares") to overseas investors. The establishment plan involved a reorganization carried out by Yantai Changyu Group Company Limited ("Changyu Group Company"), the promoter and the parent company of the Company, which injected certain assets and liabilities in relation to the brandy, wine, sparkling wine and cider and tonic wine production and sales businesses to the Company (the "reorganization"). The Company's B Shares were listed on the Shenzhen Stock Exchange on September 23, 1997.

The Company and its subsidiaries (the "Group") are principally engaged in the production and sales of brandy, wine, sparkling wine and cider and tonic wine.

The directors considered Changyu Group Company is the ultimate parent company of the Company.

2. BASIS OF PRESENTATION

The consolidated financial statements included the financial statements of the Company and its subsidiaries. All significant intra-group transactions and balances have been eliminated on consolidation.

A subsidiary is a company in which the Company has the power to govern its financial and operating policies so as to obtain benefits from its activities.

As of December 31, 1999 and 1998, the Company had the following subsidiaries which were all incorporated in the PRC:

Name of company	**Date of establishment**	**Attributable equity interest**	**Paid-in capital**	**Principal activities**
Yantai Changyu Pioneer Food Co., Ltd.	December 1, 1992	100%	RMB30,000	Sale of fruits
Yantai Changyu Pioneer Wine Machine Packaging Co., Ltd.	December 1, 1992	100%	RMB300,000	Machinery sub-contracting and repairing
Yantai Changyu Pioneer Vehicular Transport Co., Ltd.	December 1, 1992	100%	RMB300,000	Transportation service
Dalian Changyu Sales and Distribution Co., Ltd.	January 23, 1998	100%	RMB500,000	Sales of wine
Xi'an Changyu Sales and Distribution Co., Ltd.	March 27, 1998	100%	RMB500,000	Sales of wine

2. BASIS OF PRESENTATION (Cont'd)

Name of company	Date of establishment	Attributable equity interest	Paid-in capital	Principal activities
Hangzhou Changyu Sales and Distribution Co., Ltd.	April 7, 1998	100%	RMB500,000	Sales of wine
Changchun Changyu Sales and Distribution Co., Ltd.	January 20, 1998	100%	RMB500,000	Sales of wine
Zhengzhou Changyu Sales and Distribution Co., Ltd.	January 16, 1998	100%	RMB500,000	Sales of wine
Nanjing Changyu Sales and Distribution Co., Ltd.	February 10, 1998	100%	RMB500,000	Sales of wine
Changsha Changyu Sales and Distribution Co., Ltd.	January 22, 1998	100%	RMB500,000	Sales of wine
Wuhan Changyu Sales and Distribution Co., Ltd.	January 12, 1998	100%	RMB500,000	Sales of wine
Nanchang Changyu Sales and Distribution Co., Ltd.	March 24, 1998	100%	RMB500,000	Sales of wine
Taiyuan Changyu Sales and Distribution Co., Ltd.	January 20, 1998	100%	RMB500,000	Sales of wine
Shijiazhuang Changyu Sales and Distribution Co., Ltd.	April 2, 1998	100%	RMB500,000	Sales of wine
Beijing Changyu Sales and distribution Co., Ltd.	July 14, 1998	100%	RMB500,000	Sales of wine
Guangzhou Changyu Sales and Distribution Co., Ltd.	May 15, 1998	100%	RMB500,000	Sales of wine
Zhanjiang Changyu Sales and Distribution Co., Ltd.	October 20, 1998	100%	RMB500,000	Sales of wine

An associated company is a company, not being a subsidiary or a joint venture, in which the Company holds, directly or indirectly, not less than 20% nor more than 50% of the equity interest as a long-term investment and is able to exercise significant influence on this company. Investment in associated company is stated at cost less provision for permanent diminution in value, where considered necessary by the directors. The results of operations and net assets of the associated company is not accounted for on the equity basis because it is not material to the results of operations and financial position of the Group taken as a whole. The results of the associated company are accounted for to the extent of dividends received and receivable.

