

BUSINESS OF THE GROUP

BUSINESS

The Group is principally engaged in the (i) distribution of passenger vehicles, in particular, BMW, Honda and Mercedes-Benz passenger vehicles to resellers in Hong Kong and the PRC whose sales targets are the end customers in the PRC, (ii) provision of marketing and technical assistance to North Anhua, a reseller and business alliance of the Group in the PRC, (iii) provision of after-sales service such as motor vehicles repair and maintenance services in the PRC and (iv) trading of auto parts and accessories in Hong Kong and the PRC. Headquartered in Singapore, the Group currently has presences in Hong Kong, Tianjin Municipality and the Xiamen Special Economic Zone of the PRC. For each of the two years ended 31st December, 2000 and 2001, total revenues generated by the Group are set out below:

	No. of motor vehicles		FY2000		No. of motor vehicles		FY2001	
			<i>HK\$'000</i>				<i>HK\$'000</i>	
Distribution of passenger vehicles	347	87,009	70%		701	218,786	86%	
Technical fee income		27,696	22%			20,413	8%	
Servicing passenger vehicles and sales of auto parts		10,270	8%			14,585	6%	
		<u>124,975</u>	<u>100%</u>			<u>253,784</u>	<u>100%</u>	

To complement the Group's motor vehicles distribution business, the Group has recently diversified into car rental business in the PRC. The Directors believe that car rental operators will enhance their service by employing imported luxury passenger vehicles supplied by the Group. The Group has entered into license agreements with Hertz as its principal licensee for using the Hertz System and has procured three sub-licensees for using the Hertz System. The PRC legal adviser of the Group has opined that the Group is entitled to operate, within the ambit of the PRC law, as a principal licensee for sub-licensing the Hertz System to local car rental business operators in the PRC. The Group also provides management consulting, financial assistance and technical expertise to these sub-licensees in the operation of their car rental business in the PRC.

1) Distribution of passenger vehicles

Product Coverage

The Group principally distributes imported BMW, Honda and other passenger vehicles, including Land Rover, Toyota and Mercedes-Benz to resellers in Hong Kong and the PRC whose sale targets are the end customers in the PRC.

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For each of the two years ended 31st December, 2000 and 2001, revenues generated from the Group's distribution of imported BMW, Honda, Land Rover, Toyota and Mercedes-Benz passenger vehicles are set out below:

	No. of motor vehicles	FY2000 <i>HK\$'000</i>		No. of motor vehicles	FY2001 <i>HK\$'000</i>	
BMW	103	35,565	41.0%	441	128,812	58.9%
Honda	187	24,911	28.6%	124	20,526	9.4%
Land Rover	2	389	0.4%	7	690	0.3%
Toyota	—	—	—	29	4,236	1.9%
Mercedes-Benz	55	26,144	30.0%	100	64,522	29.5%
	<u>347</u>	<u>87,009</u>	<u>100.0%</u>	<u>701</u>	<u>218,786</u>	<u>100.0%</u>

Below is a description of passenger vehicles distributed by the Group:

BMW passenger vehicles

BMW passenger vehicles can be divided into three broad categories: 3, 5 and 7 Series. The 5 and 7 Series BMW passenger vehicles are developed for passenger comfort, while the 3 Series BMW passenger vehicles which are designed for the younger generation are built with special emphasis on driving pleasure. The Group specialises in the distribution of 5 and 7 Series BMW passenger vehicles which are the most popular series of BMW passenger vehicles in the PRC. For each of the two years ended 31st December, 2000 and 2001, revenue generated from the Group's distribution of 3, 5 and 7 Series and X5 of BMW passenger vehicles are set out as follows:

	No. of motor vehicles	FY2000 <i>HK\$'000</i>		No. of motor vehicles	FY2001 <i>HK\$'000</i>	
3 Series	3	957	3%	72	13,881	11%
5 Series	47	12,726	36%	204	54,264	42%
7 Series	53	21,882	61%	135	49,491	38%
X5	—	—	—	30	11,176	9%
	<u>103</u>	<u>35,565</u>	<u>100%</u>	<u>441</u>	<u>128,812</u>	<u>100%</u>

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The Group secured the distributorship of BMW passenger vehicles and auto parts in Fujian Province in the PRC by entering into a yearly renewable non-exclusive BMW Importer Contract with BMW AG in December 1993. The BMW Importer Contract was renewed by BMW AG in 2002 for a term of one year from 1st January, 2002 to 31st December, 2002.

The Group has been expanding its business activities and has subsequently been distributing, i) other brands of automobiles and parts to resellers inside and outside the contract territory, Fujian Province, including Hong Kong and ii) BMW automobiles and parts to resellers who have not been authorised by BMW AG (collectively the “Activities”). **The Activities do not strictly comply with the terms and conditions of the BMW Importer Contract.** The Group has obtained the BMW Waiver Letters from the BMW Group acknowledging the Activities and waiving all the breaches in relation to the Activities under the BMW Importer Contract. Pursuant to the BMW Waiver Letters, the BMW Group confirmed with the Group that BMW AG will not impose any penalty as stipulated in the BMW Importer Contract now or in the future in respect of any breaches whether committed in the past or to be committed in the future, as the BMW Group has tolerated the Activities and will continue to tolerate the Activities in the future unless and until it notifies the Group in writing.

In addition, the Group has obtained legal opinions from its German legal adviser and its PRC legal adviser on the legal effects of the BMW Waiver Letters. According to the German and PRC legal opinions, the BMW Waiver Letters issued by the BMW Group are enforceable and legally binding on BMW AG. According to the German legal opinion dated 19th March, 2002, (i) BMW AG is aware of and has no objections to the Activities carried on and to be carried on by GAPL; (ii) BMW AG waived its contractual rights to impose any penalty stipulated in clause 1 of the BMW Importer Contract on GAPL now or in the future in respect of any breaches committed in the past or to be committed in the future; (iii) BMW AG waived its contractual right to bring any actions or make any claims against GAPL for any past and future breaches which are relevant and/or arising from the Activities; (iv) BMW AG waived its contractual right to terminate the BMW Importer Contract by reasons of the Activities; (v) the BMW AG Waiver Letters effectively authorised GAPL in carrying on the Activities unless and until otherwise notified by BMW AG in writing; and (vi) the BMW AG Waiver Letters are enforceable and legally binding on BMW AG. There are risks to the future business of the Group should BMW AG decide to notify the Group to terminate the Activities at any time in the future as it deems appropriate. Please refer to the paragraph headed “Breach of the BMW Importer Contract” under the section headed “Risk Factors” of this prospectus for further details.

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BMW AG has recently announced a preliminary plan to form a potential new joint venture in early 2003 with a PRC company in which each party shall have an equal interest for setting up a manufacturing plant in the PRC. It is intended that such joint venture company will initially produce 3 and 5 Series models of BMW passenger vehicles and such models will be excluded from the list of models to be supplied by BMW AG to the Group under the BMW Importer Contract once such production commences. However, BMW AG indicates to the Group that it will exercise its influence over the management of the joint venture company so that the Group will be offered a dealer license from such joint venture company and engage locally licensed resellers for distribution of locally manufactured BMW passenger vehicles. Nevertheless, Directors expect that the Group will still be able to import from Germany BMW passenger vehicles other than 3 and 5 Series models for import into the PRC after the establishment of such joint venture company. Please refer to the paragraph under “Manufacturing plant set up by BMW and other suppliers in the PRC” in the section headed “Risk Factors” of the prospectus for further details.

