

IMPORTANT

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 stockbroker or other registered dealer in securities, bank manager, solicitor, professional accountant or other professional adviser.

If you have sold all your shares in **Yue Yuen Industrial (Holdings) Limited**, you should at once hand this circular together with the accompanying form of proxy to the purchaser or to the bank or stockbroker or other agent through whom the sale was effected for transmission to the purchaser.

The Stock Exchange of Hong Kong Limited takes no responsibility for the contents of this circular, makes no representation as to its accuracy or completeness and expressly disclaims any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this circular.

This circular contains information for use solely by shareholders of Yue Yuen Industrial (Holdings) Limited in connection with the Special General Meeting of the Company, notice of which is also contained herein. It is not an offer to sell, nor a solicitation of an offer to purchase, nor is it calculated to invite any offers for any securities in Yue Yuen Industrial (Holdings) Limited.



YUE YUEN INDUSTRIAL (HOLDINGS) LIMITED (裕元工業(集團)有限公司)

(incorporated in Bermuda with limited liability)

DISCLOSEABLE AND CONNECTED TRANSACTION

Financial Adviser to Yue Yuen Industrial (Holdings) Limited



Credit Suisse First Boston (Hong Kong) Securities Limited

Independent Financial Adviser to the Independent Board Committee



The Hongkong and Shanghai Banking Corporation Limited

A letter from the Independent Board Committee is set out on page 35 of this circular.

A letter from The Hongkong and Shanghai Banking Corporation Limited, being the independent financial adviser to the Independent Board Committee, containing its recommendations to the Independent Board Committee is set out on pages 36 to 45 of this circular.

A notice convening a Special General Meeting of Yue Yuen Industrial (Holdings) Limited to be held at 10:30 a.m., Tuesday on 29 October 2002 at Sung Room I, 4th Floor, Sheraton Hong Kong Hotel and Towers, 20 Nathan Road, Kowloon, Hong Kong is set out on pages 59 to 60 of this circular. A form of proxy for use at the Special General Meeting is also enclosed. Whether or not you are able to attend the meeting, you are requested to complete and return the enclosed form of proxy in accordance with the instructions printed thereon as soon as possible and in any event not less than 48 hours before the time appointed for holding the special general meeting or at any adjourned meeting. Completion and return of the form of proxy will not preclude you from attending and voting in person at the special general meeting or at any adjourned meeting should you so wish.

8 October 2002

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DEFINITIONS

In this document, the following expressions have the meanings set out below unless the context requires otherwise:

- “Acquisition” means the acquisition by the Company or its subsidiary of the Sale Shares and the Shareholders’ Loans from the Vendors pursuant to the Acquisition Agreement
- “Acquisition Agreement” means a conditional sale and purchase agreement entered into between the Company, PCC and the Vendors on 16 September 2002 pursuant to which the Company agreed to purchase or procure the purchase and the Vendors agreed to sell the Sale Shares and the Shareholders’ Loans at the Consideration and subject to the other terms and conditions contained therein including the giving of an indemnity to PCC if certain guarantees are not released at Completion. PCC has agreed, among other things, to guarantee the obligations of the Vendors therein
- “Announcement” means the announcement of the Company dated 17 September 2002 in relation to the Acquisition Agreement
- “Articles” means the Articles of Association of the Company
- “Associates” has the meaning ascribed to it under the Hong Kong Listing Rules
- “Barits” means Barits Development Corporation, a company incorporated in Taiwan and which is beneficially owned by PCC as to 97.63%
- “Board” means the board of Directors
- “Business Day(s)” means a day (other than a Saturday) on which banks are open for business in Hong Kong
- “BVI” means the British Virgin Islands
- “Chairman” means the Chairman of the Board
- “Company” or “Yue Yuen” means Yue Yuen Industrial (Holdings) Limited, a company incorporated in Bermuda with limited liability and the securities of which are listed on the main board of the Hong Kong Stock Exchange
- “Completion” means completion of the sale and purchase of the Sale Shares and the Shareholders’ Loans in accordance with the terms of the Acquisition Agreement

DEFINITIONS

“Completion Date”	means the date falling 5 business days after the date on which the conditions precedent set out in the Acquisition Agreement are fulfilled or waived (as the case may be) or such other date as the parties may agree
“Consideration”	means an aggregate amount of US\$427 million (approximately HK\$3,330.6 million), subject to adjustments, being the consideration payable by the Company to the Vendors for the acquisition of the Sale Shares and the Shareholders’ Loans pursuant to the Acquisition Agreement
“Consideration Shares”	means 60 million Shares credited as fully paid up at HK\$24.29 per Share and which are to be allotted and issued as part of the Consideration under the Acquisition Agreement
“Director(s)”	means the director(s) of the Company, including the independent non-executive directors
“Enlarged Capital”	means the Existing Capital as enlarged by the issue of the Consideration Shares assuming that, other than the Consideration Shares, there are no further issue of Shares from the date of this circular up to and including Completion
“Enlarged Group”	means the Company and its subsidiaries after Completion, including the Target Group
“Executive”	means the Executive Director of the Corporate Finance Division of the SFC and any delegate of such Executive Director
“Existing Capital”	means 712,180,953 Shares in issue as at the Latest Practicable Date
“Existing Group”	means the Company and its subsidiaries prior to Completion
“Existing Waiver”	means the waiver already granted to the Company by the Hong Kong Stock Exchange dated 5 May 1997 in respect of, among other things, the Services Agreement thereby exempting the Company from strict compliance with the requirements of the Hong Kong Listing Rules regarding those transactions and certain purchases and sales between the Group and the PCC Group
“Group”	means the Existing Group or the Enlarged Group, as the context requires
“HK\$”	means Hong Kong dollars, the lawful currency of Hong Kong

DEFINITIONS

“Hong Kong”	means the Hong Kong Special Administrative Region of the PRC
“Hong Kong Listing Rules”	means the Rules Governing the Listing of Securities on the Hong Kong Stock Exchange
“Hong Kong Stock Exchange”	means The Stock Exchange of Hong Kong Limited
“HSBC”	means The Hongkong and Shanghai Banking Corporation Limited, the independent financial adviser to the Independent Board Committee in relation to the Acquisition
“Independent Board Committee”	means the committee comprising Mr Shih Hung and Mr John J.D. Sy, both of whom are independent non-executive directors, formed to advise the Independent Shareholders in respect of the Acquisition Agreement
“Independent Shareholders”	means Mr Choi Kwok Keung (who is a non-executive Director) and Shareholders other than PCC, Max Creation and parties acting in concert with and presumed to be acting in concert with them
“Kleine”	means Kleine Developments Limited, a company owned beneficially as to 96.32% by PCC
“Latest Practicable Date”	2 October 2002 being the latest practicable date prior to the printing of this circular for ascertaining certain information for inclusion herein
“NT\$”	means New Taiwan dollars, the lawful currency of Taiwan
“PCC”	means Pou Chen Corporation (寶成工業股份有限公司), a company incorporated in Taiwan with limited liability and the securities of which are listed on the Taiwan Stock Exchange
“PCC Group”	means PCC and its subsidiaries. For the avoidance of doubt, this excludes members of the Target Group and the Existing Group
“PCC Property”	means 台灣彰化縣永靖鄉永福路一段265號 (No. 265, Section 1 Yong Fu Road, Yong Jing Hsian, Chang Hua, Taiwan), a property owned by PCC
“Production Agreement”	means the production agreement dated 24 December 1996 and made between Barits and Prime Asia Taiwan
“Production Fees”	means the production fees payable by Prime Asia Taiwan to Barits pursuant to the Production Agreement

DEFINITIONS

“Prime Asia Taiwan”	means Prime Asia Leather Corporation, Taiwan Branch, a member of the Target Group that will become a wholly-owned subsidiary of the Company upon Completion
“Pou Chien”	means Pou Chien Chemical Co. Ltd, one of the Target Companies that will become a wholly-owned subsidiary of the Company upon Completion
“Pou Chien Lease Agreement”	means the lease agreement dated 1 April 2002 and made between Pou Chien and PCC
“Pou Yuen”	means Pou Yuen Technology Limited, a company which is beneficially owned by PCC as to 96.32%
“Pou Yuen Lease Agreement”	means the lease agreement dated 1 October 2002 and made between Pou Yuen and Pou Chien or such other subsidiary of the Group as nominated by the Company
“Pou Yuen Assets”	means the assets (including the Pou Yuen Property), facilities and equipment owned by Pou Yuen for the research and development and production purposes of shoe moulds owned by Pou Yuen
“Pou Yuen Property”	means 台灣彰化縣福興鄉福工路4號 (No. 4, Fu Kung Road, Fu Hsin Hsian, Chang Hua, Taiwan), a property owned by Pou Yuen
“PRC”	means the People’s Republic of China
“Sale Shares”	means the issued share capital of each of the Target Companies held by the Vendors
“Services Agreement”	means the agreement dated 22 February 1997 and made between the Company and PCC in relation to the provision of services by PCC to the Group
“SFC”	means the Securities and Futures Commission of Hong Kong
“Share(s)”	means share(s) of par value of HK\$0.50 each in the capital of the Company
“Shareholders”	means the holders of the Shares in the Company’s share register
“Shareholders’ Loans”	means an aggregate sum of US\$62,386,041 currently payable by the members of the Target Group to Wealthplus and Kleine and which will be assigned to the Company or its nominee on a dollar for dollar basis upon Completion

DEFINITIONS

“Special General Meeting”	means the special general meeting of the Company to be held at Sung Room I, 4th Floor, Sheraton Hong Kong Hotel and Towers, 20 Nathan Road, Kowloon, Hong Kong at 10:30 a.m. on 29 October 2002, notice of which is set out on pages 59 to 60 of this circular, or any adjournment thereof
“Stable Future”	means Stable Future Trading Limited, a company which is 100% beneficially owned by Top Score, which in turn is 100% beneficially owned by Barits. Barits is beneficially owned as to 97.63% by PCC
“Takeovers Code”	means the Hong Kong Code on Takeovers and Mergers
“Taiwan”	means Taiwan, Republic of China
“Taiwan Stock Exchange”	means the Taiwan Stock Exchange Corporation
“Target Companies”	means Murata Profits Ltd., Wellspeed Trading Ltd., Pou Chien Chemical (Holdings) Ltd., Fu Tai Company Ltd., Champolian Investments Inc., Escon Enterprises Ltd., Giacinto Investments Ltd., Glenhurst Trading Ltd., Pou Ming Paper Products Manufacturing Company Ltd., Bestful Properties Ltd., Stencil International Ltd., Farquharson Holdings Corp., Patterns Developments Ltd., Forearn Company Ltd., Bortum Holdings Ltd., Blessland Enterprises Ltd., Nan Pao Resins (Holdings) Limited and Cohen Enterprises Inc., all of which are incorporated in the British Virgin Islands with limited liability and who are the intermediate holding companies of other members of the Target Group
“Target Group”	means the Target Companies, their subsidiaries, associates and jointly controlled entities, a list of which is set out in the paragraph headed “Business of the Target Group” in the letter from the Chairman as set out in this Circular
“Target Subsidiaries”	means the Target Companies and their subsidiaries excluding Blessland Enterprises Ltd., Nan Pao Resins (Holdings) Limited and Cohen Enterprises Inc.
“Top Score”	means Top Score Investments Limited, a company incorporated in the BVI which is 100% beneficially owned by Barits, which in turn is beneficially owned as to 97.63% by PCC
“US”	means the United States of America
“US\$”	means US dollars, the lawful currency of the United States of America

DEFINITIONS

“Vendors”	means Wealthplus, Kleine, and Stable Future
“Wealthplus”	means Wealthplus Holdings Limited, a company which is beneficially owned as to 100% by PCC

For information only, we have used the following exchange rates in this circular:–

$$\begin{aligned}HK\$7.8 &= US\$1.00 \\NT\$4.4 &= HK\$1.00 \\NT\$34.406 &= US\$1.00\end{aligned}$$

No representation is made that the relevant currencies were exchanged at the above rates or at all.

LETTER FROM THE CHAIRMAN



YUE YUEN INDUSTRIAL (HOLDINGS) LIMITED
(裕元工業(集團)有限公司)

(incorporated in Bermuda with limited liability)

Board of Directors:

Tsai Chi Neng (*Chairman*)
David N.F. Tsai (*Managing Director*)
Li I Nan, Steve
Kung Sung Yen
Lu Chin Chu
Kuo Tai Yu
Edward Y. Ku
Chan Lu Min

Registered Office:

Clarendon House
Church Street
Hamilton HM11
Bermuda

Principal Office:

7th Floor, Blocks A-D
Hop Hing Industrial Building
702 Castle Peak Road
Kowloon, Hong Kong

Non-executive Directors:

Choi Kwok Keung (*Vice Chairman*)
Shih Hung *
John J.D. Sy *

* *Independent Non-executive Director*

8 October 2002

*To the Shareholders and, for information only,
the holders of share options granted by the Company*

Dear Sir or Madam,

DISCLOSEABLE AND CONNECTED TRANSACTION

INTRODUCTION

On 17 September 2002, the Directors announced, among other things, that on 16 September 2002, the Company had entered into the Acquisition Agreement with PCC and the Vendors whereby the Company agreed to purchase or procure the purchase of the Sale Shares and the Shareholders' Loans. Under the Hong Kong Listing Rules, the Acquisition constitutes a discloseable transaction for the Company. As PCC is the controlling shareholder of the Company, the Acquisition also constitutes a connected transaction for the Company under the Hong Kong Listing Rules. The purpose of this circular is to provide you with further information on the Acquisition.

LETTER FROM THE CHAIRMAN

THE ACQUISITION AGREEMENT

Date: 16 September 2002

Purchaser: The Company

Vendors: Wealthplus, Kleine and Stable Future

Guarantor: PCC

Assets to be acquired

The Company agreed to acquire or procure the acquisition of the Sale Shares and the Shareholders' Loans from the Vendors for the Consideration (subject to adjustments as described in the section headed "Consideration" below).

Consideration

Subject to the adjustments as described below, the total consideration for the Acquisition is US\$427 million (approximately HK\$3,330.6 million). The Consideration can be broken down as to US\$62,386,041 (approximately HK\$487 million) for the Shareholders' Loans and as to US\$364,613,959 (approximately HK\$2,844 million) for the Sale Shares. This Consideration shall be payable at Completion in the following manner:

- a. US\$186.8 million (approximately HK\$1,457.4 million) shall be satisfied by way of allotment and issue of 60 million Consideration Shares (representing approximately 8.4% and approximately 7.8% of the Existing Capital and Enlarged Capital respectively), credited as fully paid up, at HK\$24.29 per Share. The Vendors have irrevocably directed that all of the Consideration Shares be allotted and issued to Wealthplus. The price per Consideration Share is based on the average closing price of the 90 consecutive trading days before (and excluding) 16 September 2002, the date on which trading in the Shares was suspended on the Hong Kong Stock Exchange pending the publication of the Announcement. The price per Consideration Share represents a premium of approximately 2.5% over the closing price of HK\$23.70 per Share as quoted on the Hong Kong Stock Exchange on 13 September 2002 (the last trading before and excluding the day on which trading in the Shares was suspended on the Hong Kong Stock Exchange pending the publication of the Announcement), and a premium of approximately 7.0% over the closing price on the Latest Practicable Date. The price per Consideration Share was arrived at based on arm's length negotiations and the price being acceptable by both the Company and the Vendors; and
- b. US\$240.2 million (approximately HK\$1,873.2 million) shall be payable in cash.