As of December 31, 1999 and 1998, the Company had the following associated company which was incorporated in PRC:

Name of company	Date of establishment	Attributable equity interest	Registered capital	Principal activities
Yantai Sino-French Pegase Brandy Co., Ltd.	February 25, 1992	40%	FFR1,604,060	Manufacture an sale of brandy

3. PRINCIPAL ACCOUNTING POLICIES

The consolidated financial statements for the years ended December 31, 1999 and 1998 were prepared in Renminbi and in conformity with statements of International Accounting Standards ("IAS"), as if those standards had been applied consistently throughout the year. This basis of accounting differs from that used in the statutory accounts of the Group companies which were prepared in accordance with the accounting principles and the relevant financial regulations applicable to enterprises in the PRC ("PRC GAAP").

3. PRINCIPAL ACCOUNTING POLICIES (Cont'd)

The principal accounting policies adopted in restating the statutory accounts of the Group to comply with IAS are as follows:

(a) Revenue recognition

(i) Sale of goods

Revenue is recognized when the significant risks and rewards of ownership of goods have been transferred to the buyer and no significant uncertainties remain regarding the derivation of consideration, associated costs or the possible return of goods.

(ii) Interest income

Interest income from bank deposits is recognized on a time proporation basis that take into account the effective yield on the assets.

(b) Fixed assets and depreciation

Fixed assets are stated at cost less accumulated depreciation. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

Expenditure incurred after the fixed assets have been put into operation, is recognized as an expense in the period in which it is incurred. In situations where it is probable that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of the asset, the expenditure is capitalized as an additional cost of the fixed asset.

Depreciation is calculated using the straight-line method to write off the cost, after taking into account the estimated residual value, of each asset over its expected useful life. The expected useful lives are as follows:

Buildings	40 years
Machinery and equipment	10-20 years
Motor vehicles	6-12 years

When assets are sold or retired, their cost and accumulated depreciation are eliminated from the accounts and any gain or loss resulting from their disposals is included in the operating results.

(c) Construction-in-progress

Construction-in-progress represents plant and properties under construction and is stated at cost. This includes cost of construction, plant and equipment and other direct costs plus borrowing costs which include interest charges arising from borrowings used to finance these projects during the construction period.

No provision for depreciation is made on construction-in-progress until such time as the relevant assets are completed and ready for operational use.

3. PRINCIPAL ACCOUNTING POLICIES (Cont'd)

(d) Inventories

Inventories are stated at the lower of cost and net realizable value. Cost, calculated on the weighted average basis, comprises materials and, where applicable, direct labour and an appropriate proportion of all production overhead expenditure. Net realizable value is determined on the basis of estimated selling prices less the estimated costs of completion and related selling and distribution expenses.

(e) Operating lease

Leases where substantially all the rewards and risks of ownership of assets remain with the leasing company are accounted for as operating leases. Rental payments under operating leases are charged to the income statement on a straight-line basis over the period of the relevant leases.

(f) Taxation

The Group provides for taxation on the basis of its income for financial reporting purposes, adjusted for income and expense items which are not assessable or deductible for income tax purposes.

Deferred taxation is provided under the balance sheet liability method in respect of significant temporary differences arising from differences between the tax base of an asset or liability and its carrying amount in the balance sheet. The tax base of an asset or liability is the amount attributed to that asset or liability for tax purpose. Deferred tax assets are recognized to the extent that it is probable that taxable profits will be available against which the deferred tax assets can be utilized.

(g) Foreign currency translation

The Group maintains its books and records in Renminbi Yuan. Transactions in other currencies are translated into Renminbi Yuan at exchange rates prevailing at the time of transactions. Monetary assets and liabilities denominated in other currencies at the balance sheet date are re-translated at exchange rates prevailing at that date. Non-monetary assets and liabilities in other currencies are translated at historical rates. Exchange differences, other than those capitalized a component of borrowing costs and those arising from changes in exchange rates before the commencement of business operations, are included in the determination of net income.

(h) Cash and cash equivalents

Cash represents cash in hand and deposits with any banks or other financial institutions which are repayable on demand.

Cash equivalents represent short-term, highly liquid investments which are readily convertible into known amounts of cash and which are within three months of maturity when acquired, less advances from banks repayable within three months from dates of the advances.

(i) Related parties

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party, or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence.