Honda passenger vehicles

The Group also became an importer of Honda motor vehicles for the PRC market in November 1995. The Group’s arrangement with Honda Motor Co., Ltd. is made on a case-by-case basis, that is, every order for Honda motor vehicles placed by the Group is negotiated with Honda Motor Co., Ltd. in the absence of any distribution agreement. No restriction as to the resellers and the territories to and in which Honda motor vehicles may be distributed by the Group has been imposed by Honda Motor Co., Ltd.. Honda provides different models of passenger vehicles under different sizes including Accord, Legend, Civic, Odyssey, CR-V, etc. Honda maintains a solid reputation of styling, performance, safety and value.

Land Rover passenger vehicles

In September 1997, the Group was appointed by Land Rover Group as its non-exclusive authorised distributor to distribute Land Rover passenger vehicles in Fujian Province. **The Group breaches the Land Rover distribution agreement by distributing Land Rover motor vehicles outside the contract territory of Fujian Province. However, Land Rover Group has unconditionally and irrevocably waived any past, present and future corresponding liabilities of the Group and allowed the Group to continue such distributing operations.**

The Land Rover brand name is perceived to be of high technical knowhow and luxury in the world. Accordingly, the Directors are confident that the Group will further benefit from the increasing sales of Land Rover motor vehicles in the PRC in the near future.

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Other passenger vehicles

Furthermore, the Group also distributes Toyota and Mercedes-Benz motor vehicles and the arrangements to distribute such motor vehicles are also made on a case-by-case basis.

Toyota is the largest car manufacturer in Japan and one of the largest in the world. Since its founding in the 1930's, Toyota's success has been built on a solid reputation for products of high quality, reliability and good resale value.

Mercedes-Benz commenced its production of motor vehicles in 1885. Mercedes-Benz provides wide range of vehicles models and is reputed for their performance, reliability and technological brilliance.

The Directors believe that one of the key factors to the rapid growth of the Group during the Track Record Period is the extensive distribution network of the passenger vehicles, in particular, BMW, Honda and Land Rover passenger vehicles in the PRC established by the Group's business partners. The Directors believe that the Group is able to enhance its business relationship with its major customers by providing quality pre-sales and after-sales services. Repeated orders from these customers are another key factor to the growth of the Group.

The Directors also believe that given the popular brand name and proven quality of BMW, Honda and Land Rover passenger vehicles auto parts, accessories and other products, the Group is well-positioned to benefit from the expected future growth in demand for luxury and mid-market vehicles in the PRC where the number of private enterprises and individual disposable income are expected to continue to increase, especially after the PRC's accession to the WTO.

Distribution Mechanism

The Group mainly distributes imported passenger vehicles to (i) resellers in Hong Kong and (ii) resellers in the PRC whose sales targets are the end customers in the PRC. The supply chain for distribution of passenger vehicles in the PRC involves multiple layers. The Group has diverse alternatives and options in structuring reseller networks for distributing passenger vehicles in the PRC. The distribution of passenger vehicles to Hong Kong resellers, whose sales targets are the end customers in the PRC, is just one of the many distribution and revenue contribution methods currently operated by the Group. The Group also imports passenger vehicles to PRC resellers, and CNA Anhua (Tianjin) also directly import and distribute passenger vehicles to end customers in Tianjin Free Trade Zone of the PRC. The Directors believe that it is to the benefit of the Group to implement all profitable and legally permissible distribution mechanism of passenger vehicles.

The sales derived from distribution of passenger vehicles to resellers in Hong Kong and the PRC accounted for approximately 70.4% and 29.6%, 61.3% and 38.5% respectively of the Group's revenue generated from motor vehicle distribution for each of the two years ended 31st December, 2000 and 2001 respectively.

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GAL, a Hong Kong wholly-owned subsidiary of the Company, acts as the centre for distributing passenger vehicles for the Group. The imported motor vehicles are initially delivered to GAL. GAL then distributes the same either to its resellers in the PRC or its resellers in Hong Kong for sale to resellers in the PRC for further distribution to end customers in the PRC. No custom duties are levied on imports and exports of motor vehicles in Hong Kong. In addition, since the imported motor vehicles of the Group are not for use in Hong Kong, the Group will not be subject to first registration tax under the Motor Vehicles (First Registration Tax) Ordinance (Cap. 330 of the Laws of Hong Kong). The legal adviser of the Group confirmed that the distribution of BMW passenger vehicles would not be considered as parallel import into the PRC.

For each of the two years ended 31st December, 2000 and 2001, revenues generated from motor vehicles distribution by geographic locations are set out below:

	FY2000		FY2001	
	<i>HK\$'000</i>		<i>HK\$'000</i>	
PRC resellers	25,727	29.6%	84,149	38.5%
Hong Kong resellers ⁽¹⁾	61,282	70.4%	134,148	61.3%
Others	—	—	489	0.2%
Total	<u>87,009</u>	<u>100.0%</u>	<u>218,786</u>	<u>100.0%</u>

Note ⁽¹⁾: Revenue generated in Hong Kong represents sales of passenger vehicles to Hong Kong resellers who target to further distribute the same to end customers in the PRC.

Regulatory Environment

Under the relevant PRC laws and regulations, importing of passenger vehicles and auto parts and accessories should be carried out by foreign trade corporation authorised by MOFTEC, and distribution of both domestic and imported motor vehicles should be carried out by licensed resellers authorised by the State Planning and Development Commission of the PRC and the State Administration of Industry and Commerce of the PRC. As no member of the Group in the PRC is a licensed motor vehicles reseller nor a foreign trade corporation, the Group can only be a supplier to these licensed motor vehicles resellers in the PRC. However, foreign invested enterprises which are incorporated in the free trade zones in the PRC are allowed to import and trade motor vehicles and auto parts and accessories directly to end customers within the free trade zones. CNA Anhua (Tianjin), a 70% owned joint venture of the Company, has obtained such approval from MOFTEC in April 1999 for trading motor vehicles and auto parts and accessories in Tianjin Free Trade Zone. As such, the Group is allowed to distribute motor vehicles, auto parts and accessories directly to end customers in Tianjin Free Trade Zone under the PRC laws and regulations although this is in breach of the BMW Importer Contract. For details regarding to the PRC regulatory environment in relation to the distribution of passenger vehicles, auto parts and accessories, please refer to the section headed "Industry Overview". The sales derived from direct distribution of motor vehicles, auto parts and accessories in Tianjin Free Trade Zone were approximately HK\$9,322,000 and HK\$4,801,000 for each of the two years ended 31st December, 2000 and 2001 respectively. The decrease in direct distribution was due to the decrease in demand of the Group's customers within the zone.

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Resellers

Since 1993, the Group has formed alliances with 13 Hong Kong resellers and 84 PRC resellers which includes 33 wholesalers, North Anhua and the appointed agents of North Anhua for distribution of passenger vehicles, auto parts and accessories through their respective networks in the PRC to end customers. In January 1994, the Group entered into a distribution agreement with North Anhua for a term of 16 years to distribute passenger vehicles for the Group through its distribution network and its appointed agents in the PRC. Under such agreement, North Anhua provides the Group with its distribution network and sales support, while the Group supplies North Anhua with imported BMW, Honda and Land Rover passenger vehicles and after-sale services. Other than North Anhua, the distribution arrangements between the Group and the resellers in Hong Kong and the PRC are made on a case-by-case basis and no formal distribution agreement has been signed.

Relationship with North Anhua

North Anhua, a motor vehicle reseller in the PRC, is formerly an enterprise under the People's Armed Police of the PRC(中國人民武裝警察) with net profit of approximately RMB22 million for the year ended 31st December, 2001 and a net asset value of approximately RMB200 million as at 31st December, 2001. North Anhua subsequently became a wholly-owned subsidiary of CNA in 1999. CNA is principally engaged in research and development, manufacturing, assembly and trading of motor vehicles, auto parts and accessories in the PRC.