LETTER FROM THE CHAIRMAN

The Consideration was arrived at after arm's length negotiations and represents a prospective price-earning multiple of 9.57 times of the net profit after taxation and minority interests of US\$44.6 million (approximately HK\$348 million) of the Target Group for the fiscal year ended 30 September 2002 (the "Guaranteed Profits"). If the actual net profit after taxation and minority interests of the Target Group for the fiscal year ended 30 September 2002 is:-

- a. less than US\$44.6 million (approximately HK\$348 million), then the Vendors will pay the Company an additional cash amount equal to the shortfall multiplied by 9.57 times; or
- b. more than US\$44.6 million (approximately HK\$348 million), then the Company shall pay the Vendors an additional cash sum equal to the excess multiplied by 9.57 times. In any event, however, an additional cash amount will not exceed US\$9.57 million (approximately HK\$75 million).

The aforesaid payment shall be settled within 30 days after the availability of the audited pro forma closing accounts in respect of the Target Group for the year ended and as at 30 September 2002.

Lock-up period for Shares

The Vendors and PCC undertake to the Company not to sell, and shall procure that members of the PCC Group shall not sell, any Shares (including the Consideration Shares) nor shall they dispose of interest in such Shares through the grant of options, warrants, equity related instruments or otherwise for a period of 6 full calendar months from the date of Completion.

Non-Competition Undertaking

PCC undertakes in the Acquisition Agreement that it will not, and will procure that each member of the PCC Group will not:-

- a. while PCC remains directly or indirectly interested in 10% or more of the share capital of the Company then in issue; and
- b. for a period of three years after it ceases to be directly or indirectly interested in 10% or more of the share capital of the Company then in issue directly or indirectly,

be engaged or interested in any capacity (whether for reward or otherwise) in any business (other than through the Company) which is engaged in the production on a commercial scale of raw materials, components, machinery, moulds and tools for shoes outside Taiwan and in such places where the Company and its Associates has operations and/or sales.

However, the Acquisition Agreement shall not prevent, or be breached by, the holding of an equity interest in any body corporate which does not exceed 10% of the entire equity interests in that body corporate and where such interest does not give PCC Group effective control of the relevant body corporate.

LETTER FROM THE CHAIRMAN

Conditions Precedent

Completion is subject to and conditional upon, among other things, the satisfaction of the following conditions:

- a. the passing of resolution(s) by the Independent Shareholders at a general meeting of the Company approving the Acquisition Agreement (including the Consideration Shares to be allotted and issued thereunder) to the extent required under the Hong Kong Listing Rules;
- b. the Company having been granted approval by the Listing Committee of the Hong Kong Stock Exchange for the listing of and permission to deal in the Consideration Shares to be issued;
- c. the approval, if necessary, by the Bermuda Monetary Authority, of the proposed allotment and issue of all of the Consideration Shares and the consent or approval of any other relevant regulatory authority in Bermuda in relation to such allotment and issue;
- d. in respect of the Vendors, all consents and approvals of any relevant governmental authorities or other relevant third parties in Hong Kong, Taiwan or elsewhere which are required or appropriate for the entry into and the implementation of the Acquisition Agreement having been obtained, including all filings with any relevant governmental authorities or other relevant third parties;
- e. save and except for trade receivables and payables between the Target Companies and the PCC Group which fall within the scope of the terms of the Existing Waiver in connection with the Services Agreement, all amounts due to and from any of the Target Companies to other members of the PCC Group are settled;
- f. there being no material breach of the representations, warranties, undertakings and indemnities given pursuant to the Acquisition Agreement; and
- g. confirmation by the Executive that the issue of the Consideration Shares to Wealthplus will not give rise to a mandatory general offer obligation under the Takeovers Code or, alternatively, a waiver is granted by the Executive in respect of such obligation.

Completion

Completion shall take place on the fifth business day after all the conditions precedent are fulfilled or waived, as the case may be. The Company may waive any of the conditions precedent except for (a) to (c) and (g) above. The parties have agreed that if the conditions precedent are not fulfilled or waived, as the case may be, on or before 31 October 2002 (or such later date as the parties may agree), the Acquisition Agreement shall lapse.

LETTER FROM THE CHAIRMAN

Guarantee Indemnity

The PCC Group has also provided guarantees to banks in respect of borrowings by members of the Target Group. The guarantees to banks were provided upon normal commercial terms. The Company has agreed to use its reasonable endeavours to release and/or replace these guarantees within one month after Completion. Such release and/or replacement will be in compliance with the Hong Kong Listing Rules. As far as the Directors are aware, they do not foresee any reason which will act as an impediment to the release and/or replacement of these guarantees within this period.

In the interim, pending such release and/or replacement, the Company has agreed to indemnify the relevant member of the PCC Group in the event that any of the guarantees they have provided are called upon after Completion. Save for the abovementioned guarantees, the indemnity does not cover any liability arising out of any other guarantees whether provided by or in favour of any member of the PCC Group. The total amount secured by such guarantees is US\$37.4 million (approximately HK\$291.7 million) at varying percentage spreads above local borrowing rates. US\$17.5 million (approximately HK\$136.5 million) of the guaranteed amount is given in favour of members of the Target Group that will become non-wholly owned subsidiaries or associated companies. Approximately US\$12.8 million (approximately HK\$99.8 million) of the borrowings secured by the guarantees has been utilised. This indemnity, as with other terms of the Acquisition Agreement, is a result of arm's length negotiation between the parties to the Acquisition Agreement.

If the abovementioned guarantees of US\$37.4 million cannot be released or replaced on or before Completion, they will constitute connected transactions, which are exempted from further disclosure or shareholder approval under rule 14.24(8) of the Hong Kong Listing Rules. The related indemnity given under the Acquisition Agreement will, after Completion, constitute connected transactions under rule 14.26(7). Taking into account the Company's maximum liability of US\$37.4 million plus any accrued interests, this maximum liability represents an amount higher than 3% of the Company's consolidated net tangible assets as at the fiscal year ended 30 September 2001 or HK\$10 million. This indemnity is a term of the Acquisition Agreement in respect of which Independent Shareholders' approval is sought. Should Independent Shareholders approve the Acquisition Agreement, this would also constitute an approval of the indemnity provision therein as required under the Hong Kong Listing Rules.

SHAREHOLDING STRUCTURE OF THE COMPANY

As at the Latest Practicable Date, the authorized share capital of the Company is HK\$500,000,000 divided into 1,000,000,000 Shares, and the existing issued share capital is HK\$356,090,476.5 divided into 712,180,953 Shares. After Completion and upon the issue of the Consideration Shares, the issued share capital of the Company shall increase to HK\$386,090,476.5 divided into 772,180,953 Shares.

LETTER FROM THE CHAIRMAN

The existing shareholding structure of the Company as at the Latest Practicable Date and the shareholding structure of the Company immediately upon Completion shall be as follows:–

Name of shareholder	Existing shareholdings		Immediately upon Completion	
	No. of Shares	Approximate %	No. of Shares	Approximate %
PCC, Max Creation and parties acting in concert with and presumed to be acting in concert with them				
PCC (<i>Note (a)</i>)	292,240,350	41.0%	352,240,350	45.6%
Max Creation (<i>Note (b)</i>)	174,682,750	24.5%	174,682,750	22.6%
Mr Chan Lu Min (<i>Note (c)</i>)	100,000	0.01%	100,000	0.01%
Sub-total	467,023,100	65.5%	527,023,100	68.2%
Mr Choi Kwok Keung (<i>Note (d)</i>)	21,020,560	2.95%	21,020,560	2.72%
Public	224,137,293	31.6%	224,137,293	29.1%
Total	<u>712,180,953</u>	<u>100.0%</u>	<u>772,180,953</u>	<u>100.0%</u>

Notes:

- (a) Of the 292,240,350 Shares beneficially owned by PCC, 266,231,581 Shares were held by Wealthplus, 23,911,169 Shares were held by Win Fortune Investments Limited (“Win Fortune”) and 2,097,600 Shares were held by Top Score. Both Wealthplus and Win Fortune are wholly and beneficially owned subsidiaries of PCC and Top Score is a 97.63% beneficially owned subsidiary of PCC.
- (b) Of the 174,682,750 Shares beneficially owned by Max Creation Industrial Limited (“Max Creation”), these were all held through its wholly owned subsidiaries. World Future Investments Limited (“World Future”) is deemed to be interested in the 174,682,750 Shares held by Max Creation by virtue of World Future’s interest in more than one third of the voting shares in Max Creation. Mr Tsai Chi Jui, a brother of Mr Tsai Chi Neng who is a Director and Chairman of the Company, is deemed to be interested in the 174,682,750 Shares held by Max Creation as he holds 100% of the issued share capital in World Future.
- (c) Mr Chan Lu Min is a Director who is interested in approximately 0.01% of the Existing Capital, and immediately after Completion, he will be interested in approximately 0.01% of the Enlarged Capital.
- (d) Mr Choi Kwok Keung is a non-executive director. He is not acting in concert with PCC, Max Creation and parties acting in concert with and presumed to be acting in concert with them.

As at the Latest Practicable Date, PCC, Max Creation and parties acting in concert with and presumed to be acting in concert with them, were interested in 467,023,100 Shares, representing about 65.5% of the Existing Capital. Upon completion of the Acquisition Agreement, PCC, Max Creation and parties acting in concert with and presumed to be acting in concert with them will be interested in 527,023,100 Shares, representing about 68.2% of the Enlarged Capital. If the condition precedent in (g) above is not fulfilled, the Acquisition will not proceed.

LETTER FROM THE CHAIRMAN

FINANCIAL INFORMATION ON THE COMPANY

Set out below is the financial information extracted from the Company's audited annual reports for the two fiscal years ended 30 September 2000 and 30 September 2001 and its unaudited interim report for the six month period ended 31 March 2002:–

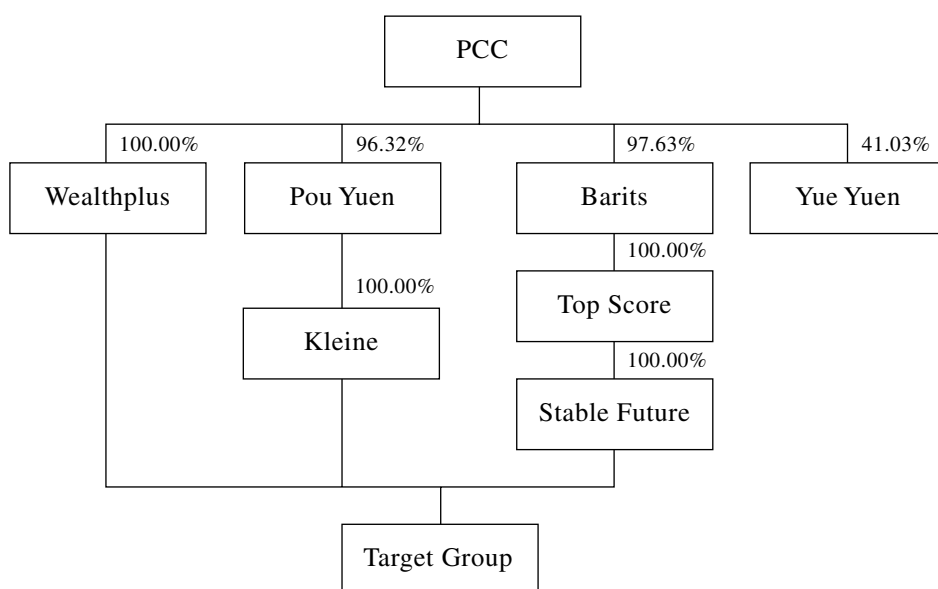
	For the fiscal year ended 30 September 2000		2001		For the six month period ended 31 March 2002	
	(US\$ million)	(HK\$ million)	(US\$ million)	(HK\$ million)	(US\$ million)	(HK\$ million)
Turnover	1,691.1	13,190.6	1,779.7	13,881.7	909.2	7,091.8
Net profit before taxation and minority interests	212.4	1,656.7	213.0	1,661.4	110.3	860.3
Net profit after taxation and minority interests	210.2	1,639.6	212.8	1,659.8	110.6	862.7
Net tangible assets	948.9	7,401.4	1,058.4	8,255.5	1,170.8	9,132.2

GROUP STRUCTURE

Yue Yuen is a company whose Shares are listed on the Hong Kong Stock Exchange and engaged in the manufacture and marketing of footwear. PCC is the controlling shareholder of Yue Yuen and currently owns 292,240,350 Shares, representing 41.0% of the total issued Shares. The following diagrams illustrate the group structure before and after Completion of the Acquisition:

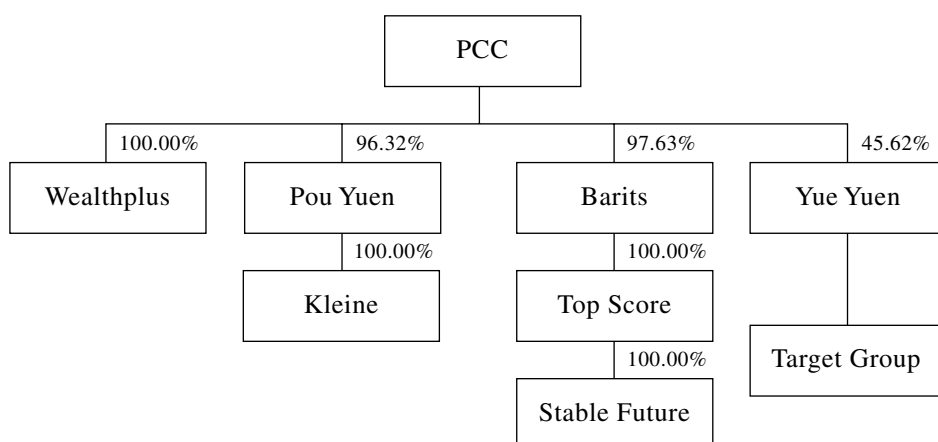
Group Structure

Before Completion of the Acquisition



LETTER FROM THE CHAIRMAN

After Completion of the Acquisition



Following Completion of the Acquisition, Yue Yuen will hold the Sale Shares of the Target Companies and continue the routine raw material procurement from the Target Group.

BUSINESS OF THE TARGET GROUP

The 67 companies in the Target Group include 47 operating companies and 20 investment holding companies which engage in the manufacture, trading or investing in raw materials, components, machinery, moulds and tools for shoes.