4. SELLING AND ADMINISTRATIVE EXPENSES

	1999	1998
	RMB' 000	RMB' 000
Selling and administrative expenses comprised of:		
Advertising expenses	89,041	63,020
Wages and salaries	36,683	38,650
Cash discount	813	14,657
Transportation expenses	28,677	22,634
Trademarks licence (Note 17(b))	12,598	11,370
Travelling expenses	13,823	9,351
Research and development	4,471	4,024
Leasing fees of assets and trademark (Note 17(e))	3,400	-
Repairs and maintenance	1,250	1,331
Other taxes	1,594	1,064
Write back of provision for doubtful debts	(614)	(9,415)
Others	25,417	25,110
	217,153	181,796

5. FINANCE INCOME, net

Finance income comprised of:

	1999	1998
	RMB' 000	RMB' 000
Interest income	4,004	5,237
Interest expense	(1,172)	(2,205)
	2,832	3,032

6. INCOME TAX

	1999	1998
	RMB' 000	RMB' 000
Current income tax	38,083	23,447
Financial refund	(20,772)	(12,789)
Deferred tax expense resulting from increase in tax rate	5,022	-
Deferred tax expense relating to the origination and reversal of temporary differences	(1,635)	578
	20,697	11,236

6. INCOME TAX (Cont'd)

The Group is subject to enterprise income tax which is levied at the rate of 33% of taxable income based on the statutory accounts.

Pursuant to relevant documents issued by the Shandong Provincial People's Government, the Group is entitled to a financial refund of 18% on its taxable income, commencing from the date of the listing of the Group's B Shares. Pursuant to relevant document issued by the State Council in January 2000, commencing from January 1, 2000, the financial refund of taxable income policies implemented by the local governments in the PRC should be terminated. Therefore, the director of the Group expected that the Group will not enjoy any financial refund starting from 2000.

7. DIVIDENDS

Pursuant to the Board Resolution dated April 14, 2000, the Directors proposed to declare cash dividends of RMB1.5 (1998: RMB1.3) for every 10 shares in respect of the year ended December 31, 1999 to shareholders of the issued 228,000,000 shares. The total amount of proposed cash dividends amounted to RMB34,200,000 (1998: RMB29,640,000) and was recorded in the 1999 consolidated financial statements.

8. EARNINGS PER SHARE

The calculating earnings per share of 1999 was based on the consolidated net profit divided by the total number of ordinary shares of 228,000,000 shares (1998:228,000,000 shares)

9. FIXED ASSETS, net

Movements in fixed assets were:

	1999				1998
	Buildings	Machinery and equipment	Motor vehicles	Total	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Cost					
Balances, beginning of year	98,535	202,445	14,544	315,524	251,336
Additions	5,101	66,386	4,045	75,532	68,518
Disposals	(121)	(7,073)	-	(7,194)	(4,330)
Balances, end of year	103,515	261,758	18,589	383,862	315,524
Accumulated depreciation					
Balances, beginning of year	31,675	81,971	6,560	120,206	107,902
Charges	2,103	16,110	1,054	19,267	13,653
Disposals	(10)	(3,694)	-	(3,704)	(1,349)
Balances, end of year	33,768	94,387	7,614	135,769	120,206
Net book value					
Balances, end of year	69,747	167,371	10,975	248,093	195,318
Balances, beginning of year	66,860	120,474	7,984	195,318	143,434

As of December 31, 1999, machinery and equipment of the Company with net book value of approximately RMB15,500,000 were pledged as collateral for the long-term bank loans.

10. DEFERRED TAX ASSETS / LIABILITIES

Components of deferred tax assets / liabilities were as follows:

	1999	1998
	RMB' 000	RMB' 000
Deferred tax assets:		
- Tax benefit on provision for doubtful receivables	11,765	5,439
Deferred tax liabilities		
- Revaluation surplus of fixed assets	12,457	6,498
- Administrative expenses using accrual basis	6,883	3,129
	19,340	9,627

11. INVENTORIES

	1999	1998
	RMB' 000	RMB' 000
Raw materials	29,430	15,205
Work-in-progress	74,103	82,127
Finished goods	129,159	71,171
	232,692	168,503

12. ACCOUNTS RECEIVABLE, net

	1999	1998
	RMB' 000	RMB' 000
Accounts receivable	111,703	165,275
Less: Provision for doubtful receivables	(35,650)	(36,264)
	76,053	129,011

13. SHARE CAPITAL

As of December 31, 1999 and 1998, share capital of the Company comprised:

	RMB' 000
140,000,000 State shares of RMB1 each	140,000
88,000,000 B Shares of RMB1 each	88,000
	228,000

Pursuant to a board resolution dated July 29, 1999 and a resolution passed in the first temporary shareholders' meeting of 1999 on August 30, 1999, the Company planned to issue 40,000,000 B shares. The issuance of B shares was approved by the China Securities Regulatory Commission on December 30, 1999 upon the issuance of approval document Zheng Jian Fa Xing Zi (1999) No. 160. As of December 31, 1999, the Company has not issued the B shares to investors.