North Anhua engages in a wide range of business operations including state-grant import and export business of motor vehicles. It possesses a distribution network for motor vehicles of 72 distribution offices and 50 distribution agents in the PRC (for details please refer to the graph on page 94), which supports the Group distribution operation. Its subsidiaries, namely CNA Anhua (Beijing), CNA Anhua (Shanghai) and CNA Anhua (Guangzhou) who are licensed car rental operators in the PRC, were appointed to operate the car rental business in Beijing, Shanghai and Guangzhou. North Anhua also involves in development project of real estates in the PRC. Currently, its main projects are located in Beijing, Guangzhou and Inner Mongolia. In addition, North Anhua engages in hi-tech environmental protection engineering projects in Tianjin, Shanghai and Beijing.

In January 1994, the Group entered into a distribution agreement with North Anhua for a term of 16 years pursuant which the Group will supply to North Anhua the imported luxury and mid-market passenger vehicles and provide after-sales service including testing, tuning, repair and maintenance of the vehicles through Xiamen BMW and Xiamen Honda. North Anhua, being a foreign trade corporation and a licensed passenger vehicle reseller is responsible for handling the necessary procedures and documentation for importing motor vehicles into the PRC and the logistics in delivering the motor vehicles to its end customers or the end customers of the Group in the PRC. In accordance with the said distribution agreement, the Group has been supplying North Anhua with the imported passenger vehicles.

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In 1999, the Group sourced imported vehicles of other brands, including Toyota and Mercedes-Benz for North Anhua's distribution in return for commission income. These vehicles were ordered by North Anhua's discretion for its own distribution. The Group did not obtain title to the vehicles.

In January 2000, the Group further entered into a non-exclusive management consultation and technical service agreement with North Anhua for a term of 5 years. Under such agreement, the Group will provide management consultation, (including sales person training, strategic planning, etc.) and technical assistance to North Anhua for promotion and maintenance of the locally manufactured Honda passenger vehicles sold by North Anhua, whereas North Anhua will pay the Group a technical fee (being a percentage of the sale price of the locally manufactured motor vehicles sold by North Anhua). Such agreement has been approved by MOFTEC. Pursuant to such arrangements with North Anhua, the Group is able to be constantly acquainted with updated market information on the market demand and trends in the PRC market.

Turnover contributed by North Anhua for the two years ended 31st December, 2000 and 2001:

	FY2000 <i>HK\$'000</i>	FY2001 <i>HK\$'000</i>
Technical fee income	27,696	20,413
Distribution of motor vehicles	3,914	—
	<u>31,610</u>	<u>20,413</u>
% of the total Group turnover	25.3%	8.0%
Total Group turnover	<u>124,975</u>	<u>253,784</u>

Among the top 5 customers in the Track Record Period, 福建省金福集團公司 (Fujian Jin Fu Group) was referred by North Anhua. Revenue generated from sales to 福建省金福集團公司 (Fujian Jin Fu Group) represented approximately 2% of total turnover in 2001 and it is forecasted that 3.9% of total turnover will be contributed by 福建省金福集團公司 (Fujian Jin Fu Group) in 2002.

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Relationship with North Anhua

The Group entered into various business transactions with North Anhua and/or its related companies, such transactions are summarised below:

Transactions *	Brief description of the transactions	Classification	Transaction Amount (Approximate) <i>HK\$'000</i>
Co-operation projects in Guangdong Province, Fujian Province & Beijing Municipality	<p>CNA Anhua (Hertz) is obliged to refund to the Group approximately HK\$34 million if appropriate land title certificates cannot be obtained in due course.</p> <p>Mr. Loh Kim Her and Mr. Anthony Chan have undertaken to indemnify the Group against all loss suffered by it in the event that CNA Anhua (Hertz) fails to obtain the appropriate title certificate or refund to the Group the said HK\$34 million. Such indemnity is secured by the 64,664,000 Shares to be placed with an escrow agent by Mr. Loh Kim Her, Mr. Anthony Chan and Loh & Loh, and HK\$2,035,000 Sale Shares proceeds to be placed with an escrow agent by Loh & Loh. Such 64,664,000 Shares will be placed with the escrow agent as a pledge to the Company immediately after the expiration of the Lock-up Period, when the restriction on the disposal (as defined in the GEM Listing Rules to include the creation of any option, rights or interests over such securities) of such Shares, as imposed by Rule 13.16 of the GEM Listing Rules, ceases after the same period. In addition, Mr. Loh Kim Her, Mr. Anthony Chan and Loh & Loh have further undertaken to the Stock Exchange and the Company that they will not pledge or charge any of such 64,664,000 Shares to any banking institutions during the Lock-up Period. The Sale Share proceeds will be placed in escrow as a security to the Company on the terms that if the Group exercises its right under the indemnity, such amounts as correspond with the terms of indemnity will be released to the Group. (please refer to paragraph headed "Initial Management Shareholders" of "Substantial, Significant and Initial Management Shareholders" section of this prospectus for further details)</p>	Prepaid rental expenses	34,013

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Transactions *	Brief description of the transactions	Classification	Transaction Amount (Approximate) <i>HK\$'000</i>
Co-operation project in Fuzhou Municipality	Jin Tian Cheng is obliged to refund to the Group approximately HK\$11 million by October 2002. North Anhua will indemnify the Group against all losses suffered by it if Jin Tian Cheng fails to make such refund.	Prepayments, deposits and other current assets	11,262 (balance as at 31st December, 2001)
	Jin Tian Cheng has refunded HK\$3.297 million on 17th May, 2002.		7,965 (balance as at the Latest Practicable Date)
	Jin Tian Cheng is obliged to repay to the Group approximately HK\$6 million if it fails to perform the agreement or complete the project contemplated thereunder.	Prepaid rental expenses	6,242
	North Anhua has agreed to guarantee the performance and discharge by Jin Tian Cheng of its obligation under the agreement.		
	Mr. Loh Kim Her and Mr. Anthony Chan have undertaken to indemnify the Group against all loss in the event that North Anhua fails to repay or refund the Group. Such indemnity is secured by 12,484,000 Shares to be placed with an escrow agent by Mr. Loh Kim Her, Mr. Anthony Chan and Loh & Loh and HK\$7,965,000 Sale Shares proceeds to be placed with an escrow agent by Loh & Loh. Such 12,484,000 Shares will be placed with the escrow agent as a pledge to the Company immediately after the expiration of the Lock-up Period, when the restriction on the disposal (as defined in the GEM Listing Rules to include the creation of any option, rights or interests over such securities) of such Shares, as imposed by Rule 13.16 of the GEM Listing Rules, ceases after the same period. Mr. Loh Kim Her, Mr. Anthony Chan and Loh & Loh have further undertaken to the Stock Exchange and the Company that they will not pledge or charge any of such 12,484,000 Shares to any banking institutions during the Lock-up Period. The Sale Share proceeds will be placed in escrow as a security to the Company on the terms that if the Group exercises its right under the indemnity, such amounts as correspond with the terms of indemnity will be released to the Group. (please refer to paragraph headed "Initial Management Shareholders" of "Substantial, Significant and Initial Management Shareholders" section of this prospectus for further details)		

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Transactions *	Brief description of the transactions	Classification	Transaction Amount (Approximate) HK\$'000
Bank guarantee that will be provided to CNA Anhua (Beijing), CNA Anhua (Shanghai), CNA Anhua (Guangzhou)	The Group intends to provide financial assistance to its sub-licensees by applying HK\$6 million of net proceeds to guarantee the 3 sub-licensees' facilities.	Future intention	6,000
Bank guarantee provided to Beijing China National Automotive Anhua Spare Parts Ltd.	The bank has agreed to unconditionally release the Directors and the Group as guarantors upon the listing of the Shares.	Contingent liabilities	34,550