Below is the table outlining the brief business description of each company of the Target Group:

No.	Company Name	Place of Incorporation	Shareholding (%)	Business
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Members of the Target Group which will become subsidiaries of Yue Yuen after Completion

Raw Materials

1	Pou Chien Chemical Company Limited	Taiwan	99.94%	Manufacturing of shoe materials (chemical products)
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Production Tools

2	Forearn Company Ltd.	BVI	100%	Manufacturing of shoe moulds
3	Golden Chain Developments Limited	BVI	80%	Manufacturing of cutting moulds
4	Multiform Enterprises Limited	BVI	100%	Moulding equipment
5	Octavia Developments Limited	BVI	51%	Ventilation slots
6	PT. Suksespermatana Indonusa	Indonesia	90%	Manufacturing of mould & cutting for shoes
7	Veeragoo Trading Limited	BVI	100%	Inactive

LETTER FROM THE CHAIRMAN

No.	Company Name	Place of Incorporation	Shareholding (%)	Business
<i>Shoe Components</i>				
8	Bestful Properties Limited	BVI	100%	Property investment – leases Huangjiang factory to Prime Asia
9	Escon Enterprises Limited	BVI	100%	Leases machinery, equipment to Prime Asia, provision of sub-contracting services for manufacturing of leather
10	Essington Developments Limited	BVI	55%	Manufacturing of shoe counters
11	Fu Tai Company Limited	BVI	100%	Manufacturing of shoe moulds and EVA midsole for shoes
12	Chang Yang Vietnam Limited	Vietnam	51%	Plastic shoe materials injection
13	Overboard Investments Limited	BVI	100%	Shoe pads
14	Pou Ming Paper Products Manufacturing Company Limited	BVI	100%	Production of paper carton boxes and investment holding company
15	PT. Citra Cikande	Indonesia	51%	Manufacturing of insole for shoe counters
16	PT. Variadhana Citraselaras	Indonesia	55%	Manufacturing of injection moulds for shoe components
17	Dah-Chen Shoe Materials Ltd.	Vietnam	51%	Shoe pads, reprinting, etc
18	Upturn Investments Limited	BVI	100%	Manufacturing of paper inner boxes and carton boxes
19	Chiya Vietnam Enterprise Limited	Vietnam	51%	Foamed cotton
20	Super Foam Vietnam Enterprise Limited	Vietnam	51%	Foamed cotton
21	Wellspeed Trading Limited	BVI	100%	Manufacturing of counter and oil bladder for shoes
22	Prime Asia Upper Company Limited	BVI	100%	Inactive
23	Optima Worldwide Corporation	BVI	100%	Provision of administration services to Prime Asia
24	Optima Worldwide Services Company Limited	Macau	100%	Provision of administration services to Prime Asia
25	Prime Asia China Leather Corporation	BVI	100%	Leather Trading
26	Prime Asia Leather Corporation, Taiwan Branch	Taiwan	100%	Leather Trading
27	Prime Asia (S.E. Asia) Leather Corporation	BVI	100%	Provision of administration services to Prime Asia
28	Wet Blue International Corporation	BVI	100%	Wet blue trading

LETTER FROM THE CHAIRMAN

No.	Company Name	Place of Incorporation	Shareholding (%)	Business
<i>Investment Holding Companies</i>				
29	High Shine Investments Limited	BVI	51%	Investment holding company
30	Top Units Developments Limited	BVI	51%	Investment holding company
31	Valuable Developments Limited	BVI	51%	Investment holding company
32	Aimful Investments Limited	BVI	51%	Investment holding company
33	Bond Ocean Investments Limited	BVI	51%	Investment holding company
34	Bortum Holdings Limited	BVI	100%	Investment holding company
35	Champolian Investments Inc.	BVI	100%	Investment holding company
36	Ettalon Investments Limited	BVI	100%	Investment holding company
37	Farquharson Holdings Corp.	BVI	100%	Investment holding company
38	Giacinto Investments Limited	BVI	100%	Investment holding company
39	Glenhurst Trading Limited	BVI	100%	Investment holding company
40	Murata Profits Limited	BVI	100%	Investment holding company
41	Patterns Developments Limited	BVI	100%	Investment holding company
42	Pou Chien Chemical (Holdings) Limited	BVI	100%	Investment holding company
43	Stencil International Limited	BVI	100%	Investment holding company
44	World Street Investments Limited	BVI	55%	Investment holding company
45	Prime Asia Leather Corporation	BVI	100%	Investment holding company
Members of the Target Group which will become jointly controlled entities of Yue Yuen after Completion				
<i>Production Tools</i>				
46	High Style Investments Limited	BVI	50%	High frequency, CNC, screen printing and spraying
<i>Shoe Components</i>				
47	Blessland Enterprises Limited	BVI	50%	Shoe pads
48	Cohen Enterprises Inc.	BVI	50%	Manufacturing of leather products for shoes
49	Topmost Industries Limited	BVI	50%	Manufacturing of counters for shoes
50	Twinways Investments Limited	BVI	50%	Manufacturing of injection moulds for shoe components

LETTER FROM THE CHAIRMAN

No.	Company Name	Place of Incorporation	Shareholding (%)	Business
Members of the Target Group which will become associates of Yue Yuen after Completion				
<i>Raw Materials</i>				
51	Nan Pao Resins (China) Co., Ltd.	PRC	37%	Glues/liquid coatings/powder coatings
52	Credition International Group Limited	BVI	35%	PU Plastic/hardeners/processing agents/lotion plaster/powder coatings
53	Eastlion Industrial Ltd.	BVI	35%	PU Plastic/hardeners/processing agents/lotion plaster/powder coatings
54	Eastlion Enterprises Ltd.	BVI	35%	Property investments provision for Nan Pao Resins (Holdings) Ltd.
55	Nan Pao Resins (Vietnam) Enterprise Limited	Vietnam	37%	Liquid coating/glues
<i>Production Tools</i>				
56	Original Designs Developments Limited	BVI	47%	Shoe lasts
<i>Shoe Components</i>				
57	Enthroned Group Limited	BVI	48.76%	Inactive
58	Bigfoot Limited	BVI	48.76%	Cloth product trading/cloth dyeing & processing/cloth shoe material binding
59	Platinum Long John Company Limited	Taiwan	48.76%	Cloth product trading/cloth dyeing & processing/cloth shoe material binding
60	Chifley Tower Limited	BVI	40%	Trademark
61	Natural Options Limited	BVI	38.3%	Foamed cotton
62	Just Lucky Investments Limited	BVI	38.3%	Provision of real estate leasing for the operation of Natural Options Ltd.
63	Nice Pearl Enterprises Limited	BVI	35%	Investment in land, factory and various equipments
<i>Investment Holdings Company</i>				
64	All Saints Enterprises Limited	BVI	37%	Investment holding company
65	Nan Pao Resins (Holdings) Limited	BVI	35%	Investment holding company
66	Rising Sun Associates Limited	BVI	37%	Investment holding company
Member of the Target Group which will become investment securities of Yue Yuen after Completion				
67	Precise Zone Investments Limited	BVI	17.65%	Provision of electroplating services

LETTER FROM THE CHAIRMAN

The 67 companies can be generally categorized into three major groups based on their activities and products:

- Manufacturing of the raw materials, mainly glues, hardeners, coatings and chemical materials used for shoe components;
- Manufacturing of the production tools, including moulds, moulding equipment and cutting equipment; and
- Manufacturing of major shoe components such as leather, shoe pads, midsoles, and counters

Members of the Target Subsidiaries which contribute a significant portion of the unaudited turnover in the Target Group include Prime Asia Leather Corporation (“Prime Asia” or item no. 45), Fu Tai Company Limited (“Fu Tai” or item no. 11) and Forearn Company Ltd. (“Forearn” or item no. 2). In addition, Cohen Enterprises Inc. (“Cohen” or item no. 48), one of the jointly controlled entities of the Company after Completion is a major profit contributor in the jointly controlled entities group and Nan Pao Resins (Holdings) Limited (“Nan Pao” or item no. 65), one of the associates of the Company after Completion is also a major profit contributor in the associates group. These five companies in aggregate contributed US\$18.1 million (approximately HK\$141.2 million) and US\$22.5 million (approximately HK\$175.5 million), or 65.8%, of the unaudited pro forma combined net profits of the Target Group for the fiscal year ended 30 September 2001 and the nine month period ended 30 June 2002, respectively.

Prime Asia

Prime Asia is one of the largest full grain leather tanneries in the world with a total factory area of approximately 110,000 square meters in Huangjiang, China. The company has a monthly production capacity in Taiwan and China of approximately 9 to 10 million square feet of full grain. Prime Asia is the single largest profit contributor to the Target Group.

The company imports wet blue as a raw material mainly from the US and Brazil. After various manufacturing processes such as dyeing, coloring, and drying, the final product is primarily provided to shoe manufacturers for sport and/or casual footwear production. Due to its stable quality, Prime Asia is one of the major designated full grain suppliers to the leading international shoe brands, including NIKE, ADIDAS and TIMBERLAND.

In 2001, the company suffered from soaring raw material costs due to the mad cow disease. Wet blue purchase cost soared to US\$87 per hide in 2001. This led to a profit decline in 2001 as the increase in costs were not fully reflected in the selling price. However, starting from September 2001, wet blue costs had dropped back to US\$65 per hide and the company experienced stronger margins.

Prime Asia is currently planning its production expansion into Vietnam through further investment in the manufacturing assets/facilities.

Fu Tai

Fu Tai is the largest manufacturer of ethylene vinylacetate (“EVA”) injection midsoles in the Target Group. It was founded in 1997 and since then, rapidly grew to become the biggest single EVA injection factory in southern China.

LETTER FROM THE CHAIRMAN

The company's production base is located in Huangjiang, the PRC, with approximately 4,500 employees. The factory, built in 1997, currently has a monthly production capacity of approximately 600 tonnes of EVA pellets, 1.8 million pairs of EVA injected midsoles, 0.8 million pairs of EVA compression moulded midsoles, 1.5 million pairs of rubber shoe soles, and 200 shoe moulds.

EVA injection is a manufacturing technology which was developed in 1995. Fu Tai achieved a strong profit growth of approximately 60% from 1999 to 2000 due to its leadership in applying the new technology relative to other manufacturers. However, since 2001, many competitors in southern China started to use the same technologies, which caused price competition and declining margins.

To improve profitability, Fu Tai has set out to enhance its manufacturing technology with further capital expenditures, maximise work force efficiency and vertically integrate its product portfolio.

Forearn

Forearn is the largest manufacturer of shoe moulds in the Target Group. It was founded in 1996 and now is a primary supplier to Yue Yuen.

The company's production bases are located in Dongguan and Zhongshan, the PRC, with approximately 1,300 employees. The company's manufacturing base includes 4 factories with a monthly production capacity of approximately 1,500-1,600 moulds. The footwear production process begins with creating moulds for the soles. The moulds are manufactured using multiple techniques including a three dimensional scaled computer, injection and compression to create the finished mould product prototype comprised of either steel or aluminum alloy.

Cohen

Cohen is a joint venture established in 1993 by Taiwan Kuo Yuen Tannery and Giacinto Investments Limited. It manufactures polyurethane ("PU") split leather to produce sport shoes for worldwide brands, including NIKE, REEBOK, ADIDAS, and NEW BALANCE. Cohen's factory is located in Huangjiang, the PRC, with a total area of approximately 74,000 square meters and has a monthly production capacity of approximately 5 to 6 million square feet of split.

PU split is the second layer of the genuine leather and is approximately 40% cheaper than full grain leather (the first layer). With PU coating on the surface, the product looks very similar to full grain leather and because of PU splits' low cost, it is widely used by many sport footwear brands nowadays as a substitute for full grain leather.

Cohen has one of the largest PU Split factories in the world with superior research and development capability. The company researches new technologies to improve the appearance and the texture of PU split, to achieve a consistency similar to real full grain leather. The company's competences in R&D and quality production have become its competitive advantages against other split producers. It works closely with all shoe brands to develop special split materials for new shoe designs. Due to such value-adding services and continuous efforts on new product development, 35% to 40% of the company's sales was generated from new products which enjoyed higher margins.

LETTER FROM THE CHAIRMAN

Nan Pao

Nan Pao is a joint venture established in 1992 between PCC and Nan Pao Resins Chemical Co., Ltd., an industry leader in Taiwan with 50 years of experience in manufacturing various kinds of resins, paints and adhesives. The holding company owns Huangjiang Nan Pao Shoe-Materials Factory in China as its production base which are ISO9002 and ISO14000 approved, employing nearly 500 workers with a production capacity of approximately 1,700 tonnes per month for adhesives, as well as approximately 500 tonnes per month for powder coating goods.

Currently the business focus of Nan Pao is on the production of all types of adhesives (e.g., hot-melt adhesives, water-based adhesives, PU adhesives, and etc.), powder coating and liquid coating. The products are used mainly in shoes, home furniture and appliances, and construction. Approximately 80% of the total sales was generated from adhesive products and approximately 20% from coating products.

In the future, the company aims to further improve its manufacturing automation, to develop non-toxic products, and to expand its customer base to include domestic China shoe manufacturers. In addition, the company is in the process of building a new factory, expected to be completed in 2003, which should boost the company's production capacity with a focus on increasing the capability of powder coating manufacturing and adhesives.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

Overview

The following table sets out a summary of the unaudited pro forma combined operating results of the Target Group:

	Pro Forma Combined					
	For the fiscal year ended 30 September		2001		For the nine month period	
	2000	2001	2001	2002	ended 30 June 2002	2002
	<i>(US\$ million)</i>	<i>(HK\$ million)</i>	<i>(US\$ million)</i>	<i>(HK\$ million)</i>	<i>(US\$ million)</i>	<i>(HK\$ million)</i>
Turnover	293.8	2,291.7	311.9	2,432.8	244.2	1,904.8
Raw materials	14.7	114.7	12.9	100.6	8.2	64.0
Production tools	32.6	254.3	35.2	274.6	24.4	190.3
Shoe components	246.5	1,922.7	263.8	2,057.6	211.6	1,650.5
Net profit before taxation and minority interests	41.3	322.1	29.8	232.4	35.5	276.9
Net profit after taxation and minority interests	41.0	319.8	27.5	214.5	34.2	266.8

The attributable unaudited pro forma combined net tangible assets for the Target Group was US\$194.3 million (approximately HK\$1,515.5 million) as at 30 June 2002 (excluding existing goodwill of US\$197,726 (approximately HK\$1.5 million)).

LETTER FROM THE CHAIRMAN

General

Turnover for the Target Subsidiaries can be segregated into three main segments including raw materials, production tools and shoe components which comprise approximately 4%, 11% and 85%, respectively, of the aggregate unaudited turnover for the latest fiscal year ended 30 September 2001.

Raw Materials

Being the first stage of the footwear manufacturer supply chain, the raw material supply segment principally engages in the processing and trading of raw materials for footwear manufacturing such as rubber, glue and other chemicals.

Production Tools

Being the manufacture of production tools for footwear manufacturing, such as shoe moulds and mould related equipments. The operating results of the shoe mould segment is dependent on the development of and the number of new designs which will be introduced to the market. The life cycle of a shoe mould is normally about six to twelve months unless there is unusually high demand to sustain production.

Shoe Components

This segment involves the manufacturing and trading of shoe components, including shoe soles, leather, paper boxes and other shoe components. The operating results of this segment is driven by the demand of footwear, which is affected by the overall business environment.

Nine Month Period Ended 30 June 2002 as compared to the Fiscal Year Ended 30 September 2001

The unaudited pro forma combined financial statements are not itself audited but the financial statements of the individual companies are themselves individually audited or reviewed for the fiscal year ended 30 September 2001 and Deloitte & Touche, Taiwan have reviewed the management accounts of the individual companies for the nine month period ended 30 June 2002.

Turnover

Turnover for the Target Subsidiaries reached US\$244.2 million (approximately HK\$1,904.8 million) for the nine month period ended 30 June 2002 which represents approximately 78% of the annual turnover of US\$311.9 million (approximately HK\$2,432.8 million) for the fiscal year ended 30 September 2001.

LETTER FROM THE CHAIRMAN

Turnover for each segment during the year/period are as follows:

Business Segment	Pro Forma Combined				Turnover for the nine month period ended 30 June 2002 as a percentage of the year ended 30 September 2001
	For the fiscal year ended 30 September 2001		For the nine month period ended 30 June 2002		
	<i>(US\$ million)</i>	<i>(HK\$ million)</i>	<i>(US\$ million)</i>	<i>(HK\$ million)</i>	
Raw materials	12.9	100.6	8.2	64.0	63.4%
Production tools	35.2	274.6	24.4	190.3	69.4%
Shoe components	263.8	2,057.6	211.6	1,650.5	80.2%
Total	<u>311.9</u>	<u>2,432.8</u>	<u>244.2</u>	<u>1,904.8</u>	78.3%

For the nine month period ended 30 June 2002, the raw materials segment achieved sales of US\$8.2 million (approximately HK\$64.0 million), or 63.4% of the sales of US\$12.9 million (approximately HK\$100.6 million) for the fiscal year ended 30 September 2001.

For the nine month period ended 30 June 2002, the production tools segment achieved sales of US\$24.4 million (approximately HK\$190.3 million), or approximately 69.4% of the sales of US\$35.2 million (approximately HK\$274.6 million) for the fiscal year ended 30 September 2001. The events of “September 11” have weakened consumer confidence and impacted the earnings of major global footwear players as reported in quarterly announcements. It is anticipated that this will lead to a reduction in research and development (“R&D”) and a slowdown in mould development which will impact the turnover for the fiscal year ended 30 September 2002.