14. STATUTORY RESERVES

(a) According to the Company Laws of the PRC and Articles of Association of the Company, the Company is required to provide certain statutory reserves, which are appropriated from the net profit as reported in the statutory accounts. Accordingly, the Company shall set aside 10% of its net profit for statutory surplus reserve fund (except where the fund has reached 50% of the Company's registered capital) and 5% for the statutory public welfare fund. The Company may make appropriations from its net profit to the discertionary revenue reserve fund upon approval by shareholders. These reserves cannot be used for purposes other than those of which they are created and are not distributed as cash dividends without the prior approval by shareholders under certain conditions. The statutory public welfare fund is designated for collective welfare of the employees.

When the statutory surplus reserve fund is not sufficient to cover the prior years' losses, the current year's net profit shall first be used to compensate the previous losses before the appropriations to the statutory surplus reserve fund and statutory public welfare fund.

The statutory surplus reserve fund, discretionary surplus reserve fund and capital reserve as approved by shareholders may be converted into share capital provided that the balance of the statutory reserve does not fall below 25% of the registered share capital.

For the year ended December 31, 1999, the directors of the Company proposed that 10% (1998: 10%) of the profit as reported in the statutory accounts be appropriated to statutory surplus reserve fund and statutory public welfare fund respectively, totalling approximately RMB18,464,000 (1998: RMB13,431,000). The resolution is subject to approval by shareholders in the annual general meeting.

(b) According to the Articles of Association of the Company, the maximum retained earnings available for distribution is the lower of the amount determined under the PRC accounting standards and the amount determined under IAS. As of December 31, 1999, the retained earnings available for distribution was approximately RMB63,742,000 (1998 : RMB24,084,000), after taking into account the current year's proposed final dividend.

15. BANK LOANS

(a) Short-term bank loans

As of December 31, 1999, all short-term bank borrowings were guaranteed by a third party, Yantai Wanhua Hechengge Group Company Limited. The short-term bank loans bore interest at 6.70% per annum (1998: from 8.27% to 10.67% per annum).

(b) Long-term bank loans

All long-term bank borrowings were secured by certain machinery and equipment of the Company and bore interest at 7.33% per annum (1998: 9.5%). The long-term bank borrowings will be due for repayment in 2002.

16. RETIREMENT PLANS

The Group' s staff are enrolled under a pension scheme. Under the scheme, payments are made to retired staff based on the basic salary at retirement. The Group is only required to make specific contributions of 20% of the salaries to the state sponsored pension scheme and the PRC government is responsible for the ultimate pension liabilities to the retired staff.

17. RELATED PARTY TRANSACTIONS

For the years ended December 31, 1999 and 1998, the Company had the following significant related party transactions:

(a) Services agreement

Pursuant to a services agreement dated May 18, 1997, starting from September 18, 1997 (date of the Company' s incorporation), Changyu Group Company has provided facilities and services such as kindergarten and canteen to the Company. An annual service fee of RMB500,000 is payable by the Company to Changyu Group Company from the date of incorporation, until the end of the fourth accounting year (i.e. 2000). As from the fifth accounting year, the service fee may be adjusted every three years by not more than 10% of the previous annual service fee. The agreement is effective until December 31, 2007. In 1998, the Company paid service fee of RMB500,000 (1998: RMB500,000) to Changyu Group Company.

(b) Trademarks licence

Pursuant to a trademarks licence dated May 18, 1997, starting from September 18, 1997, the Company may use certain trademarks of Changyu Group Company which have been registered by the PRC Trademarks Office. An annual fee at 2% of the Company' s annual sales is payable to Changyu Group Company. The licence is effective until the expiry of the registration of the trademarks. For the year ended December 31, 1999, the Company paid trademarks fee of approximately RMB12,598,000 (1998: RMB11,370,000) to Changyu Group Company. Changyu Group Company has used all the trademarks fee for advertising expenses.