* The Company will procure a semi-annual board meeting, to be initiated by independent non-executive Directors, after the listing of the Company on GEM (The executive Directors (Mr. Anthony Chan, Mr. Lob Kim Her and Mr. Lob Nee Peng) will abstain from voting in the board meeting) to review the relevant obligations under the deed of indemnity from Mr. Anthony Chan and Mr. Lob Kim Her (including their individual asset statements to be certified by the certified public accountant on a semi-annual basis after the listing of the Company on GEM) and the outstanding obligations from North Anhua and/or its related companies. In the event if either (i) North Anhua and/or its related companies or (ii) Mr. Anthony Chan and Mr. Lob Kim Her cannot meet their relevant respective obligations, the independent non-executive Directors of the Company will call a special general meeting for all shareholders of the Company. At the special general meeting, a resolution will be passed by the independent Shareholders (with the shareholders who are connected persons to the executive Directors and North Anhua and their respective associates abstaining from voting) as to whether to enforce the deed of indemnity and to decide whether further legal action should be taken.

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Distribution Coverage

According to 2000 China Statistical Yearbook, Beijing Municipality, Tianjin Municipality, Shanghai Municipality, Guangzhou Municipality and the Xiamen Special Economic Zone in the PRC are among the top municipals and special economic zones and cities in the PRC in terms of GDP in 2000. The following map illustrates Group's product market in the PRC:



The Group is currently the authorised distributor of BMW passenger vehicles as well as auto parts and accessories in Fujian Province. In order to expand its distribution network to cover the central and western regions of the PRC, the Group is presently in active negotiations with BMW China for a right to operate authorised distributorship in the central region of the PRC.

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2) Marketing and technical assistance

For the year ended 31st December, 2000, the revenue generated from distributing imported Honda passenger vehicles of the Group decreased by 46% compared to the year ended 31st December, 1999. Such decrease was due to the commencement of manufacturing of locally manufactured Honda passenger vehicles in the PRC in 1999. Since the foreign companies are prohibited under the PRC laws from operating trading business and foreign invested domestic companies were prohibited from distributing vehicles in the PRC, the Group cannot distribute locally manufactured Honda passenger vehicles in the PRC. In order to compensate the potential loss of revenue due to the reduction in the share of imported Honda passenger vehicles in the PRC in January 2000, the Group entered into a 5-year non-exclusive management consulting and technical service agreement with North Anhua for the locally manufactured Honda passenger vehicles distributed by North Anhua. North Anhua, acts as one of the resellers of locally manufactured Honda passenger vehicles. The Group does not obtain title to such passenger vehicles.

The Group provides management consulting and technical assistance to North Anhua and its distribution agents for the promotion and maintenance of locally manufactured Honda passenger vehicles distributed by North Anhua in exchange for technical fees. The technical fees are calculated based on a mutually agreed percentage, which is currently around 13% (5% to 15% pursuant to the technical agreement), of the sales of the locally manufactured Honda passenger vehicles distributed by North Anhua. The current percentage is based on the Group's internal pricing model that comprises various kinds of fees including engineers, technicians, administration and marketing, and is calculated on a cost plus margins basis. The current allocation of the 13% technical fees is approximately 5% for engineers, 2% for technicians, 3% for administration and 3% for marketing. The current technical fee is subject to revision should there be a change in the Company's cost structure in providing such services or government regulation. The scope of marketing assistance to North Anhua includes formulating marketing strategy, market positioning, assistance in market study, training of North Anhua's sales persons, etc. Technical services comprise performing pre-sale testing and tuning, pre-delivery inspection, performing after-sale repairs and maintenance services to each vehicle sold by North Anhua on the earliest of either after 1 year from the purchase or when the vehicle runs for 10,000 km, providing technical advice and solutions on technical services, and training of North Anhua's technical staff, etc.

The marketing and technical services provided to North Anhua by the Group are summarised as below:

Marketing consulting services

- Assisting the sales and marketing team of North Anhua to conduct market research on the domestic vehicle market.
- Assessing the market positioning of North Anhua's products for domestic vehicle market by comparing its own products to products of its competitors.
- Formulating marketing strategy to secure a foothold in domestic vehicle market.

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- Sourcing experienced expatriates and local sales staff.
- Providing training program to sales persons, covering sales technique and product knowledge

Technical services

- Performing pre-sale testing and tuning (pre-delivery inspection includes testing of brake system, ventilation system etc).
- Performing after-sale repairs and maintenance services (including engine inspection, steering system inspection etc).
- Providing advice and solutions on technical services to the staff of North Anhua.
- Providing technical training program to staff of North Anhua covering technical knowledge of its own products as well as competitors' products.

For each of the two years ended 31st December, 2000 and 2001, technical fee income received from North Anhua were approximately HK\$27,696,000 and HK\$20,413,000 respectively. Notwithstanding the prohibition under the PRC law, the Group had been providing technical service to North Anhua before it obtained the approval from MOFTEC. However, the Group's PRC legal adviser confirmed that there is no detailed provision in the PRC law concerning the penalty of such violation. In addition, pursuant to the PRC Technology Import and Export Administration Regulations passed by the State Council on 31st October, 2001 (effective as of 1st January, 2002), the MOFTEC registration of the technical service agreement is no longer a condition precedent for the same to become effective. It is the understanding of the PRC legal adviser that the relevant PRC authority will not impose penalty on the Group in respect of the violation committed by the Group prior to the enactment of the said regulations based on precedents and past experience in practice. Please refer to paragraph headed "Violation of certain PRC laws regarding provision of technical services" under the "Risk Factors" section for further details.

3) After-sales service

The Group provides after-sales service such as repair and maintenance services to BMW, Honda and other mid-market motor vehicles by Xiamen BMW and Xiamen Honda in the Xiamen Special Economic Zone in the PRC. The Group established Xiamen BMW, its first authorised service centre of BMW motor vehicles in the Xiamen Special Economic Zone in January 1994. The Group set up, through Xiamen BMW, a branch to operate a Honda authorised service centre in the Xiamen Special Economic Zone in February 1996 for imported Honda passenger vehicles servicing. Such auto service centres are subject to stringent quality control which are reviewed by the management of the Group on a regular basis. The Group intends to, upon the Group's successfully receiving its right of operating authorised service centres in the central region of the PRC from BMW China, establish a BMW authorised service centre in the central region of the PRC.

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As most of the passenger vehicles distributed by the Group are mid-market and luxury cars, the Group places great emphasis on achieving a consistently high quality in its after-sales service. The Group received ISO 9002 accreditation in 2000 for its high quality services. It is the Group's policy to continuously update and upgrade the skills of its service centre technicians through internal training and skill trainings offered by BMW AG. In upholding a high standard, the Group also implements certain quality assurance measures and regularly review. The Group also frequently seeks feedback from its customers. The Group generally offers warranty for its services and third party products for a term of one year and the end users are responsible for the relevant cost beyond the warranty period.

Breakdown of cost of maintenance and cost of auto parts including costs incurred for passenger vehicles within and after the warranty period are as follows:

	FY2000 <i>HK'000</i>	FY2001 <i>HK'000</i>
Cost of service & maintenance	3,871	4,632
Cost of sales of auto parts	<u>2,163</u>	<u>7,199</u>
Total	<u><u>6,034</u></u>	<u><u>11,831</u></u>

In respect of the maintenance services performed on BMW passenger vehicles covered under warranty, the amount of cost of spare parts to be reimbursed from BMW AG were HK\$145,000 and HK\$139,000 respectively for the years ended 31st December, 2000 and 2001. The amounts of reimbursement were insignificant, therefore the claims has not been forwarded to BMW AG yet.