For the nine month period ended 30 June 2002, the shoe components segment has achieved sales of US\$211.6 million (approximately HK\$1,650.5 million), or approximately 80.2% of the sales of US\$263.8 million (approximately HK\$2,057.6 million) for the fiscal year ended 30 September 2001. The increase in sales was mainly due to improved economies of scale of certain factories and sales expansion to external customers, offset by slower growth in leather products as a result of a slowdown in the footwear industry.

Cost of Sales and Gross Profit Margin

The overall gross profit margin for the nine month period ended 30 June 2002 has increased by 2% to 24% from 22% for the fiscal year ended 30 September 2001. The increase was as a result of an increase in gross margins for the raw materials and shoe components segments of 5% and 2% respectively. The raw materials margin for the nine month period ended 30 June 2002 is higher as compared to the fiscal year ended 30 September 2001 as a result of the termination of a sourcing contract with a third party sales agent and now undergoes direct procurement. Margins for the shoe components segment for the fiscal year ended 30 September 2001 is lower as compared to the nine month period ended 30 June 2002 as a result of higher cost prices of leather which were affected by the mad cow disease leading to higher cost of sales. Margins for the production tools segment have stabilised throughout the fiscal year ended 30 September 2001 and the nine month period ended 30 June 2002.

LETTER FROM THE CHAIRMAN

The cost of sales and gross profit margin of each segment are set out as below:

Business Segment	Pro Forma Combined				% Change
	For the fiscal year ended 30 September 2001		For the nine month period ended 30 June 2002		
	(US\$ million)	(HK\$ million)	(US\$ million)	(HK\$ million)	
Turnover					
Raw materials	12.9	100.6	8.2	64.0	
Production tools	35.2	274.6	24.4	190.3	
Shoe components	263.8	2,057.6	211.6	1,650.5	
Total	311.9	2,432.8	244.2	1,904.8	
Cost of Sales					
Raw materials	11.2	87.4	6.7	52.3	
Production tools	17.9	139.6	12.4	96.7	
Shoe components	214.8	1,675.4	167.1	1,303.4	
Total	243.9	1,902.4	186.2	1,452.4	
Gross Margin					
Raw materials	13%		18%		5%
Production tools	49%		49%		0%
Shoe components	19%		21%		2%
Weighted Average	22%		24%		2%

Other Non-Operating Revenue

Other non-operating revenue is expected to decrease for the fiscal year ended 30 September 2002 as a result of a lower contribution from the Taiwan operations.

Administrative Expenses

Administrative expenses are expected to decrease resulting from lower staff costs from the transfer of the supporting function from Hong Kong to the PRC which includes divisions such as accounting, financial reporting, company secretaries, purchasing and sales.

Distribution Expenses

Distribution expenses are not expected to fluctuate significantly.

Other Operating Expenses

Other operating expenses are not expected to fluctuate, which historically has been attributed to the fluctuation of the New Taiwan dollar which has stabilised.

Finance Costs

Finance costs have reduced significantly as a result of the repayment of short-term bank loans during the fiscal year ended 30 September 2001 as well as declining interest rates.

LETTER FROM THE CHAIRMAN

Taxation

The key driver for the fluctuation in taxation is primarily due to losses from the Taiwan operations. For the nine month period ended 30 June 2002, estimated losses from the Taiwan operations as per the management accounts which generate a tax credit of US\$0.38 million (approximately HK\$3.0 million).

Fiscal Year Ended 30 September 2001 as compared to the Fiscal Year Ended 30 September 2000

The unaudited pro forma combined financial statements are not itself audited but the financial statements of the individual companies are themselves individually audited or reviewed by Deloitte & Touche, Taiwan for each of the two fiscal years ended 30 September 2000 and 2001.

Turnover

Turnover for the Target Subsidiaries increased to US\$311.9 million (approximately HK\$2,432.8 million) for the fiscal year ended 30 September 2001, which represented an increase of US\$18.1 million (approximately HK\$141.2 million), or 6.2%, from US\$293.8 million (approximately HK\$2,291.7 million) for the fiscal year ended 30 September 2000.

Turnover of each segment during the year are as follows:

Business Segment	Pro Forma Combined			
	For the fiscal year ended 30 September 2000		For the fiscal year ended 30 September 2001	
	<i>(US\$ million)</i>	<i>(HK\$ million)</i>	<i>(US\$ million)</i>	<i>(HK\$ million)</i>
Raw materials	14.7	114.7	12.9	100.6
Production tools	32.6	254.3	35.2	274.6
Shoe components	246.5	1,922.7	263.8	2,057.6
Total	<u>293.8</u>	<u>2,291.7</u>	<u>311.9</u>	<u>2,432.8</u>

The raw materials segment fell by US\$1.8 million (approximately HK\$14.1 million) or approximately 12.2% to US\$12.9 million (approximately HK\$100.6 million) as a result of clients switching from PU materials to EVA materials for shoe midsole production.

Sales in the production tools segment increased by approximately 8% due to an increase in new moulds sold as a result of the growing shoe industry.

The shoe components segment increased by US\$17.3 million (approximately HK\$134.9 million), or 7.0%, to US\$263.8 million (approximately HK\$2,057.6 million) for the fiscal year ended 30 September 2001 from US\$246.5 million (approximately HK\$1,922.7 million) for the fiscal year ended 30 September 2000. The increase was attributed to increased sales to outsiders, the set-up of new factories and the growth in the shoe industry.

LETTER FROM THE CHAIRMAN

Cost of Sales and Gross Profit Margin

The overall gross profit margin for the fiscal year ended 30 September 2001 decreased by 1% to 22% from 23% for the fiscal year ended 30 September 2000. This was due to a decrease of 2% in gross margins for the raw materials, offset by an increase in gross margins of 1% for the production tools segment. The raw materials margin for the fiscal year ended 30 September 2001 is lower as compared to the fiscal year ended 30 September 2000 as a result of an increase in oil prices. However, margins in production tools segment for the fiscal year ended 30 September 2001 were higher as compared to the previous fiscal year as a result of greater economies of scale in production.

The cost of sales and gross profit margin of each segment are set out as below:

Business Segment	Pro Forma Combined				% Change
	For the fiscal year ended 30 September 2000		For the fiscal year ended 30 September 2001		
	<i>(US\$ million)</i>	<i>(HK\$ million)</i>	<i>(US\$ million)</i>	<i>(HK\$ million)</i>	
Turnover					
Raw materials	14.7	114.7	12.9	100.6	(13%)
Production tools	32.6	254.3	35.2	274.6	8%
Shoe components	246.5	1,922.7	263.8	2,057.6	7%
Total	293.8	2,291.7	311.9	2,432.8	6%
Cost of Sales					
Raw materials	12.5	97.5	11.2	87.4	(10.4%)
Production tools	17.0	132.6	17.9	139.6	5.2%
Shoe components	196.8	1,535.0	214.8	1,675.4	9.2%
Total	226.3	1,765.1	243.9	1,902.4	7.8%
Gross Margin					
Raw materials	15%		13%		
Production tools	48%		49%		
Shoe components	20%		19%		
Weighted Average	23%		22%		

Other Non-Operating Revenue

Other non-operating revenue decreased by US\$4.9 million (approximately HK\$38.3 million), or 43.2%, to US\$6.5 million (approximately HK\$50.7 million) for the fiscal year ended 30 September 2001 from US\$11.4 million (approximately HK\$88.8 million) for the fiscal year ended 30 September 2000.

The decrease in non-operating revenue resulted from a decrease in sales of scrap materials which in fiscal year ended 30 September 2000 were attributed to the disposal of defect moulds to external parties. In addition, the recovery of bad debts in the fiscal year ended 30 September 2000 has resulted in an increase in non-operating revenue as compared to the fiscal year ended 30 September 2001 which was immaterial.

LETTER FROM THE CHAIRMAN

Administrative Expenses

Administrative expenses for the Target Subsidiaries increased to US\$33.6 million (approximately HK\$262.1 million) for the fiscal year ended 30 September 2001, which represented an increase of US\$5.0 million (approximately HK\$38.9 million), or approximately 17.4%, from US\$28.6 million (approximately HK\$223.2 million) for the fiscal year ended 30 September 2000.

The increase in administrative expenses for the fiscal year ended 30 September 2001 was attributed to an increase in staff costs of US\$2.4 million (approximately HK\$18.7 million) relating to the expansion and new factories built for the production tools segment.

In addition, rental and building management fees increased by US\$2.6 million (approximately HK\$20.3 million) as a result of the establishment of new factories in Huangjiang by Fu Tai and Prime Asia, which includes the payment of technical fees and administrative expenses paid to PCC upon the establishment of these new factories in Huangjiang, which is one off and not expected to be recurring in nature.

Distribution Expenses

Distribution expenses for the Target Subsidiaries increased to approximately US\$10.5 million (approximately HK\$82.2 million) for the fiscal year ended 30 September 2001, which represented an increase of US\$2.8 million (approximately HK\$21.7 million), or approximately 36.0%, from US\$7.7 million (approximately HK\$60.4 million) for the fiscal year ended 30 September 2000.

The increase in distribution expenses was as a result of US\$2.0 million (approximately HK\$15.6 million) increase in commission expenses relating to the shoe components segment as the new commission structure only became in force from July 2000.

Other Operating Expenses

Other operating expenses for the Target Subsidiaries decreased to US\$4.3 million (approximately HK\$33.6 million) for the fiscal year ended 30 September 2001, which represented a decrease of US\$0.2 million (approximately HK\$1.6 million), or approximately 4.4%, from US\$4.5 million (approximately HK\$35.2 million) for the fiscal year ended 30 September 2000.

Exchange losses accounted for US\$4.1 million (approximately HK\$32.0 million), or approximately 95.3%, of total other operating expenses for the fiscal year ended 30 September 2001, primarily attributed to the Target Group's external sales which were denominated in New Taiwan dollars.

Finance Costs

Finance costs for the Target Subsidiaries decreased to US\$0.6 million (approximately HK\$4.7 million) for the fiscal year ended 30 September 2001, which represented a decrease of US\$0.2 million (approximately HK\$1.5 million), or approximately 22.9%, from US\$0.8 million (approximately HK\$6.5 million) for the fiscal year ended 30 September 2000.

The decrease in finance costs for the fiscal year ended 30 September 2001 was a result of the repayment of US\$5.0 million (approximately HK\$39.0 million) in short-term bank loans and a fall in general interest rates on trust receipt loans.

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Taxation

The income tax fluctuation is affected by the Taiwan operations. For the fiscal year ended 30 September 2000, the Taiwan operations made a loss of approximately NT\$45.8 million (approximately US\$1.3 million or HK\$10.4 million) with a tax credit of US\$0.14 million (approximately HK\$1.1 million). For the fiscal year ended 30 September 2001, these Taiwan operations made a profit of NT\$70.4 million (approximately US\$2.1 million or HK\$16.0 million) and has therefore incurred a tax charge of US\$0.71 million (approximately HK\$5.5 million).

RATIONALE FOR THE ACQUISITION

The Directors believe that the Acquisition represents a unique opportunity for the Group and will benefit the Group in the following ways.

- **Complete vertical integration**

The Acquisition is consistent with the Group's strategy to focus on and to expand its core business of footwear production. The Acquisition is a critical step for the Group towards completing its upstream integration and supply chain management strategy. After the Acquisition, the Group will gain control over most of the raw material manufacturing businesses currently controlled by the PCC Group and fully integrate the footwear manufacturing process. As a result, the Group will be able to manage both production quality, inventory and purchasing costs in a more efficient and flexible manner.

- **Enhance financial position and performance**

The Acquisition enhances the Group's earnings base and enlarges the asset base. The Acquisition is expected to further diversify the Group's business activities and client base. The Target Group's unaudited net profit after taxation and minority interests was US\$34.2 million (approximately HK\$266.8 million) for the first nine months ended 30 June 2002 and over 50% of the Target Group's turnover was generated from independent customers. By consolidating the operation of the Target Group, the Company is expected to capture a wider customer base and financially, to achieve higher revenue and margin enhancement.

- **Consolidate market leadership**

The Company has long been recognized as one of the leading manufacturers and suppliers to a number of internationally well-known brands of athletic and casual footwear. The Acquisition will enable the Group to maintain its strong market leadership through providing more efficient and better services and products to its clients.

- **Enhance the capital structure**

Following the Acquisition, through the issue of Consideration Shares, the Group's equity base will be enlarged by approximately 8.4%, which will strengthen the Group's capital base.

- **Improve corporate transparency**

Following the Acquisition, the Group will have acquired substantially all the companies from the PCC Group which are involved in the manufacture of raw materials and components for

LETTER FROM THE CHAIRMAN

shoes and related production tools, moulds and equipment operations. As a result, after Completion, the number of connected transactions between the Group and the PCC Group is expected to reduce significantly. For the fiscal year ended 30 September 2001, the amount of purchases by the Group from the Target Group amounted to approximately US\$114.1 million (approximately HK\$890.0 million), which represents the majority of the aggregate connected transactions between the Group and the PCC Group.

Following the Acquisition, the Group expects to be able to improve its profitability and operational efficiency by gaining a stronger control over the quality and purchasing costs of the raw materials. In addition, the Acquisition simplifies the Group's current complicated organizational structure, and reduces the Group's connected transactions with the PCC Group. After the Acquisition, the Group will continue its routine raw material procurement from the members of the Target Group.

FINANCIAL IMPACT OF THE ACQUISITION

Impact on Earnings

The Acquisition is expected to increase the Group's revenue and earnings base. For the nine month period ended 30 June 2002, the Target Group achieved unaudited revenue of approximately US\$244.2 million (approximately HK\$1,904.8 million) and unaudited net profit before taxation and minority interests of US\$35.5 million (approximately HK\$276.9 million) respectively. The financial results of the Target Group are expected to make additional financial contributions to the Group.

Impact on Balance Sheet

As a result of the issue of the Consideration Shares, which represent approximately 8.4% and approximately 7.8% of the Existing Capital and Enlarged Capital respectively, the Company's shareholders' equity is expected to increase by approximately US\$186.8 million (approximately HK\$1,457.4 million), which represents approximately 16.0% increase from the Group's shareholders' equity of US\$1,171 million as at 31 March 2002. It is expected that the Group will settle the cash portion of the Consideration by utilising its existing financing facilities, new bank loans and its cash holdings. After Completion, based on the Group's net debt of approximately US\$224.8 million (approximately HK\$1,753.4 million) as at 31 March 2002 and taking into account the settlement of the Consideration only, it is expected that the net debt will increase to approximately US\$467.5 million (approximately HK\$3,646.5 million), and the net debt to equity ratio will increase from 19.2% to 34.4%.

CONNECTED TRANSACTIONS AFTER COMPLETION

After Completion, a number of transactions or business arrangements between the Target Group with the PCC Group are expected to continue and these transactions will, after Completion, constitute new connected transactions for the Company under the Hong Kong Listing Rules.

LETTER FROM THE CHAIRMAN

POU CHIEN LEASE AGREEMENT

Parties to the Pou Chien Lease Agreement

Landlord: PCC

Tenant: Pou Chien

PCC Property: 台灣彰化縣永靖鄉永福路一段265號 (No. 265, Section 1 Yong Fu Road, Yong Jing Hsian, Chang Hua, Taiwan), which consists of building and land. The floor area for the building and the land is approximately 8,142.00 m² and 5,808.54 m² respectively

Reasons for the Pou Chien Lease Agreement

Pou Chien is a manufacturer of chemical products used in shoe manufacturing. Historically, Pou Chien has been carrying out its business on the PCC Property pursuant to the Pou Chien Lease Agreement and the Company has decided that this arrangement should continue after Completion to avoid any possible disruption to Pou Chien's operations.