17. RELATED PARTY TRANSACTIONS (Cont' d)

(c) Patents implementation licence

Pursuant to patents implementation licence dated May 18, 1997, starting from September 18, 1997, the Company may use the patents of Changyu Group Company. The annual patents usage fee payable by the Company to Changyu Group Company is RMB50,000. The contract is effective until December 20, 2005. For the year ended December 31, 1998, the annual patents usage fee payable to Changyu Group Company amounted to RMB50,000 (1998: RMB50,000).

(d) Agreement for the lease of land use rights

Pursuant to an agreement dated May 18, 1997, the Company agreed to lease from Changyu Group Company certain pieces of land for the period from September 18, 1997 to April 21, 2047. The annual rental payable by the Company to Changyu Group Company is approximately RMB550,000. For the year ended December 31, 1999, the annual rental of land use rights payable to Changyu Group Company amounted to approximately RMB550,000 (1998: RMB550,000).

(e) Lease agreement

Pursuant to a lease agreement dated April 28, 1999, starting from May 28, 1999, Changyu Group Company agreed to lease the fixed assets, facilities and trademark of "Zhongya" of Yantai Chinese Traditional Medicine Factory, a wholly owned subsidiary of Changyu Group Company, to the Company. An annual leasing fee payable by the Company to Changyu Group Company is RMB3,400,000. The agreement is effective until May 28, 2004. For the year ended December 31, 1999, the Company paid leasing fee of RMB3,400,000 (1998: nil) to Changyu Group Company.

(f) Amount due from Changyu Group Company

The amount due from Changyu Group Company was unsecured, non-interest bearing and had no fixed repayment date.

18. IMPACTS OF IAS ADJUSTMENTS ON NET PROFIT/NET ASSETS

	Net profit		Net assets	
	1999	1998	1999	1998
	RMB' 000	RMB' 000	RMB' 000	RMB' 000
As reported in the statutory accounts	92,322	79,489	573,098	514,976
Impact of adjustments, net				
- adjustment on administrative expenses using accrual basis	-	-	20,857	20,857
- write-off of deemed input value added tax	500	5,520	-	(500)
- deferred tax (Note 6)	(3,387)	(578)	(7,575)	(4,188)
As restated in accordance with IAS	89,435	84,431	586,380	531,145

19. PRIOR YEAR' S COMPARATIVE FIGURES

Certain 1998 comparative figures have been reclassified to conform to the current year' s presentation.

1006/SME

IX. OTHER RELATED INFORMATION OF THE COMPANY

1. **The Company completed the first registration in Shandong Province Administration for Industry and Commerce on 18th September, 1997.**
2. **legal person business license number: 26718011-9**
3. **Taxation registration number: 37060216500338-1**
4. **Depository of non-marketable Shares: Shenzhen Securities Register Co., Ltd.**
5. **International Certified Public Accountants of the Company: Arthur Andersen & Co., 25/F, Wing On Center, 111 Connaught Road Central, Hong Kong PRC Certified Public Accountants of the Company: Arthur Andersen · Hua Qiang Certified Public Accountants, 1118 China World Tower, 1 Jianguomenwai Avenue, Beijing, PRC**

X . DOCUMENTS AVAILABLE FOR INSPECTION

1. **Original copy of the Annual Report signed by the Chairman of the Board;**
2. **Financial Statements signed by and under the seal of the legal representative, Chief Accountant and accounting supervisors;**
3. **Original copy of the Auditors' Report under the seal of the accounting firm, and signed by and**

under the seal of the Certified Accountants;

4. **The "Prospectus" and "Public Listing Notice" related to the issue of domestically listed foreign Shares (B Shares) by the Company;**
5. **All the originals of the Company's documents and public notice disclosed in the newspapers designated by the Securities Supervision Committee of China in the Reporting Period .**

The above documents will be available for inspection upon requested by shareholders in accordance with the regulations or the Articles of Association.

Yantai Changyu Pioneer Wine Company Limited
Board of Directors
Dated 18th April, 2000