Xiamen Honda provides maintenance service to Honda passenger vehicles covered under warranty period, which include but not limited to Honda passenger vehicles sold through North Anhua.

The Directors believe that the Group's commitment to provides quality after-sales service is another factor contributing to its success. As a result of the Group's stringent quality control procedures, operational failure of the repair and maintenance services, delivered by the Group and companies from customers during the Active Business Pursuit Period have been minimal.

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Since December 1997, the Group has been offering free comprehensive membership service packages under the GA Privilege Club to owners of the motor vehicles distributed by the Group. Currently the club has more than 500 members. Features of such service package include discounted and several free services, which include engine oil change, collection and delivery, tire rotation, cleaning after car repairment and towing. By offering such membership service, the Directors believe that the end customers will have more confidence in buying the motor vehicles distributed by the Group and hence, increase the sales of the motor vehicles of the Group.

4) Trading of auto parts and accessories

The Directors have observed that original and quality auto parts and accessories are in great demand as a result of increasing sales of luxury and mid-market motor vehicles in the PRC. The Directors believe that trading of auto parts and accessories is an area of tremendous growth potential.

Accordingly, the Group began to import auto parts and accessories from their manufacturing companies such as BMW AG into the PRC market in January 1994. Since the incorporation of GAL in 1997, the Group has been engaged in trading auto parts in Hong Kong and selling of original auto parts to resellers in the PRC and Hong Kong. Incidentally, the Group also sell motor vehicle auto parts through Xiamen BMW in the PRC to resellers and end users for pre-sales service and after-sales repair and maintenance services respectively. The Group also orders parts and accessories from Singapore and Japan, and then deliver to the workshops in the PRC for replacement in repair and maintenance.

5) Car rental service

Leveraging on and while maintaining the Group's core business in the distribution and maintenance services of passenger vehicles in the PRC, the Group has recently diversified into car rental business in the PRC in hope that this can diversify these revenue base by way of sub-licensing the Hertz System and car rental fleets that will be sourced from the Group by the sub-licensees. The car rental operation of the Group's sub-licensees started in January 2002, and the Group has started to provide management consulting service to the sub-licensees. The Group has been appointed by Hertz as its principal licensee and has the right to use and to sub-license its right to use the Hertz System in the operation of car rental business in the PRC for a term of 5 years commencing from 1st August, 2001. The sub-licensees acquired the car rental fleet by utilizing capitals and funds from their parent company, CNA Anhua (Hertz). The Group provided financial assistance to the car rental sub-licensees, who are subsidiaries of North Anhua, for their working capital needs in respect of the HK\$34 million banking facilities guarantee granted to Beijing China National Automotive Anhua Spare Parts Ltd. whose 45% equity interest is held by CNA Anhua (Hertz), a wholly-owned subsidiary of North Anhua to be used in connection with the car rental business operated by the three sub-licensees. Hertz, which was founded in 1918, is the leading vehicle renting organisation in the world with a fleet of approximately 525,000 vehicles in approximately 6,500 locations in over 140 countries. The Directors believe that this is the first move of Hertz to develop its car rental business in the PRC market.

BUSINESS OF THE GROUP

In order to engage in car rental business in the PRC, a company must meet certain prescribed economic and technology requirements and obtain both a License for Operating Road Transportation (道路運輸經營許可證) and a Certificate for Road Transportation (道路運輸證) from the relevant administrative authority. Despite that the Group is currently not a licensed car rental operator in the PRC, the Group has the right pursuant to the agreement with Hertz, with CNA Anhua (Tianjin) as the principal licensee of Hertz, to appoint sub-licensees in the PRC who are licensed car rental operators. Although the scope of business as set out in the business license of CNA Anhua (Tianjin) does not expressly cover car rental operation, the PRC legal adviser of the Group has opined that the sub-licensing of the Hertz System by CNA Anhua (Tianjin) to other PRC companies which are permitted to operate car rental business is not in violation of the PRC law. Effectively, such role of CNA Anhua (Tianjin) as the principal licensee of Hertz involves the provision of co-ordination and consultancy services which falls within the ambit of its scope of business. These sub-licensees have entered into non-exclusive sub-license agreements with Hertz for using the Hertz System to provide car rental service in the PRC. Being the principal licensee, CNA Anhua (Tianjin) is responsible for identifying sub-licensees, appointing sub-licensees to Hertz and providing management consulting, financial assistance and technical expertise which includes strategic planning, staff training and daily supervision of the car rental operation of all sub-licensees.

As such, the Group has appointed 3 licensed car rental operators in the PRC, namely CNA Anhua (Beijing), CNA Anhua (Shanghai) and CNA Anhua (Guangzhou), all of which are subsidiaries of North Anhua, to enter into non-exclusive sub-license agreements with Hertz for five years commencing from 1st August, 2001. As the Group's sub-licensees, they are entitled to use the Hertz System to operate car rental business in the PRC. The sub-licensees are authorised and approved by the State Administration of Industry and Commerce to conduct car rental operations in the PRC. Under this arrangement, these sub-licensees are required to pay Hertz, through the Group, an annual pro-rated license fee for using the Hertz System. The Group, as the principal licensee, acts as a collecting agent for Hertz to collect these license fees from the sub-licensees and pass on the same to Hertz. The Group is required to pay Hertz an one-time initial fee and these sub-licensees are required to pay the Group a one-time initial fee plus a share of their respective annual profit based on the audited net profit derived from these sub-licensees for the management consulting, financial assistance and technical expertise services provided by the Group. Management consulting includes consulting on car rental management and operation, training to car rental personnel customer referral, etc. Whereas technical expertise includes testing, provisions of repairs and maintenance services to car rental fleet. The Group will receive its share of these sub-licensees annual profit at the end of each financial year in December. Currently, the Group does not meet the criteria set out by MOFTEC to invest in the car rental business in the PRC (please refer to "Industry Overview" section of this prospectus for details of the regulations), however, the Group has the intention to acquire 19.8% interest in each of CNA Anhua (Beijing), CNA Anhua (Shanghai) and CNA Anhua (Guangzhou) and the acquisition will only take place until such time the Group meets the criteria.

In January 2002, the Group commenced the provision of management and technical expertise in the operation of the Hertz System to its designated sub-licensees in Beijing Municipality, Shanghai Municipality and Guangzhou Municipality with management consultation support from Hertz. The Directors believe that this will allow the Group to capture the tremendous potential of the PRC car rental market in provision of consulting and technical expertise services and will secure a foothold in the PRC.

BUSINESS OF THE GROUP

The Directors further believe that the Group's alliance with Hertz will enhance its service competence, public reputation and generate business from Hertz's extensive global business connections with foreign investors and tourists coming to the PRC. The Directors also believe that the synergy created from the expertise of Hertz in the car rental business worldwide and the Group's proven knowledge about the PRC motor vehicle market will enable the Group to capitalise on the potential of the car rental market in the PRC, especially after PRC's accession to the WTO. The car rental business will allow the Group to extend its presence to Beijing, Shanghai and Guangzhou to form a car rental network. The Directors believe that this will allow the Group to establish its reputation and recognition in the PRC car rental industry as well as to expand its geographical coverage in respect of its distribution of motor vehicles in the PRC so as to facilitate the Group to attain additional distributorships from other foreign motor vehicle in the future.

SALES AND MARKETING

The Group's sales and marketing activities are carried out by its sales departments in Hong Kong and Xiamen Special Economic Zone of the PRC. As at the Latest Practicable Date, the Group's sales and marketing team comprised 3, 2 and 9 employees in Singapore, Hong Kong and the PRC respectively.