Terms of the Pou Chien Lease Agreement

Under the Pou Chien Lease Agreement, PCC agreed to lease to Pou Chien the PCC Property situated in Taiwan for a period of 21 months from 1 April 2002 to 31 December 2003 at a monthly rent of NT\$476,280 (approximately US\$13,843 and HK\$108,245). Completion is not expected to occur until after 30 September 2002, and for reference only, the estimated value of this connected transaction for the period from 1 October 2002 to 31 December 2003 is NT\$7,144,200 (approximately US\$207,644 and HK\$1.6 million). This has been based on the agreed monthly rental under the Pou Chien Lease Agreement, and has been the subject of an independent valuation issued by an independent valuer in Taiwan.

As PCC is the controlling shareholder of the Company, and Pou Chien will, after Completion, become a wholly-owned subsidiary of the Company, the transactions under the Pou Chien Lease Agreement will, after Completion, constitute a connected transaction for the Group. The Directors believe that the amount of rental is fair and reasonable and as the aggregate rental is less than the higher of 0.03% of the Company's consolidated net tangible assets as at 30 September 2001 or HK\$1 million, no further announcement or shareholder approval is required pursuant to Rule 14.24 of the Hong Kong Listing Rules.

POU YUEN LEASE AGREEMENT

Parties to the Pou Yuen Lease Agreement

Landlord: Pou Yuen

Tenant: Pou Chien or such other subsidiary of the Group as nominated by the Company

Pou Yuen Property: 台灣彰化縣福興鄉福工路4號 (No. 4, Fu Kung Road, Fu Hsin Hsian, Chang Hua, Taiwan), which consists of building and land. The floor area for the building and land is approximately 8,355.68 m² and 7,888.00 m² respectively

LETTER FROM THE CHAIRMAN

Reasons for the Pou Yuen Lease Agreement

Historically, Pou Yuen has been providing R&D of shoe moulds for certain members of the Target Group. After the Acquisition, the Company intends to establish this R&D capability within the Group but will continue to carry out such activities on the Pou Yuen Property pursuant to the Pou Yuen Lease Agreement. The Company has decided that this arrangement after Completion is preferable to utilise existing facilities at the Pou Yuen Property and to expedite its establishment of such R&D capability.

Terms of the Pou Yuen Lease Agreement

The Pou Yuen Lease Agreement is conditional on Completion. Under the Pou Yuen Lease Agreement, Pou Yuen agreed to lease to Pou Chien or such other subsidiary of the Group as nominated by the Company the Pou Yuen Assets for a period of 36 months from 1 October 2002 to 30 September 2005. The approximate and estimated total rental for the Pou Yuen Assets estimated by the Company for each of the fiscal years ending 30 September 2005 is US\$1 million (approximately HK\$7.8 million). This is based on an independent valuation issued by an independent valuer in Taiwan.

As Pou Yuen is a member of the PCC Group, and Pou Chien will, after Completion, become a wholly-owned subsidiary of the Company, the transactions under the Pou Yuen Lease Agreement will, after Completion, constitute a connected transaction for the Group. The Directors believe that the amount of rental is fair and reasonable and as the rental for each relevant financial year is expected to be over the higher of 0.03% of the Company's consolidated net tangible assets as at 30 September 2001 or HK\$1 million but less than the higher of 3% of the Company's consolidated net tangible assets as at 30 September 2001 or HK\$10 million, no shareholder approval is required for the Pou Yuen Lease Agreement pursuant to Rule 14.25 of the Hong Kong Listing Rules. However, details of the Pou Yuen Lease Agreement will be included in the Company's relevant annual report and accounts.

PRODUCTION AGREEMENT

Terms of the Production Agreement

The Production Agreement between Barits and Prime Asia Taiwan came into effect as of 1 January 1997.

Prime Asia Taiwan engages in the business of leather trading and manufacturing. Pursuant to the Production Agreement, Barits agreed to provide tanning facilities and processing services to Prime Asia Taiwan for the processing of Prime Asia Taiwan's raw leather in Taiwan into finished leather. In return, Prime Asia Taiwan agreed to pay Barits a monthly Production Fee. The Production Fee is equal to the total of the following:—

Variable costs	including costs for supplies and labour which will be charged to Prime Asia Taiwan at cost
Direct selling, general costs	including costs for transportation and insurance, R&D and other general administrative costs, which will be charged to Prime Asia Taiwan at cost

LETTER FROM THE CHAIRMAN

Fixed costs including rental of land, building, equipment and machinery. Rental charges for land and building is a fixed monthly rental determined on the basis of an independent valuation report issued at the time the Production Agreement was entered into. The total rental charges for land and building for the year ended 30 September 2001 amounted to approximately 2% of the total Production Fees paid for the same period. Rental charges for equipment and machinery are calculated by reference to the acquisition cost of the fixed assets plus a rate which is determined by reference to the funding costs of any machinery purchased

Prime Asia Taiwan also agreed under the Production Agreement to reimburse Barits for up to US\$2,000,000 for costs to Barits incurred in connection with any claim by any third person or governmental authority against Barits for violating applicable environmental laws in connection with its facilities in Taiwan used by Prime Asia Taiwan or with the depositing or transporting of any hazardous materials in relation to the Production Agreement.

Reasons for the Production Agreement

The Directors believe that current trends will eventually result in Prime Asia's operation being relocated to the PRC. Therefore, the Group intends not to further increase its investment in property, plants and equipment in Prime Asia's operations in Taiwan. The Production Agreement provides Prime Asia Taiwan manufacturing capacity and flexibility with a cost based production fee structure but without taking actual operating risks in Taiwan.

The Board believes that it is in the best interest of the Group and the Shareholders to continue Prime Asia Taiwan's operations under the Production Agreement and the terms are fair and reasonable to the Company.

Prime Asia Taiwan will become a wholly-owned subsidiary of the Company upon Completion. Barits is a member of the PCC Group and therefore a connected person of the Company. The Production Agreement will therefore become a connected transaction for the Group upon Completion.

Production Fees

The approximate and estimated total Production Fees estimated by the Company for any future financial year is US\$16 million (approximately HK\$124.8 million). This is determined on the basis of historical production fees paid by Prime Asia Taiwan to Barits, which was approximately US\$11.4 million (approximately HK\$89 million) for the first 9 months of year 2002 and approximately US\$15 million (approximately HK\$117 million) for the year 2001.

The Production Fees payable by the Group to Barits and the amount of costs reimbursement up to US\$2,000,000 mentioned above for any future financial year are expected to exceed the higher of 0.03% of the Company's consolidated net tangible assets for the relevant financial year or HK\$1 million but are not expected to exceed the higher of 3% of the Company's consolidated net tangible assets for the relevant financial year or HK\$10 million.

LETTER FROM THE CHAIRMAN

WAIVER FROM THE HONG KONG STOCK EXCHANGE

The Company has applied to the Hong Kong Stock Exchange for a waiver from the future obligations in making press announcements under Rule 14.25 of the Hong Kong Listing Rules in respect of ongoing connected transactions under the Production Agreement after Completion for the reasons set out below:–

- a. the Production Agreement represents ongoing transactions until such time as the agreement is terminated. The Directors consider that it would be impractical and unduly onerous on the part of the Group if the Company were required to comply fully with the applicable disclosure requirements on each occasion there is a connected transaction pursuant to the Production Agreement;
- b. the Production Agreement was entered into by Prime Asia Taiwan and Barits in the ordinary and usual course of their businesses;
- c. the Production Fees (including the amount of costs reimbursement up to US\$2,000,000 mentioned above) were negotiated between Prime Asia Taiwan and Barits on an arm's length basis and are on normal commercial terms or better for Prime Asia Taiwan; and
- d. the terms of the Production Agreement (including the amount of costs reimbursement up to US\$2,000,000 mentioned above) are fair and reasonable to the Shareholders as a whole.

The Hong Kong Stock Exchange has, subject to Completion, granted the waiver on the basis that:–

- a. the Production Fees for each financial year will not exceed the higher of 3% of the Company's consolidated net tangible assets for that financial year or HK\$10 million;
- b. for as long as the Production Agreement is in place, the Company's independent non-executive directors will confirm in the Company's next annual report whether:–
 - (i) the transactions contemplated under the Production Agreement have been entered into by the Group in the ordinary and usual course of its business;
 - (ii) the transactions contemplated under the Production Agreement have been entered into by the Group in accordance with the terms of the Production Agreement;
 - (iii) the transactions contemplated under the Production Agreement have been entered into on terms that are fair and reasonable as far as the Company and the Shareholders as a whole are concerned;
- c. the auditors of the Company will review the connected transactions under the Production Agreement annually and confirm in a letter to the Board, a copy of which shall be provided to the Listing Division of the Hong Kong Stock Exchange, stating whether:

LETTER FROM THE CHAIRMAN

- (i) the connected transactions were entered into in accordance with the terms of the Production Agreement;
 - (ii) the transactions under the Production Agreement have been approved by the Board; and
 - (iii) the Production Fees for that financial year exceeds the higher of 3% of the Company's consolidated net tangible assets for that financial year or HK\$10 million;
- d. the details of the connected transactions contemplated under the Production Agreement, shall be disclosed in the Company's next and each successive annual report pursuant to Rule 14.25(1)(ii)(A) to (D) of the Hong Kong Listing Rules;
- e. the Company and Barits will also provide to the Hong Kong Stock Exchange an undertaking that, for so long as the Production Agreement remains in place and continues to constitute connected transaction for the Group and the Company's shares are listed on the Hong Kong Stock Exchange, the Company and Barits will provide the Company's auditors with full access to their relevant records for the purpose of the auditors' review of the transactions under the Production Agreement; and
- f. if any terms of the Production Agreement is altered in any material respect, the Company must comply with the provisions of Chapter 14 of the Hong Kong Listing Rules unless it otherwise applies for and is granted a separate waiver from the Hong Kong Stock Exchange from such strict compliance.

DISCLOSEABLE AND CONNECTED TRANSACTION

As at the Latest Practicable Date, PCC indirectly owns or controls approximately 41% of the Company's issued share capital. PCC and the Vendors are therefore "connected persons" of the Company under the Hong Kong Listing Rules. Given that the consideration payable under the Acquisition Agreement is over 15% but below 50% of the Company's consolidated net tangible assets as at 31 March 2002, the Acquisition Agreement constitutes a "discloseable and connected transaction" for the Company under the Hong Kong Listing Rules and requires approval of the Independent Shareholders in the Special General Meeting. In accordance with the Hong Kong Listing Rules, PCC and its Associates who are Shareholders will abstain from voting on the resolutions to approve the Acquisition Agreement at the Special General Meeting of the Company.

CONFIRMATION ON NO GENERAL OFFER OBLIGATION

An application was made to the Executive requesting for the confirmation that there is no obligation on the part of the Vendors or any parties acting in concert with them to make a general offer to purchase the issued Shares as a result of the issue of Consideration Shares to Wealthplus under the Acquisition Agreement. Such confirmation was granted by the Executive on 4 October 2002 pursuant to Note 6 to Rule 26.1 of the Takeovers Code.

SPECIAL GENERAL MEETING

A notice concerning the Special General Meeting to be held at Sung Room I, 4th Floor, Sheraton Hong Kong Hotel and Towers, 20 Nathan Road, Kowloon, Hong Kong at 10:30 a.m. on 29 October 2002 is set out on pages 59 to 60 of this circular. Whether or not you are able to attend

LETTER FROM THE CHAIRMAN

the meeting in person, please complete the accompanying form of proxy in accordance with the printed instructions therein and deposit it at the office of the Company's principal office at 7th Floor, Blocks A-D, Hop Hing Industrial Building, 702 Castle Peak Road, Kowloon, Hong Kong as soon as possible but in any event no later than 48 hours before the time appointed for the holding of the meeting.

RECOMMENDATION

The letter from the Independent Board Committee containing its recommendation to the Independent Shareholders in respect of the Acquisition Agreement is set out on page 35 of this circular. The letter from independent financial advisor containing its advice to the Independent Board Committee in relation to the Acquisition Agreement and the principal factors and reasons taken into account in arriving at its recommendation is set out on pages 36 to 45 of this circular.

The Independent Board Committee, having taken into account the principal factors and reasons considered by independent financial advisor and the advice of independent financial advisor, considers that the terms of the Acquisition Agreement are fair and reasonable so far as the Independent Shareholders are concerned. Accordingly, the Independent Board Committee recommends the Independent Shareholders to vote in favour of the ordinary resolution to be proposed at the Special General Meeting to approve the Acquisition Agreement.

ADDITIONAL INFORMATION

Your attention is drawn to the letter from the Independent Board Committee set out on page 35 of this circular which contains its recommendations to the Independent Shareholders of the Company and the letter from the Independent Financial Adviser set out on pages 36 to 45 of this circular which sets out its advice to the Independent Director and the principal factors and reasons taken into consideration in arriving at such advice.

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

Yours faithfully,
Tsai Chi Neng
Chairman

LETTER FROM THE INDEPENDENT BOARD COMMITTEE



YUE YUEN INDUSTRIAL (HOLDINGS) LIMITED
(裕元工業(集團)有限公司)

(incorporated in Bermuda with limited liability)

Principal Office:

7th Floor, Blocks A-D
Hop Hing Industrial Building
702 Castle Peak Road
Kowloon, Hong Kong

Registered Office:

Clarendon House
Church Street
Hamilton HM11
Bermuda

8 October 2002

To the Independent Shareholders

Dear Sir or Madam,

DISCLOSEABLE AND CONNECTED TRANSACTION

We refer to the circular of the Company despatched to the Independent Shareholders dated 8 October 2002 (the "Circular"), of which this letter forms part. Terms defined in the Circular shall have the same meanings in this letter unless the context otherwise requires.

We, being the independent non-executive directors consisting the Independent Board Committee, have been appointed by the Board to advise you as to whether the terms of the Acquisition Agreement are fair and reasonable so far as the Independent Shareholders are concerned.

The Hongkong and Shanghai Banking Corporation Limited ("HSBC") has been appointed by the Company as the independent financial adviser to advise us regarding the terms of the Acquisition Agreement. Details of its advice, together with the principal factors taken into consideration in arriving at such advice, are set out in its letter on pages 36 to 45 of the Circular.

Your attention is also drawn to the letter from the Chairman set out on pages 7 to 34 of the Circular and the additional information set out in the appendices of the Circular.

Having taken into account the terms of the Acquisition Agreement, the interests of the Independent Shareholders as a whole and the advice of HSBC, we consider that the terms of the Acquisition Agreement are fair and reasonable so far as the Independent Shareholders are concerned. Accordingly, we recommend the Independent Shareholders to vote in favour of resolution number 1 to be proposed at the Special General Meeting to approve the Acquisition Agreement.

Yours faithfully,

For and on behalf of the
Independent Board Committee
Shih Hung and John J.D. Sy
Independent Non-executive Directors
of
Yue Yuen Industrial (Holdings) Limited

LETTER FROM INDEPENDENT FINANCIAL ADVISER

The following is the text of the letter of advice to the Independent Board Committee from The Hongkong and Shanghai Banking Corporation Limited dated 8 October 2002 prepared for incorporation in this Circular.



The Hongkong and Shanghai Banking Corporation Limited
Investment Banking and Markets
Level 15, 1 Queen's Road Central, Hong Kong

8 October 2002

The Independent Board Committee
Yue Yuen Industrial (Holdings) Limited
7th Floor, Blocks A-D
Hop Hing Industrial Building
702 Castle Peak Road
Kowloon, Hong Kong

Dear Sirs,

We have been appointed to act as the independent financial adviser to the Independent Board Committee in relation to the Acquisition Agreement. Details of the Acquisition Agreement are contained in the letter from the Chairman set out in a circular to shareholders of the Company dated 8 October 2002 (the "Circular") of which this letter forms part therein. Terms defined in the Circular shall have the same meanings in this letter unless the context otherwise requires.