The Group mainly conducts its business through agency sales approach. Each of the Group account managers, who is responsible for a particular region of the Group's agents, contacts the Group's existing and potential licensed distributors on a regular basis and provides them with, among other things, the latest information on new models, government regulations and industrial trends in relation to the luxury and mid-market passenger vehicle market as well as information on products and services offered by BMW AG, Honda Corporation and the Group. The Directors believe that good relationship with the Group's agents can be established through such marketing strategy and consider that the Group's strong agent relationship is one of the key factors for its success. The marketing expense of the Group for the two years ended 31st December, 2000 and 2001 were approximately HK\$711,000 and HK\$772,000 respectively.

CUSTOMERS

There are over 90 resellers in total, distributing imported vehicles for the Group including 13 resellers in Hong Kong, 33 resellers in the PRC, North Anhua and 50 agents appointed by North Anhua. The Group also conducts direct sales in Tinajin Free Trade Zone, however, it is just a special case to the Group's operation as almost all sales were actually sales to distributors.

In formulating its marketing strategies, the Group divides the PRC passenger vehicle market into two targeted segments, namely the upper-end and mid-end segments. The upper-end segment customers refer to enterprises and individuals who are able to afford higher price in return for prestige, luxury and high technology. The mid-end segment customers are enterprises and individuals who are more budget conscious but also value quality and services.

BUSINESS OF THE GROUP

The Group's largest customer, which is a Hong Kong reseller, contributed to approximately 30% and 27% of the Group's turnover for each of the two years ended 31st December, 2000 and 2001 respectively.

The five largest customers including 4 Hong Kong resellers and 1 PRC reseller, contributed to approximately 59% and 52% of the Group's turnover for each of the two years ended 31st December, 2000 and 2001 respectively. Neither the Group nor any of the Directors, their respective associates (as defined in the GEM Listing Rules), has any interests in any of the five largest customers, of the Group for each of the two years ended 31st December, 2000 and 2001.

PRODUCT SOURCING

BMW AG is the Group's major supplier and accounted for approximately 36% and 52% of the Group's total purchases for each of the two years ended 31st December, 2000 and 2001 respectively.

BMW AG

BMW AG was founded in 1916 and was one of the largest passenger vehicle manufacturers. In 2000, BMW products were sold in more than 14 countries worldwide and approximately 70.73% of such products were sold outside Germany.

The sales volume of BMW passenger vehicles in the PRC in 2000 recorded a growth rate of approximately 171% over the previous year. BMW AG expected that sales of BMW passenger vehicles will grow by approximately 54% in 2001 when compared with 2000.

BMW AG has a set of systematic procedures for its authorised distributors to place orders. At the beginning of each year, the Group is required to provide BMW AG with an annual projection of the estimated number of vehicles that it plans to purchase from BMW AG during that year for the PRC market. The Group places orders for motor vehicles with BMW AG on a monthly basis based on its quarterly and monthly projections of customer demand and its target inventory level of auto parts and accessories. The lead time for the delivery of BMW vehicles may range from three to four months and the Group will keep a small volume of inventory.

All orders the Group places with BMW AG are on an "ex-factory" basis. Under such arrangement, the Group is responsible for insurance coverage, shipment transportation to Hong Kong, the Group's logistic hub. Payments are effected by the Group to BMW AG by letters of credit in euro. All orders are payable by the issuing bank acting on behalf of the Group against delivery of certain documents, which typically include shipping invoices and bills of lading. Settlement is normally made within 60 days upon the receipt of the relevant bank instructions and documents.

BUSINESS OF THE GROUP

The Group aims to maintain sufficient stock of BMW auto parts and accessories in the PRC so that such auto parts and accessories would be available when first requested by its customers. The Group places orders for auto parts and accessories with BMW Asia Pte. Ltd in respect of its PRC operations on a monthly basis. Payments are effected by the Group in euro by telegraphic transfer through its banks.

BMW AG warrants that the BMW passenger vehicles distributed by the Group are free of defects for one year. The Group will be reimbursed by BMW AG for all replacement costs of parts incurred in any warranty claim made against the Group during such warranty period.

Honda Motor Co., Ltd.

Honda Motor Co., Ltd. is recognised internationally for its expertise and leadership in developing and manufacturing a wide variety of products, ranging from small general-purpose engines to specialty sports cars that incorporate highly efficient internal combustion engine technology. Approximately 11.5 million Honda engines were sold worldwide during the year ended 31st March, 2001.

The Honda passenger vehicles sold in the PRC are either imported or domestically manufactured in the PRC. The Group places orders to Honda Motor (China) Co., Ltd. for imported Honda passenger vehicles and distributes them through the resellers' network.

The Group became an importer of Honda motor vehicles for the PRC market in November 1995 whereas the Honda agreement was made on a case-by-case basis.

Land Rover Group

Land Rover Group has been manufactured since 1948 and is accredited as the world's leading four-wheel-drive vehicles. The vehicles are designed for on-road and off-road conditions. The manufacturing plant for Land Rover in United Kingdom and all the products are imported from United Kingdom. The Group attained the non-exclusive distributorship of Land Rover in September 1997 when it commenced distribution to Fujian Province in the PRC. Such distribution agreement shall continue until terminated by either party giving 12 months' prior notice. The Group directly places orders with the headquarter of Land Rover in the United Kingdom for the passenger vehicles and distributes them through the reseller's network.

Other brands

The Group distributes other brands, such as Toyota and Mercedes-Benz, from respective dealers to the PRC market. The Group only places orders with the resellers of Toyota and Mercedes-Benz in Hong Kong on a case-by-case basis.

BUSINESS OF THE GROUP

The Directors are confident that the Group is a valued and preferred distributor of BMW AG and importer of Honda passenger vehicles in the PRC market respectively based on:

- its long-standing relationship with BMW AG and Honda Motor (China) Co., Ltd.;
- its experience and successful record in distributing BMW and Honda passenger vehicles in the PRC market, contributing to approximately 41% and 29%, 59% and 9% of the turnover of the Group for the two years ended 31st December, 2000 and 2001 respectively;
- its ability to provide quality after-sales service to its customers and its plans to develop a network of service centres in selected regions in the PRC; and
- its strong working relationship with North Anhua and CNA which have extensive distribution networks in the PRC.

The largest supplier of the Group accounted for approximately 36% and 52% of the Group's turnover for each of the two years ended 31st December, 2000 and 2001 respectively. For each of the two years ended 31st December, 2000 and 2001, the Group's five largest suppliers accounted for approximately 82% and 94% of the total purchases made by the Group respectively. Neither the Group nor any of the Directors, their respective associates (as defined in the GEM Listing Rules), has any interests in any of the five largest suppliers of the Group for each of the two years ended 31st December, 2000 and 2001.

STOCK CONTROL

In order to control the stock levels of motor vehicles, auto parts and accessories so as to achieve minimum stock holding periods and to minimise loss attributable to stock obsolescence in the automobiles industry while being able to meet the client's demand on a timely basis, the Group normally keeps a small volume of inventory and quarterly reviews the level, movements and aging of its inventory. The Group also maintains close contacts with its customers to keep abreast of the latest market trends and potential customer demand. Based on the continuous review on its inventory position and the feedback from its customers, the Group adjusts the types of orders and the amount of such orders it places with its suppliers with a view to optimising the effectiveness of its inventory management. The Group carries out the following measures in controlling stock: (i) placing most of the purchasing orders to the Group's suppliers after reviewing and forecasting the market demand; (ii) analysing and ascertaining the appropriate levels of accessories for each product line based on the past records, and (iii) conducting regular management meetings to enhance communications between the sales department, purchasing and finance departments.

BUSINESS OF THE GROUP

The Group does not make general provision for stock obsolescence. However, specific provision will be made based on regular specific review on the stock movement.

The ability of the Group to maintain effective control on inventory is evidenced by the fact that the provisions for inventory obsolescence made by the Group amounted to HK\$252,000 and HK\$Nil for the two years ended 31st December, 2000 and 2001 respectively, representing less than one per cent. of the Group's total sales during the same year.

CREDIT POLICY

The Group only experienced minimal bad debt during the Track Record Period. Nonetheless, in addition to the careful selection of customers with payment credibility, the senior management of the Group closely monitors the credit terms given to the Group's customers, and the Group does not accept payment by instalment arrangement. For the PRC market, sales of imported vehicles are mostly denominated in euro and HK dollars. Due to the restrictions imposed on the issue of foreign currency denominated letters of credit in the PRC, only certain entities (including foreign trade corporations) which have obtained the relevant approval from the State Administration of Foreign Exchange may apply for the issue of such letters of credit.

The Group's motor vehicle distribution transactions are mainly made on a letters of credit basis, the remaining transactions are settled either on a cash on delivery basis or credit terms. For each of the two years ended 31st December, 2000 and 2001, approximately 41%, 30% and 29% and approximately 59%, 12% and 29% of motor vehicle distribution transaction were settled by letters of credit, cash on delivery basis and credit terms of 60 to 150 days respectively. The majority of the Group's auto parts and accessories trading transactions are made on a cash on delivery basis. For the rest of auto parts and accessories trading transactions, their terms of sale, including the credit terms, generally require the approval of the senior management of the Group. The senior management of the Group reviews on a quarterly basis and, if necessary, makes appropriate adjustments to the credit limits that have been assigned to the Group's customers based on their latest spending and repayment behavior. The senior management of the Group also closely monitors the credit position of the Group and the amount and aging of the receivables due from its customers and, if necessary, takes appropriate action to ensure that effective credit control is implemented.

The Group has established credit control systems to tighten control over accounts receivables. Such systems assist the Group in shortening the receivables settlement periods and improving debt collection. Salient features of such control systems include: (i) transactions with new agents/customers are carried out on a strict cash-term basis; (ii) thorough studies are conducted on the creditworthiness of new agents/customers before credit terms are provided to them; (iii) reminders will be sent to overdue accounts; and (iv) legal advices will be sought for delinquent accounts.

BUSINESS OF THE GROUP

The Group did not make general provision for bad debts in 2000 and approximately 1.9% general provision for bad debts was made for the year ended 31st December, 2001. Specific provision will be made based on quarterly review on the settlement of receivables. For each of the two years ended 31st December, 2000 and 2001, the provision for bad and doubtful debts in the Group's balance sheet amounted to approximately HK\$2,060,000 and HK\$1,556,000 respectively, representing less than 2% of the Group's turnover for each of such periods.

SEASONALITY

To a certain extent, the sales of the Group are subject to seasonal factors. During the second and the fourth quarters of the year, the sales of the Group are generally slower. The Group's sales are positively correlated to its customers' business operating result, since most of their customers made purchases after the announcement of their annual or interim business results, thus, the second and fourth quarters are usually the low season for the Group's sales. Whereas, the peak seasons usually lie in the first and third quarters. Customers place orders in the first and third quarters after the release of their annual and interim business results to assure their financial position in making capital expenses.

STRATEGIC INVESTOR

Comfort Group

Comfort Group, whose shares are listed on the Stock Exchange of Singapore is an indirect substantial shareholder of the Company, through its wholly-owned subsidiary, Comfort (China). Comfort Group is mainly engaged in the taxi and bus operation business in Singapore as well as motor vehicle distribution business in Singapore. Comfort Group engages in taxi and bus operation business in the PRC as well as petrol service station and car and auto parts distribution in Suzhou of the PRC. As Comfort Group's core businesses are different from those of the Group and that the car and auto parts distribution businesses are geographically mutually exclusive from where the Group is operating in the PRC, the Directors believe that there is no competing interest and the relationship with Comfort Group will provide the Group financial support in the future business development of its business in the PRC.

STRATEGIC ALLIANCES

North Anhua

North Anhua was formerly a division-bureau level enterprise under the direct administration of the army headquarters of the Chinese People's Armed Police (中國人民武裝警察). Headquartered in Beijing, North Anhua is currently a subsidiary of CNA, which is one of the 163 key state-owned enterprises affiliated to 中央企業工委管理 (China Central Enterprise Industrial Commission). North Anhua has set up a number of subsidiary enterprises with several local branches being established in China's domestic regions.

BUSINESS OF THE GROUP

North Anhua engages in a wide range of business operations including state-grant import and export business of motor vehicles with net profit of approximately RMB22 million for the year ended 31st December, 2001 and a net asset value of approximately RMB200 million as at 31st December, 2001. The Group has been in close business relationship with North Anhua since 1994 and the Directors believe that the prestigious history and foundation of North Anhua have also been a key element in the business development of Group throughout the period. It possesses a distribution network for motor vehicles of 72 distribution offices and 50 distribution agents in the PRC (for details please refer to the graph on page 94), which supports the Group distribution operation. Its subsidiaries, namely CNA Anhua (Beijing), CNA Anhua (Shanghai) and CNA Anhua (Guangzhou) who are licensed car rental operators in the PRC, were appointed to operate the car rental business in Beijing, Shanghai and Guangzhou. North Anhua also involves in development project of real estates in the PRC. Currently, its main projects are located in Beijing, Guangzhou and Inner Mongolia. In addition, North Anhua engages in hi-tech environmental protection engineering projects in Tianjin, Shanghai and Beijing.

The Group has been in close business relationship with North Anhua in distributing passenger vehicles since 1994. The Directors believe that North Anhua has been a key element in the Group's business development as it assists the Group's distribution of motor vehicles and overcomes various trade barriers for importing motor vehicles as well as facilitates the Group's implementation of its car rental services in the PRC. However, North Anhua currently has no intention to become a shareholder of the Group as at the date of the prospectus.

Hertz

Hertz, which was founded in 1918 is a wholly-owned subsidiary of Ford Motor Company. It is the leading vehicle renting organisation in the world with a fleet of approximately 525,000 vehicles in approximately 6,500 locations in over 140 countries. Hertz has developed and maintained an extensive network of car rental locations around the world, enabling it to provide consistent quality, pricing and service worldwide.

The Directors believe that pursuant to the arrangements between the Group and Hertz in respect of operating car rental business through the sub-licensing arrangements in the PRC, the Group, leveraging on the brand name and the international business contacts of Hertz, and utilising the Hertz System and the Group's expertise and business network in the PRC, will be well-positioned to provide quality management services to meet the needs of its targeted car rental clients.

BUSINESS OF THE GROUP

COMPETITION

The key competitors of the luxury and mid-market passenger vehicles distributed by the Group in the markets in which it operates mainly include other European and Japanese importers and distributors. The Japanese importers and distributors have traditionally enjoyed a competitive advantage, offering relatively more competitive prices. Notwithstanding the difference in initial acquisition costs, the Group intends to principally compete on the basis of:

- the quality of its products, which the Directors believe, are well-recongnised in the market;
- its ability to provide quality after-sales service to its customers in the PRC; and
- its position as one of the leading distributors of BMW in the PRC and one of the importers of Honda motor vehicles in the PRC.