In formulating our opinion, we have relied on the information and facts supplied and the opinions expressed by the Directors and we have assumed that all information and representations concerning the Group, the Target Group, the Acquisition, and the Acquisition Agreement contained or referred to in the Circular, which have been provided by the Directors and for which they are wholly responsible, are true and accurate in all respects at the date thereof and may be relied upon. We have also sought and received confirmation from the Directors that opinions expressed in the Circular have been arrived at after due and careful consideration and there are no other facts the omission of which would make any statement in the Circular misleading. We have not, however, conducted any form of investigation into the affairs of the Group nor have we carried out any independent verification of the information supplied.

Our recommendations with regard to the terms of the Acquisition Agreement have been made on the assumption that all reports made by experts within the meaning and context of the Hong Kong Listing Rules are fair and accurate and, accordingly, have relied upon them. We have further assumed that all the statements of intention of the Directors as set out in the Circular will be implemented.

LETTER FROM INDEPENDENT FINANCIAL ADVISER

In arriving at our recommendation on the terms of the Acquisition Agreement, we have taken into consideration, inter alia, the following principal factors and reasons:

(i) Business and Recent Performance of the Target Group

Business

The Target Group comprises 67 companies, the business of which can be generally categorized into three major groups based on their activities and products:

- Manufacturing of the raw materials, mainly glues, hardeners, coatings and chemical materials used for shoe components
- Manufacturing of the production tools, including moulds, moulding equipment and cutting equipment
- Manufacturing of major shoe components such as leather, shoe pads, midsoles, and counters

Members of the Target Subsidiaries which contribute a significant portion of the unaudited turnover in the Target Subsidiaries include Prime Asia Leather Corporation (“Prime Asia”), Fu Tai Company Limited (“Fu Tai”) and Forearn Company Ltd. (“Forearn”). In addition, Cohen Enterprises Inc. (“Cohen”) is a major profit contributor in the jointly controlled entities group and Nan Pao Resins (Holdings) Limited (“Nan Pao”) is a major profit contributor in the associates group. These five companies in aggregate contributed US\$18.1 million (approximately HK\$141.2 million) and US\$22.5 million (approximately HK\$175.5 million), or 65.8 per cent. and 65.8 per cent. respectively, of the unaudited combined net profit of the Target Group for the fiscal year ended 30 September 2001 and the first nine month period ended 30 June 2002, respectively.

Operating Results of the Target Group

Set out below is certain financial information extracted from the unaudited pro forma combined operating results of the Target Group:

	For the year ended 30 September				For the nine month period	
	2000		2001		ended 30 June 2002	
	<i>(US\$ million)</i>	<i>(HK\$ million)</i>	<i>(US\$ million)</i>	<i>(HK\$ million)</i>	<i>(US\$ million)</i>	<i>(HK\$ million)</i>
Turnover	293.8	2,291.7	311.9	2,432.8	244.2	1,904.8
Raw material	14.7	114.7	12.9	100.6	8.2	64.0
Production tools	32.6	254.3	35.2	274.6	24.4	190.3
Shoe component	246.5	1,922.7	263.8	2,057.6	211.6	1,650.5
Net profit before taxation and minority interests	41.3	322.1	29.8	232.4	35.5	276.9
Net profit after taxation and minority interests	41.0	319.8	27.5	214.5	34.2	266.8

LETTER FROM INDEPENDENT FINANCIAL ADVISER

Unaudited pro forma combined turnover of the Target Subsidiaries increased by approximately 6.2 per cent. to approximately US\$311.9 million for the fiscal year ended 30 September 2001 when compared with the corresponding period in 2000 due to increased sales to independent third parties, new factories and the growing shoe industry which is offset by a slight decrease in turnover from the raw materials segment. Unaudited pro forma combined net profit after taxation and minority interests of the Target Group decreased by approximately 32.9 per cent. to approximately US\$27.5 million for the fiscal year ended 30 September 2001 when compared with the corresponding period in 2000 as a result of a reduction in the overall gross profit margin and non-operating revenue, and an increase in administrative expenses and distribution costs. Unaudited pro forma combined turnover for the Target Subsidiaries and net profit after taxation and minority interests of the Target Group for the nine month period ended 30 June 2002 represent approximately 78.3 per cent. and 124.4 per cent. respectively of the respective figures for the fiscal year ended 30 September 2001. The high net profit contribution figure is mainly due to high sales contribution from the shoe components segment and an increase in overall gross profit margin.

(ii) Business Strategy of the Group

As noted from the Company's interim report for the 6 month period ended 31 March 2002, the Group has continued to actively execute its growth strategy through a combination of horizontal expansion and vertical integration.

From a horizontal perspective, the Group is expanding its customer base and broadening its product categories. In terms of vertical integration, the Group will continue to focus on opportunities to strengthen its strategic positions in upstream material supplies and downstream logistics in order to enhance cost efficiency and establish closer ties with customers.

The Acquisition forms an important part of the Group's continuing strategy of seeking vertical integration opportunities referred to above.

(iii) Rationale for the Acquisition

Through the Acquisition, the Group expects to be able to improve its profitability and operational efficiency by gaining a stronger control over the quality and purchasing costs of the raw materials. In addition, the Acquisition simplifies the Group's current complicated organizational structure, and materially reduces the Group's connected transactions with the PCC Group. After the Acquisition, the Group will continue its routine raw material procurement from the members of the Target Group. In summary, the Directors believe that the Acquisition represents a unique opportunity for the Group and will benefit the Group in the following ways.

- Complete vertical integration
- Enhance financial position and performance
- Consolidate market leadership

LETTER FROM INDEPENDENT FINANCIAL ADVISER

- Enhance the capital structure
- Improve corporate transparency

For details of the above reasons, please refer to the “Letter from the Chairman” of this Circular.

(iv) Valuation

The Consideration was arrived at after arm’s length negotiations and represents a prospective price earning multiple of 9.57 times of the guaranteed unaudited pro forma combined net profit after taxation and minority interests of US\$44.6 million (approximately HK\$348 million) of the Target Group for the year ended 30 September 2002 (the “Guaranteed Profits”).

The Consideration shall be subject to the achievement by the Target Group of the Guaranteed Profits for the year ended 30 September 2002. If the actual net profit after taxation and minority interests of the Target Group for the year ended 30 September 2002 is:

- a. less than US\$44.6 million (approximately HK\$348 million), then the Vendors will pay the Company an additional cash amount equal to the shortfall multiplied by 9.57 times; or
- b. more than US\$44.6 million (approximately HK\$348 million), then the Company shall pay the Vendors an additional cash sum equal to the excess multiplied by 9.57 times. This additional cash amount will be subject to a cap that will not exceed US\$9.57 million (approximately HK\$75 million).

We have had particular regard to both the past performance of the Target Group’s operations and the future prospects of the Target Group’s business as represented by the Directors. As explained above, fiscal year 2001 was a poor year for the Target Group and the unaudited pro forma combined net profit after taxation and minority interests was approximately US\$27.5 million for the fiscal year ended 30 September 2001 as compared to US\$41.0 million for the fiscal year ended 30 September 2000. It is particularly noted in the Acquisition Agreement that the unaudited pro forma combined net profit after taxation and minority interests of the Target Group for the fiscal year ended 30 September 2002 used in the calculation of the aforesaid payment must relate only to those businesses and transactions of the companies which (i) are in the ordinary course of their respective businesses, (ii) are recurring in nature and (iii) do not include any notional adjustments relating to any income from new transactions arising between the Group, the Target Group and the PCC Group. Based on the Consideration, the Target Group is valued at earnings multiple (“PER”) of approximately 10.4 times and 15.5 times for the fiscal year ended 30 September 2000 and 2001 respectively.

LETTER FROM INDEPENDENT FINANCIAL ADVISER

We have reviewed the historical and current PER of certain comparable companies (the “Listed Comparables”) whose shares are listed either on Hong Kong Stock Exchange or Taiwan Stock Exchange and are shown in the following tabulation:

	Historical PER¹	Estimated PER^{1,2}	Year End
<i>Hong Kong</i>			
Yue Yuen Industrial (Holdings) Limited	9.6x	9.3x	30 Sept
Kingmaker Footwear Holdings Limited	11.8x	10.1x	31 Mar
Pegasus International Holdings Limited	10.8x	N/A ³	31 Dec
Sunny Global Holdings Limited	6.8x	N/A ³	30 Sept
Nority International Group Limited	9.2x	N/A ³	31 Dec
KTP Holdings Limited	4.1x	N/A ³	31 Mar
<i>Taiwan</i>			
Pou Chen Corporation	9.0x	10.3x	31 Dec
Feng Tay Enterprise Co Ltd	9.3x	N/A ³	31 Dec

Notes:

1. Based on the closing price of the Shares and the shares of the Listed Comparables as at the Latest Practicable Date.
2. Based on consensus net profit estimates for 2002 from the Institutional Brokers Earnings System earnings estimates. For Kingmaker Footwear Holdings Limited, the estimated PER is based on the net profit estimate for the year ending 31 March 2003.
3. N/A means not available.

(v) Payment Terms

The total consideration for the Acquisition is US\$427 million (approximately HK\$3,330.6 million), which shall be payable at Completion in the following manner:

- US\$186.8 million (approximately HK\$1,457.4 million) shall be satisfied by way of allotment and issue of 60 million Consideration Shares to Wealthplus (representing approximately 8.4 per cent. and approximately 7.8 per cent. of the Existing Capital and Enlarged Capital respectively) (credited as fully paid) at HK\$24.29 per Share.
- The price per Consideration Share is based on the average closing price of the 90 consecutive trading days before (and excluding) 16 September 2002, the date on which trading in the shares of the Company was suspended on the Hong Kong Stock Exchange pending the publication of the Announcement. The price per Consideration Share represents a premium of approximately 2.5 per cent. over the closing price of HK\$23.70 per Share as quoted on the Hong Kong Stock Exchange on 13 September 2002 (the last trading day preceding the day on which trading in the shares of the Company was suspended on the Hong Kong Stock Exchange pending the publication of the Announcement). In addition, the price per Consideration Share represents a premium of 7.0 per cent. over the closing price of HK\$22.70 per share on the Latest Practicable Date.

LETTER FROM INDEPENDENT FINANCIAL ADVISER

- The price per Consideration Share was arrived at based on arm's length negotiations and the price being acceptable to both the Company and the Vendors.
- US\$240.2 million (approximately HK\$1,873.2 million) shall be payable in cash.
- It is noted that the Vendors and PCC undertake to the Company not to sell, and shall procure that members of the PCC Group shall not sell, any Shares (including the Consideration Shares) nor shall they dispose of interest in such Shares through the grant of options, warrants, equity related instruments or otherwise for a period of 6 full calendar months from the date of Completion.

The payment as a result of any shortfall or excess to the Guaranteed Profits as mentioned in (iv) above shall be settled within 30 days after the availability of the audited pro forma closing accounts in respect of the Target Group for the fiscal year ended 30 September 2002.

(vi) Financing of the Acquisition

The sum of US\$186.8 million (approximately HK\$1,457.4 million) payable is to be satisfied by the issue and allotment to Wealthplus of the Consideration Shares.

The sum of US\$240.2 million (approximately HK\$1,873.2 million) payable is to be satisfied by payment in cash which is to be financed by existing financing facilities, new bank loans and the Group's cash holdings. As at 31 March 2002, the Group had unaudited cash and bank balances amounting to approximately US\$182.8 million. The Directors have confirmed that the Group has sufficient cash resources to meet such cash consideration.

(vii) Financial Effects of the Acquisition

- *Earnings*

The Acquisition is expected to increase the Group's revenue and earnings base. For the nine month period ended 30 June 2002, the Target Subsidiaries achieved unaudited pro forma combined turnover of approximately US\$244.2 million (approximately HK\$1,904.8 million) and unaudited net profit before taxation and minority interests of US\$35.5 million (approximately HK\$276.9 million) respectively. The financial results of the Target Group are expected to make additional financial contributions to the Group.

LETTER FROM INDEPENDENT FINANCIAL ADVISER

For illustration purposes, we have further conducted an analysis which gives an indication of the impact on earnings per share of the Company as a result of the Acquisition.

	For the year ended 30 September 2002	
	<i>US\$'million</i>	<i>HK\$'million⁷</i>
Estimated Net Profit of Yue Yuen ¹	222.7	1,737.0
Estimated Net Profit of the Target Group ²	44.6	347.9
Consolidated Net Profit of the Group before consolidation adjustments	267.3	2,084.9
Consolidation Adjustments:		
Goodwill ³	-12.9	-100.6
Interest Expense (after-tax) ⁴	-5.4	-42.1
Total Consolidation Adjustments	-18.3	-142.7
Consolidated Net Profit of the Group after consolidation adjustments	249.0	1,942.2
Pro forma EPS ⁵	0.3225	2.5152
Standalone EPS ⁶	0.3127	2.4390
Enhancement	3.1%	3.1%

Note:

1. Source: The Institutional Brokers Earnings System earnings estimates. The unaudited net profit of the Company for the 6 month period ended 31 March 2002 represents approximately 50% of this estimate.
2. Based on the Guaranteed Profits of US\$44.6 million.
3. Based on the net book value of US\$169.92 million as at 30 September 2001, the consideration of US\$427 million and an amortization period of 20 years.
4. Based on a tax rate of 16% and an effective interest rate of the London Inter-bank offer rate (12 months) of approximately 1.7% as at the Latest Practicable Date plus a spread of 100 basis points per annum on the cash consideration of US\$240.2 million.
5. Based on 772.18 million shares.
6. Based on 712.18 million shares.
7. Based on an exchange rate of US\$1 : HK\$7.8.

- *Shareholders' equity*

As a result of the issue of the Consideration Shares, which represent approximately 8.4 per cent. and approximately 7.8 per cent. of the Existing Capital and Enlarged Capital respectively, the Company's shareholders' equity is expected to increase by approximately US\$186.8 million (approximately HK\$1,457.4 million), which represents approximately 16.0 per cent. increase from the Group's unaudited shareholders' equity of US\$1,171 million as at 31 March 2002.

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- *Gearing*

It is expected that the Group will settle the cash portion of the Consideration by utilising its existing financing facilities, new bank loans and cash holdings. After Completion, based on the Group's net debt of approximately US\$224.8 million (approximately HK\$1,753.4 million) as at 31 March 2002 and taking into account the settlement of the Consideration only, it is expected that the net debt will increase to approximately US\$467.5 million (approximately HK\$3,646.5 million), and the net debt to equity ratio will increase from 19.2 per cent. to 34.4 per cent..

(viii) Non-competition Undertaking

PCC undertakes in the Acquisition Agreement that it will not, and will procure that each member of the PCC Group will not:

- a. while PCC remains directly or indirectly interested in 10 per cent. or more of the share capital of the Company then in issue; and
- b. for a period of three years after it ceases to be directly or indirectly interested in 10 per cent. or more of the share capital of the Company then in issue directly or indirectly,

be engaged or interested in any capacity (whether for reward or otherwise) in any business (other than through the Company) which is engaged in the production on a commercial scale of raw materials, components, machinery, moulds and tools for shoes outside Taiwan and in such places where the Purchaser and its Associates has operations and/or sales.

However, the Acquisition Agreement shall not prevent, or be breached by, the holding of an equity interest in any body corporate which does not exceed 10 per cent. of the entire equity interests in that body corporate and where such interest does not give PCC Group effective control of the relevant body corporate.

(ix) Guarantee Indemnity

The PCC Group has also provided guarantees to banks in respect of borrowings by members of the Target Group. It is noted that the guarantees to banks were provided upon normal commercial terms. The Company has agreed to use its reasonable endeavours to release and/or replace these guarantees within one month after Completion. As far as the Directors are aware, they do not foresee any reason which will act as an impediment to the release and/or replacement of such guarantees within this period.

In the interim, pending such release and/or replacement, the Company has agreed to indemnify the relevant member of the PCC Group in the event that any of the guarantees they have provided are called upon after Completion. Save for the abovementioned guarantees, the indemnity does not cover any liability arising out of any other guarantees whether provided by or in favour of any member of the PCC Group. The total amount secured by such guarantees is US\$37.4 million (approximately HK\$291.7 million) at varying percentage spreads above local borrowing rates. US\$17.5 million (approximately HK\$136.5 million) of the guaranteed amount is given in favour of members of the Target Group that will become non-wholly owned subsidiaries or associated companies. Approximately US\$12.8 million

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(approximately HK\$99.8 million) of the borrowings secured by the guarantees has been utilised. It is noted particularly that this indemnity, as with other terms of the Acquisition Agreement, is a result of arm's length negotiation between the parties to the Acquisition Agreement.

If the abovementioned guarantees of US\$37.4 million cannot be released or replaced on or before Completion, they will constitute connected transactions, which are exempted from further disclosure or shareholder approval under rule 14.24(8) of the Hong Kong Listing Rules. The related indemnity given under the Acquisition Agreement will also, after Completion, constitute connected transactions under rule 14.26(7) of the Hong Kong Listing Rules. Taking into account the Company's maximum liability of US\$37.4 million plus any accrued interests, this maximum liability represents an amount higher than 3 per cent. of the Company's consolidated net tangible assets as at the fiscal year ended 30 September 2001 or HK\$10 million.

(x) Conditions Precedent

Completion is subject to and conditional upon, among other things, the satisfaction of the following conditions:

- a. the passing of resolution(s) by the Independent Shareholders at a general meeting of the Company approving the Acquisition Agreement (including the Consideration Shares to be allotted and issued thereunder) to the extent required under the Hong Kong Listing Rules;
- b. the Company having been granted approval by the Listing Committee of the Hong Kong Stock Exchange for the listing of and permission to deal in the Consideration Shares to be issued;
- c. the approval, if necessary, by the Bermuda Monetary Authority, of the proposed allotment and issue of all of the Consideration Shares and the consent or approval of any other relevant regulatory authority in Bermuda in relation to such allotment and issue;
- d. in respect of the Vendors, all consents and approvals of any relevant governmental authorities or other relevant third parties in Hong Kong, Taiwan or elsewhere which are required or appropriate for the entry into and the implementation of the Acquisition Agreement having been obtained, including all filings with any relevant governmental authorities or other relevant third parties;
- e. save and except for trade receivables and payables between the Target Companies and the PCC Group which fall within the scope of the terms of the Existing Waiver in connection with the Services Agreement, all amounts due to and from any of the Target Companies to other members of the PCC Group are settled;
- f. there being no material breach of the representations, warranties, undertakings and indemnities given pursuant to the Acquisition Agreement; and

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- g. confirmation by the Executive that the issue of the Consideration Shares to Wealthplus will not give rise to a mandatory general offer obligation under the Takeovers Code or, alternatively, a waiver is granted by the Executive in respect of such obligation.

OPINION

Having taken the above principal factors and reasons into account, we consider the terms of the Acquisition Agreement are fair and reasonable so far as the Independent Shareholders as a whole are concerned. Accordingly, we advise the Independent Board Committee to recommend to the Independent Shareholders to vote in favour of the respective resolution to be proposed at the Special General Meeting to approve the Acquisition Agreement.

Yours faithfully,
For and on behalf of
The Hongkong and Shanghai Banking Corporation Limited
Herbert L. W. Hui
Corporate Finance Director – China
Investment Banking

眾信聯合會計師事務所
台北市光復南路 102 號 7 樓(華視大樓)

Deloitte & Touche
7th Floor, 102, Kuang Fu South Road,
Taipei, Taiwan, R.O.C.

**Deloitte
& Touche**

8 October 2002

To the Board of Directors
Yue Yuen Industrial (Holdings) Limited
7th Floor, Blocks A-D
Hop Hing Industrial Building
702 Castle Peak Road
Kowloon, Hong Kong

Dear Sirs,

We set out below the pro forma combined balance sheets as of 30 September 2000 and 2001 and 30 June 2002 (“Pro forma Combined Balance Sheets”), and the pro forma combined income statements for the years ended 30 September 2000 and 2001 and the nine month period ended 30 June 2002 (the “Relevant Periods”) (“Pro forma Combined Income Statements”, together with the Pro forma Combined Balance Sheets referred to as “Pro forma Combined Financial Statements”) of the target companies (hereinafter collectively referred to as the “Companies”), which Yue Yuen Industrial (Holdings) Limited (“Yue Yuen”) plans to acquire from the subsidiaries of Pou Chen Corporation (hereinafter collectively referred to as the “PCC Group”).

The Pro forma Combined Financial Statements have been prepared in accordance with the bases and assumptions as set out in Section 1 below. It is the sole responsibility of the management of the PCC Group to prepare the Pro forma Combined Balance Sheets and Pro forma Combined Income Statements. Our responsibility is to form an opinion on the Pro forma Combined Financial Statements for the Relevant Periods and report our opinion to you.

We conducted our work by independent examination of the underlying financial information of the Companies to assess whether accounting policies have been consistently applied and make inquiries of management of the PCC Group.

In our opinion, on the basis of presentation set out in Section 1 below, the Pro forma Combined Balance Sheets and the Pro forma Combined Income Statements for the Relevant Periods have truly and fairly presented its financial position and results. In addition, we are not aware of any material adjustments that are required to be made to the results as presented.

1. BASIS OF PRESENTATION

Except for the treatment of the disposal of 1.24% equity interest of Bigfoot Limited in March 2002 and the acquisition of 50% equity interest of Prime Asia Leather Corporation in February 2002, which is accounted for assuming the latest shareholding interests of Bigfoot Limited and Prime Asia Leather Corporation throughout the Relevant Periods presented, the Pro forma Combined Financial Statements are prepared in accordance with Accounting Principles Generally Accepted in Hong Kong, and assuming that the existing group structure had been in existence since the beginning of the Relevant Periods.

The Pro forma Combined Financial Statements are not itself audited but the financial statements of the individual companies are themselves individually audited or reviewed for each of the two years ended 30 September 2001. For the purpose of this report, we have reviewed the management accounts of the individual companies for the nine month period ended 30 June 2002.

All significant inter-company transactions and balances have been eliminated upon combination.

At the date of this report, the particulars of the Companies are set out below:

No.	Company Name	Place of Incorporation	Shareholding (%)	Business
Subsidiaries				
<i>Raw Materials</i>				
1	Pou Chien Chemical Company Limited	Taiwan	99.94%	Manufacturing of shoe materials (chemical products)
<i>Production Tools</i>				
2	Forearn Company Ltd.	BVI	100%	Manufacturing of shoe moulds
3	Golden Chain Developments Limited	BVI	80%	Manufacturing of cutting moulds
4	Multiform Enterprises Limited	BVI	100%	Moulding equipment
5	Octavia Developments Limited	BVI	51%	Ventilation slots
6	PT. Suksespermatama Indonesia	Indonesia	90%	Manufacturing of mould & cutting for shoes
7	Veeragoo Trading Limited	BVI	100%	Inactive
<i>Shoe Components</i>				
8	Bestful Properties Limited	BVI	100%	Property investment – leases Huangjiang factory to Prime Asia
9	Escon Enterprises Limited	BVI	100%	Leases machinery, equipment to Prime Asia, provision of sub-contracting services for manufacturing of leather
10	Essington Developments Limited	BVI	55%	Manufacturing of shoe counters
11	Fu Tai Company Limited	BVI	100%	Manufacturing of shoe moulds and EVA midsole for shoes

No.	Company Name	Place of Incorporation	Shareholding (%)	Business
12	Chang Yang Vietnam Limited	Vietnam	51%	Plastic shoe materials injection
13	Overboard Investments Limited	BVI	100%	Shoe pads
14	Pou Ming Paper Products Manufacturing Company Limited	BVI	100%	Production of paper carton boxes and investment holding company
15	PT. Citra Cikande	Indonesia	51%	Manufacturing of insole for shoe counters
16	PT. Variadhana Citraselaras	Indonesia	55%	Manufacturing of injection moulds for shoe components
17	Dah-Chen Shoe Materials Ltd.	Vietnam	51%	Shoe pads, reprinting, etc
18	Upturn Investments Limited	BVI	100%	Manufacturing of paper inner boxes and carton boxes
19	Chiya Vietnam Enterprise Limited	Vietnam	51%	Foamed cotton
20	Super Foam Vietnam Enterprise Limited	Vietnam	51%	Foamed cotton
21	Wellspeed Trading Limited	BVI	100%	Manufacturing of counter and oil bladder for shoes
22	Prime Asia Upper Company Limited	BVI	100%	Inactive
23	Optima Worldwide Corporation	BVI	100%	Provision of administration services to Prime Asia
24	Optima Worldwide Services Company Limited	Macau	100%	Provision of administration services to Prime Asia
25	Prime Asia China Leather Corporation	BVI	100%	Leather Trading
26	Prime Asia Leather Corporation, Taiwan Branch	Taiwan	100%	Leather Trading
27	Prime Asia (S.E. Asia) Leather Corporation	BVI	100%	Provision of administration services to Prime Asia
28	Wet Blue International Corporation	BVI	100%	Wet blue trading

Investment Holding Companies

29	High Shine Investments Limited	BVI	51%	Investment holding company
30	Top Units Developments Limited	BVI	51%	Investment holding company
31	Valuable Developments Limited	BVI	51%	Investment holding company
32	Aimful Investments Limited	BVI	51%	Investment holding company
33	Bond Ocean Investments Limited	BVI	51%	Investment holding company
34	Bortum Holdings Limited	BVI	100%	Investment holding company
35	Champolian Investments Inc.	BVI	100%	Investment holding company
36	Ettalon Investments Limited	BVI	100%	Investment holding company
37	Farquharson Holdings Corp.	BVI	100%	Investment holding company
38	Giacinto Investments Limited	BVI	100%	Investment holding company
39	Glenhurst Trading Limited	BVI	100%	Investment holding company
40	Murata Profits Limited	BVI	100%	Investment holding company
41	Patterns Developments Limited	BVI	100%	Investment holding company
42	Pou Chien Chemical (Holdings) Limited	BVI	100%	Investment holding company
43	Stencil International Limited	BVI	100%	Investment holding company
44	World Street Investments Limited	BVI	55%	Investment holding company
45	Prime Asia Leather Corporation	BVI	100%	Investment holding company

No.	Company Name	Place of Incorporation	Shareholding (%)	Business
Jointly Controlled Entities				
<i>Production Tools</i>				
46	High Style Investments Limited	BVI	50%	High frequency, CNC, screen printing and spraying
<i>Shoe Components</i>				
47	Blessland Enterprises Limited	BVI	50%	Shoe pads
48	Cohen Enterprises Inc.	BVI	50%	Manufacturing of leather products for shoes
49	Topmost Industries Limited	BVI	50%	Manufacturing of counters for shoes
50	Twinways Investments Limited	BVI	50%	Manufacturing of injection moulds for shoe components
Associates				
<i>Raw Materials</i>				
51	Nan Pao Resins (China) Co., Ltd.	PRC	37%	Glues/liquid coatings/powder coatings
52	Credition International Group Limited	BVI	35%	PU Plastic/hardeners/processing agents/lotion plaster/powder coatings
53	Eastlion Industrial Ltd.	BVI	35%	PU Plastic/hardeners/processing agents/lotion plaster/powder coatings
54	Eastlion Enterprises Ltd.	BVI	35%	Property investments provision for Nan Pao Resins (Holdings) Ltd.
55	Nan Pao Resins (Vietnam) Enterprise Limited	Vietnam	37%	Liquid coating/glues
<i>Production Tools</i>				
56	Original Designs Developments Limited	BVI	47%	Shoe lasts

No.	Company Name	Place of Incorporation	Shareholding (%)	Business
<i>Shoe Components</i>				
57	Enthroned Group Limited	BVI	48.76%	Inactive
58	Bigfoot Limited	BVI	48.76%	Cloth product trading/cloth dyeing & processing/cloth shoe material binding
58	Platinum Long John Company Limited	Taiwan	48.76%	Cloth product trading/cloth dyeing & processing/cloth shoe material binding
60	Chifley Tower Limited	BVI	40%	Trademark
61	Natural Options Limited	BVI	38.3%	Foamed cotton
62	Just Lucky Investments Limited	BVI	38.3%	Provision of real estate leasing for the operation of Natural Options Ltd.
63	Nice Pearl Enterprises Limited	BVI	35%	Investment in land, factory and various equipments
<i>Investment Holdings Company</i>				
64	All Saints Enterprises Limited	BVI	37%	Investment holding company
65	Nan Pao Resins (Holdings) Limited	BVI	35%	Investment holding company
66	Rising Sun Associates Limited	BVI	37%	Investment holding company
Investment Securities				
67	Precise Zone Investments Limited	BVI	17.65%	Provision of electroplating services

2. PRO FORMA COMBINED INCOME STATEMENTS

(Expressed in US Dollars)

		Year ended 30 September		9 month period ended 30 June 2002
		2000	2001	(Unaudited)
	<i>Note</i>			
Turnover	(1)	293,785,108	311,942,965	244,229,980
Cost of Sales		<u>(226,293,073)</u>	<u>(243,914,659)</u>	<u>(186,205,180)</u>
Gross Profit		67,492,035	68,028,306	58,024,800
Other Revenue		11,381,723	6,466,593	4,172,553
Selling and Distribution Expenses		(7,748,502)	(10,536,655)	(8,050,864)
Administrative Expenses		(28,620,879)	(33,605,188)	(24,163,858)
Other Operating Expenses		<u>(4,512,542)</u>	<u>(4,313,468)</u>	<u>(1,436,228)</u>
Profit from Operations		37,991,835	26,039,588	28,546,403
Finance Costs		(836,477)	(644,768)	(44,154)
Share of Results of Associates	(2)	2,963,437	2,608,257	3,578,709
Share of Results of Jointly Controlled Entities	(3)	<u>1,136,383</u>	<u>1,830,690</u>	<u>3,457,575</u>
Profit Before Taxation		41,255,178	29,833,767	35,538,533
Income Tax Benefit (Expense)		<u>87,812</u>	<u>(940,768)</u>	<u>235,718</u>
Profit Before Minority Interests		41,342,990	28,892,999	35,774,251
Minority Interests		<u>(359,897)</u>	<u>(1,384,357)</u>	<u>(1,587,188)</u>
Net Profit for the Year/Period	(4)	40,983,093	27,508,642	34,187,063
Dividends		<u>–</u>	<u>–</u>	<u>–</u>
Profit for the Year/Period Retained		<u><u>40,983,093</u></u>	<u><u>27,508,642</u></u>	<u><u>34,187,063</u></u>

Notes to the Pro forma Combined Income Statements:*(Expressed in US Dollars)***(1) Turnover**

	Year ended 30 September		9 month period ended 30 June 2002
	2000	2001	<i>(Unaudited)</i>
Raw materials	14,658,171	12,863,893	8,151,762
Production tools	32,555,974	35,216,639	24,449,739
Shoe components	246,570,963	263,862,433	211,628,479
Total	<u>293,785,108</u>	<u>311,942,965</u>	<u>244,229,980</u>
Outsiders	166,706,025	175,888,706	138,789,503
Related companies	127,079,083	136,054,259	105,440,477
Total	<u>293,785,108</u>	<u>311,942,965</u>	<u>244,229,980</u>

(2) Share of Results of Associates

	Year ended 30 September		9 month period ended 30 June 2002
	2000	2001	<i>(Unaudited)</i>
Raw materials	1,324,224	674,500	1,614,256
Production tools	762,497	602,173	665,893
Shoe components	876,716	1,331,584	1,298,560
Total	<u>2,963,437</u>	<u>2,608,257</u>	<u>3,578,709</u>