CONNECTED TRANSACTIONS

Prior to the listing of the Shares on GEM, the Group has entered into the following connected transactions (as defined in the GEM Listing Rules):

1. on 3rd April, 1997, a 10-year loan agreement was entered into between Malayan Banking Berhad, Malaysia and GAPL for a term of 10 years in respect of a loan of US\$420,000 for the acquisition of a real estate property in Beijing, PRC. Mr. Anthony Chan and Mr. Loh Nee Peng provided personal guarantee in favour of Malayan Banking Berhad.
2. on 23rd March, 1998, a 10-year loan agreement was entered into between Overseas Union Bank Limited, Singapore and GAPL for a term of 10 years in respect of a loan of US\$147,000 for the acquisition of another real estate property in Beijing, PRC. Mr. Anthony Chan, Mr. Loh Kim Her and Mr. Loh Nee Peng provided unconditional & irrevocable personal guarantee in favour of Overseas Union Bank Limited.
3. on 21st December, 1998 credit facilities in the nature of overdrafts, letters of credit and/or trust receipts and shipping guarantees of SGD5.5 million were granted by Oversea-Chinese Banking Corporation Limited, Singapore to GAPL. The following guarantees were provided in favour of Oversea-Chinese Banking Corporation Limited:
 - Mr. Loh Kim Her, Mr. Loh Nee Peng, Mr. Anthony Chan and Mr. Chan Kung Git, father of Mr. Anthony Chan provided a joint and several personal guarantee for SGD8.985 million;
 - Mr. Loh Boon Cha, brother of Mr. Loh Kim Her provided a personal guarantee for SGD4.867 million;

BUSINESS OF THE GROUP

- L&B provided a corporate guarantee for SGD3.776 million; and
 - Eng Kheng (S) Pte Ltd, a company which is held as to 61% by Mr. Anthony Chan, provided a corporate guarantee for SGD8.302 million.
4. on 27th October, 1999, a loan agreement was entered into between GAPL and Commerzbank Aktiengesellschaft, Singapore branch for a term loan facility in U.S. dollars equivalent to Japanese Yen 767,738,319 and two banker's guarantees in the respective amount of DEM380,000 and SGD10,848. In order to secure full repayment of such banking facilities, the following security was provided in favour of Commerzbank Aktiengesellschaft:
- Mr. Loh Kim Her, Mr. Loh Nee Peng, Mr. Anthony Chan and Mr. Chan Kung Git, father of Mr. Anthony Chan provided two joint and several personal guarantees for an aggregate amount of US\$27.7 million;
 - Mr. Loh Boon Cha, brother of Mr. Loh Kim Her US\$1.54 million at Commerzbank Aktiengesellschaft as security;
 - L&B provided a corporate guarantee for US\$1.925 million;
 - Eng Kheng (S) Pte Ltd, a company which is held as to 61% by Mr. Anthony Chan, provided a corporate guarantee for US\$11 million; and
 - GAPL charged and assigned all its interests, rights in certain of its receivables in favour of Commerzbank Aktiengesellschaft.
5. on 4th January, 2001, banking facilities in the nature of overdraft, letters of credit, trust receipts and/or shipping guarantees of SGD10.5 million were granted by Bank of China, Singapore Branch to GAPL. In order to secure full repayment of such banking facilities, Harley Investment Pte Ltd and Ivory Investment Pte Ltd., companies all shares of which are beneficially owned by Mr. Loh Kim Her, provided legal mortgage over certain properties in Singapore owned by them in favour of Bank of China. Mr. Anthony Chan and Mr. Chan Kung Git, father of his also provided a joint and several personal guarantee in favour of Bank of China to secure the advances, credits and banking facilities extended by Bank of China to GAPL up to sum of S\$11,500,000.
6. on 17th July, 2001, a loan agreement was entered into between Industrial and Commercial Bank of China, Singapore Branch and GAPL for banking facilities of US\$5,000,000 for the operation of the Group. In order to secure full repayment of such banking facilities, Mr. Anthony Chan and Mr. Loh Kim Her provided unconditional & irrevocable personal guarantee in favour of Industrial and Commercial Bank of China, Singapore branch.

BUSINESS OF THE GROUP

7. on 11th June, 1999, a tenancy agreement was entered into between Atland Properties Pte Ltd, a company all shares of which are beneficially held by Ms. Chan Xiao Li, sister of Mr. Anthony Chan, as the lessor and GAPL as the lessee in respect of a premises in Singapore, for a term of 36 months commencing on 25th September, 1998. Such tenancy agreement was renewed on 6th September, 2001 for a term of 12 months from 25th September, 2001 to 24th September, 2002. The monthly rent under such tenancy agreement is SGD3,890, which the Company's property valuer, DTZ Debenham Tie Leung Limited, has opined as an open market rental.
8. on 11th June, 1999, a tenancy agreement was entered into between GAPL as the lessor and Octavus Properties Pte Ltd, a company all shares of which are beneficially held by Mr. Anthony Chan, as the lessee in respect of a premises of approximately 353 sq.ft. in Singapore, for a term of 36 months commencing on 25th September, 1998. Such tenancy agreement was renewed on 10th September, 2001 for a term of 12 months upon its expiration. The monthly rent under such tenancy agreement is SGD800, which the Company's property valuer, DTZ Debenham Tie Leung Limited, has opined as an open market rental.
9. on 11th June, 1999, a tenancy agreement was entered into between GAPL as the lessor and Eng Kheng (S) Pte Ltd, a company which is held as to 61% by Mr. Anthony Chan, as the lessee in respect of a premises of approximately 353 sq.ft. in Singapore, for a term of 36 months commencing on 25th September, 1998. Such tenancy agreement was renewed on 10th September, 2001 for a term of 12 months upon its expiration. The monthly rent under such tenancy agreement is SGD800, which the property valuer, DTZ Debenham Tie Leung Limited, has opined as an open market rental.
10. on 4th October, 1999, a tenancy agreement was entered into between Xiamen L & B Property Co., Ltd, a company which is beneficially held as to 5% by Mr. Loh Kim Her and 95% by his family members, as the lessor and GAPL as the lessee in respect of a premises of 710 sq. metres in Xiamen, for a term of 21 years commencing on 1st November, 1999. Such premises is used as the office of Xiamen BMW and its monthly rent is RMB31,388, which the Company's property valuer, DTZ Debenham Tie Leung Limited, has opined as an open market rental.

Each of the abovementioned banks has confirmed with the Directors that the respective personal guarantees in transactions 1., 2., 3., 4., 5. and 6. above will be released prior to or upon the listing of the Shares on GEM as concurred by the banks and thus such transactions will not constitute connected transactions.

Transactions 7., 8., 9. and 10., above will continue after the listing of the Shares on GEM and thus constitute a continuing connected transaction (as defined in the GEM Listing Rules).

BUSINESS OF THE GROUP

The Directors have confirmed that such continuing connected transactions have been entered into on normal commercial terms, determined on an arm's length basis and are carried out in the usual and ordinary course of business of the Group and the terms of which are fair and reasonable so far as the shareholders of the Company are concerned. The Sponsors and the Directors (including the independent non-executive Directors) are of the opinion that the above transactions have been and will be entered into on normal commercial terms and in the usual and ordinary business of the Group and the terms of which are fair and reasonable so far as the shareholders of the Company are concerned. Each of the above transactions will fall within the exemption under Rule 20.23 of the GEM Listing Rules as the total consideration for each of the transaction is less than HK\$1,000,000 per annum. Accordingly, the transactions will be exempt from the reporting, announcement and shareholders' approval requirements under Chapter 20 of the GEM Listing Rules. The Directors will closely monitor the aggregate of the amounts involved in each of the continuing connected transactions and if the aggregate amount of such transaction exceeds HK\$1,000,000 or if any term of such transaction is altered or if any new connected transaction is entered into in the future, the Company will comply with all applicable requirements of the GEM Listing Rules in connection therewith.