(3) Share of Results of Jointly Controlled Entities

	Year ended 30 September		9 month period ended 30 June 2002
	2000	2001	<i>(Unaudited)</i>
Production tools	–	(30,553)	119,418
Shoe components	1,136,383	1,861,243	3,338,157
Total	<u>1,136,383</u>	<u>1,830,690</u>	<u>3,457,575</u>

(4) Net Profit

	Year ended 30 September		9 month period ended 30 June 2002
	2000	2001	<i>(Unaudited)</i>
Raw materials	511,705	1,927,536	2,342,350
Production tools	8,716,852	5,045,393	2,980,473
Shoe components	31,754,536	20,535,713	28,864,240
Total	<u>40,983,093</u>	<u>27,508,642</u>	<u>34,187,063</u>

3. PRO FORMA COMBINED BALANCE SHEETS

(Expressed in US Dollars)

		30 September		30 June 2002
		2000	2001	(Unaudited)
	Note			
Non-current Assets				
Goodwill		233,486	208,471	197,726
Property, Plant and Equipment	(1)	63,520,139	64,731,691	63,400,775
Interests in Associates	(2)	19,890,702	20,027,862	22,085,891
Interests in Jointly Controlled Entities	(3)	12,018,751	16,086,490	18,074,673
Investment Securities		1,158,426	1,048,812	1,663,961
		<u>96,821,504</u>	<u>102,103,326</u>	<u>105,423,026</u>
Current Assets				
Inventories	(4)	50,628,473	52,546,176	55,756,760
Accounts Receivable		25,986,357	27,682,812	37,496,959
Prepayments & Other Receivables		6,222,689	8,589,580	8,054,234
Amounts Due from Associates		35,878	48,414	36,030
Amounts Due from Jointly Controlled Entities		403,639	114,473	256,061
Amounts Due from Related Companies		34,288,918	28,547,621	37,059,381
Other Investments		849,378	0	688,417
Bank Balances and Cash		11,894,412	19,547,393	19,419,229
		<u>130,309,744</u>	<u>137,076,469</u>	<u>158,767,071</u>
Current Liabilities				
Accounts Payable		9,123,254	10,226,834	13,134,082
Taxation Payables		2,952	5,209	67,026
Other Payables		9,505,585	10,480,044	11,540,900
Amounts Due to Associates		34,729	58,467	58,931
Amounts Due to Jointly Controlled Entities		17,353	79,893	50,624
Amounts Due to Related Companies		25,669,021	41,226,492	37,047,370
Short-term Bank & Other Borrowings		6,509,878	2,407,141	2,688,523
		<u>50,862,772</u>	<u>64,484,080</u>	<u>64,587,456</u>
Net Current Assets		<u>79,446,972</u>	<u>72,592,389</u>	<u>94,179,615</u>
Total Assets Less Current Liabilities		176,268,476	174,695,715	199,602,641
Minority Interests		3,458,118	4,771,709	5,128,938
Net Assets		<u>172,810,358</u>	<u>169,924,006</u>	<u>194,473,703</u>

Notes to the Pro forma Combined Balance Sheets:
(Expressed in US Dollars)

(1) Property, Plant and Equipment

	30 September		30 June 2002 (Unaudited)
	2000	2001	
Leasehold Improvement	6,207,875	5,972,924	5,124,520
Land and Building	10,941,399	12,223,523	11,904,553
Machinery	43,018,510	43,368,923	43,597,178
Transportation and Motor Vehicles	773,906	837,949	671,978
Furniture Fixture	1,942,928	1,810,863	1,226,127
Other Equipment	635,521	517,509	876,419
Total	<u>63,520,139</u>	<u>64,731,691</u>	<u>63,400,775</u>

(2) Interests in Associates

	30 September		30 June 2002 (Unaudited)
	2000	2001	
Raw materials	8,914,996	8,873,367	9,980,116
Production tools	2,116,840	2,202,952	2,313,776
Shoe components	8,858,866	8,951,543	9,791,999
Total	<u>19,890,702</u>	<u>20,027,862</u>	<u>22,085,891</u>

(3) Interests in Jointly Controlled Entities

	30 September		30 June 2002 (Unaudited)
	2000	2001	
Production tools	–	769,447	888,865
Shoe components	12,018,751	15,317,043	17,185,808
Total	<u>12,018,751</u>	<u>16,086,490</u>	<u>18,074,673</u>

(4) Inventories

	30 September		30 June 2002 (Unaudited)
	2000	2001	
Raw Materials and supplies	46,936,394	49,381,804	51,175,941
Work in Progress	1,129,917	1,267,015	1,739,982
Finished Goods	2,216,205	2,017,812	2,644,270
Goods in Transit	499,568	105,044	428,976
Less: allowance	(153,611)	(225,499)	(232,409)
Net	<u>50,628,473</u>	<u>52,546,176</u>	<u>55,756,760</u>

Yours truly,
Deloitte & Touche
Certified Public Accountants
Taiwan

1. RESPONSIBILITY STATEMENT

This circular includes particulars given in compliance with the Hong Kong Listing Rules for the purpose of giving information with regard to the Company. 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 the omission of which would make any statement herein misleading.

2. MATERIAL CHANGES

As at the Latest Practicable Date, save as disclosed herein, there has been no material adverse change in the financial or trading position of the Company and its subsidiaries since 30 September 2001, being the date of the latest published audited accounts of the Group.

3. DISCLOSURE OF INTERESTS BY DIRECTORS

As at the Latest Practicable Date, the following Directors were interested in the following Shares or securities of the Company or any of its associated corporations (within the meaning of the Securities (Disclosure of Interests) Ordinance (“SDI Ordinance”)) which were required to be notified to the Company and the Hong Kong Stock Exchange pursuant to section 28 of the SDI Ordinance (including interests which they were taken or deemed to have taken under section 31 of, or Part I of the Schedule to, the SDI Ordinance) or which were required, pursuant to section 29 of the SDI Ordinance, to be entered in the register referred to therein or which were required to be notified to the Company and the Hong Kong Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of the Listed Companies:—

Name of Director	Personal interest	Family interest	Number of Shares held		Number of share options
			Corporate interest	Other interest	
Tsai Chi Neng	–	–	–	–	–
David N.F. Tsai	–	–	–	–	6,000,000 (b)
Li I Nan, Steve	–	–	–	–	1,466,666 (c)
Kung Sung Yen	–	–	–	–	2,500,000 (b)
Lu Chin Chu	–	–	–	–	2,500,000 (b)
Kuo Tai Yu	–	–	–	–	2,500,000 (b)
Edward Y. Ku	–	–	–	–	–
Chan Lu Min	100,000	–	–	–	–
Choi Kwok Keung	–	–	–	21,020,560 (a)	–
Shih Hung	–	–	–	–	–
John J.D. Sy	–	–	–	–	–

Notes:

- (a) 15,180,000, 2,920,280 and 2,920,280 Shares of the Company were held by Hearty Choice Limited, Golden Path Company Limited and Grand Scope Company Limited respectively, all of which were ultimately held by HSBC International Trustee Limited as trustee for a discretionary trust. The discretionary objects of the trust include children of Mr Choi Kwok Keung.
- (b) Pursuant to the Company’s share option scheme, the share options were granted on 12 December 1996 to subscribe for Shares at a subscription price of HK\$10.22 per Share.
- (c) Pursuant to the Company’s share option scheme, the share options were granted on 28 April 1993 to subscribe for Shares at a subscription price of HK\$6.35 per Share.

No Directors or proposed Directors or experts (as named below) has any interest, direct or indirect, in any assets which have been, since 30 September 2001, the date to which the latest published audited accounts of the Company were made up, acquired or disposed of by or leased to any member of the Group, or are proposed to be acquired or disposed of by or leased to any member of the Group.

4. SUBSTANTIAL SHAREHOLDERS

As at the Latest Practicable Date, the following persons and corporations (other than the Directors or chief executive of the Company) were, so far as is known to the Directors, directly or indirectly, interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of the Company in respect of such capital:

Name of Shareholder	<i>Notes</i>	Number of ordinary shares beneficiary held
PCC	<i>(a)</i>	292,240,350
Wealthplus	<i>(a)</i>	266,231,581
Max Creation Industrial Limited	<i>(b)</i>	174,682,750
Quicksilver Profits Limited (“Quicksilver”)	<i>(b)</i>	89,747,411
Red Hot Investments Limited (“Red Hot”)	<i>(b)</i>	76,233,720
World Future Investments Limited	<i>(c)</i>	174,682,750
Mr Tsai Chi Jui	<i>(c)</i>	174,682,750

Notes:

- (a) Of the 292,240,350 Shares beneficiary owned by PCC, 266,231,581 Shares were held by Wealthplus as listed above, 23,911,169 Shares were held by Win Fortune and 2,097,600 Shares were held by Top Score. Both Wealthplus and Win Fortune are wholly-owned subsidiaries of PCC and Top Score is a 97.63% owned subsidiary of PCC.
- (b) Of the 174,682,750 Shares beneficiary owned by Max Creation, 89,747,411 Shares were held by Quicksilver, 76,233,720 Shares were held by Red Hot (both listed above) and 8,701,619 Shares were held by Moby Dick Enterprises Limited (“Moby Dick”). Quicksilver, Red Hot and Moby Dick are wholly owned subsidiaries of Max Creation.
- (c) World Future is deemed to be interested in 174,682,750 Shares under section 8(3) of the SDI ordinance by virtue of its interest in more than one third of the voting shares in Max Creation. Mr Tsai Chi Jui is also deemed to be interested in 174,682,750 Shares under the same section as he holds 100% of the issued share capital in World Future.

5. SERVICE CONTRACTS

There are no service contracts between any Directors of the Company and any member of the Group, excluding those expiring or determinable by the employer within one year without payment of compensation (other than statutory compensation).

6. CONSENTS

HSBC and Deloitte & Touche, Taiwan, have given and have not withdrawn their written consents to the issue of this circular with the inclusion herein of their names, letters and reports in the form and context in which they respectively appear.

7. QUALIFICATIONS OF EXPERTS

The following are the qualifications of the experts who have given their opinions or advice which are contained in this circular:–

Name	Qualification
HSBC	An exempt dealer and an investment adviser registered under the Securities Ordinance (Chapter 333 of the Laws of Hong Kong) and a licensed bank under the Banking Ordinance 1 Chapter 155 of the Laws of Hong Kong
Deloitte & Touche, Taiwan	Certified Public Accountants, Taiwan

Neither of the experts has any shareholding in any member of the 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 Group. From time to time, HSBC provides banking services to the Group but is not the Group's main banker.

8. LITIGATION

No member of the Group is engaged in any litigation or arbitration of material importance and the Directors are not aware of any litigation or claim of material importance pending or threatened by or against any member of the Group.

9. MISCELLANEOUS

- (a) The secretary of the Company is Danny C.W. Lam, *ACS, ACIS*.
- (b) The share registrars of the Company are Secretaries Limited, 5th Floor, Wing On Centre, 111 Connaught Road Central, Hong Kong.
- (c) The English text of this circular and form of proxy shall prevail over the Chinese text.

10. DOCUMENT AVAILABLE FOR INSPECTION

Copies of the following documents are available for inspection during normal business hours on any weekday (public holidays excepted) at the office of Richards Butler at 20th Floor, Alexandra House, 16-20 Chater Road, Hong Kong up to and including the date of the Special General Meeting:

- (a) the Memorandum and Bye-laws of the Company;
- (b) the audited consolidated accounts of the Company for the fiscal years ended 30 September 2001 and 2000;
- (c) the letter from the Independent Board Committee;

- (d) the letter from HSBC, the text of which is set out on pages 36 to 45 of this circular;
- (e) the unaudited pro forma combined financial information on the Target Group;
- (f) the Acquisition Agreement;
- (g) the Pou Chien Lease;
- (h) the Pou Yuen Lease; and
- (i) the Production Agreement.

NOTICE OF SPECIAL GENERAL MEETING



YUE YUEN INDUSTRIAL (HOLDINGS) LIMITED (裕元工業(集團)有限公司)

(incorporated in Bermuda with limited liability)

SPECIAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that a special general meeting (the “Special General Meeting”) of Yue Yuen Industrial (Holdings) Limited (the “Company”) will be held at Sung Room I, 4th Floor, Sheraton Hong Kong Hotel and Towers, 20 Nathan Road, Kowloon, Hong Kong on 29 October 2002 at 10:30 a.m. for the purpose of considering and, if thought fit, passing the following resolutions.

1. “**THAT**:-

- (a) the agreement dated 16 September 2002 (the “Acquisition Agreement”, a copy of which marked “A” and initialled by the chairman of the meeting will be available at the meeting for the purposes of identification) made between the Company as purchaser, Pou Chen Corporation as guarantor, Wealthplus Holdings Limited (“Wealthplus”), Kliene Developments Limited and Stable Future Trading Limited (together the “Vendors”) pursuant to which the Company agreed, among other things, to purchase or procure the purchase from the Vendors their respective interests in the companies referred to therein and the shareholders’ loans of an aggregate amount of US\$62,386,041 (“Shareholders’ Loans”) referred to therein for an aggregate consideration of US\$427 million (approximately HK\$3,330.6 million), US\$186.8 million (approximately HK\$1,457.4 million) of which would be satisfied by way of allotment and issue of 60 million shares of HK\$0.50 each of the Company (“Shares”) at HK\$24.29 each Share to Wealthplus, credited as fully paid, and US\$240.2 million (approximately HK\$1,873.2 million) of which would be satisfied by way of cash, be and is hereby approved and any one of the directors of the Company be and are hereby authorised to take such steps and/or execute (under seal if necessary) such documents as they shall in their absolute discretion consider desirable, necessary or expedient to effect the transactions contemplated thereunder; and
- (b) the allotment and issue of 60 million Shares at HK\$24.29 each Share, credited as fully paid, to Wealthplus be and is hereby approved.”

By order of the Board
Tsai Chi Neng
Chairman

Hong Kong, 8 October 2002

NOTICE OF SPECIAL GENERAL MEETING

Registered Office:

Clarendon House
Church Street
Hamilton HM11
Bermuda

Principal office in Hong Kong:

7th Floor, Blocks A-D
Hop Hing Industrial Building
702 Castle Peak Road
Kowloon, Hong Kong

Notes:

1. A form of proxy for use at the meeting is enclosed.
2. Any member entitled to attend and vote at a meeting of the Company shall be entitled to appoint another person as his proxy to attend and vote instead of him unless otherwise required by statutes. A proxy need not be a member. A member may appoint a proxy in respect of part only of his holding of shares in the Company.
3. The instrument appointing a proxy shall be in writing under the hand of the appointor or of his attorney duly authorised in writing or, if the appointor is a corporation, either under its seal or under the hand of an officer, attorney or other person authorised to sign the same. In the case of an instrument of proxy purporting to be signed on behalf of a corporation by an officer thereof it shall be assumed, unless the contrary appears, that such officer was duly authorised to sign such instrument of proxy on behalf of the corporation without further evidence of the fact.
4. The instrument appointing a proxy and (if required by the Board) the power of attorney or other authority (if any) under which it is signed, or a certified copy of such power or authority, shall be delivered to the Company's principal office in Hong Kong at 7th Floor, Blocks A-D, Hop Hing Industrial Building, 702 Castle Peak Road, Kowloon not less than forty-eight (48) hours before the time appointed for holding the meeting or adjourned meeting at which the person named in the instrument proposes to vote or, in the case of a poll taken subsequently to the date of a meeting.
5. In the case of joint holders of a share if more than one of such joint holders be present at any meeting, the vote of the senior who tenders a vote, whether in person or by proxy, shall be accepted to the exclusion of the votes of the other joint holders, and for this purpose seniority shall be determined by the order in which the names stand in the register of members of the Company in respect of the joint holding.