



Sino-Forest Corporation



1999 ANNUAL REPORT

嘉漢林業

MISSION

Sino-Forest's mission is to become the dominant integrated forest products supplier throughout Asia and the leader in practising sustainable forestry management in the region.

CORPORATE PROFILE

Sino-Forest Corporation is the only foreign-owned, fully integrated forest products company practising sustainable forestry management in China.

Sino-Forest's business strategy incorporates a new paradigm for the forestry industry in China by focussing on the three "Ts" of its business: trees, technology and trading.

Since becoming a public company in 1994, Sino-Forest has grown profitably, meeting or exceeding financial performance targets for 24 consecutive quarters and increasing revenue and net income by more than 590 and 835 per cent, respectively, as production increased by 1,209 per cent.

As the first entrant into China's private forestry sector, Sino-Forest has captured the largest market share of privately owned, fast-growing hardwood plantation trees in China.

Going forward, Sino-Forest will continue to diversify its operations and expand its markets for value-added wood products and lumber and wood trading throughout Asia.



TABLE OF CONTENTS

Highlights and Six-year Overview	2
Report to Shareholders	3
President's Message	7
Review of Operations	
China, Growing, Harvesting, Sustaining	8
Management's Discussion and Analysis	18
Management's Report	23
Auditors' Report	23
Consolidated Financial Statements and Notes	24
Directors and Officers	40
Corporate and Shareholder Information	41

生生不息



SINO-FOREST: SUSTAINING GROWTH

Just as trees require certain elements and conditions for growth, so too do corporations. And just as resources sustain growth when managed effectively, so too are businesses sustainable when well managed.

As Sino-Forest enters its seventh year as a profitable public company, we remain committed to sustaining growth for our investors through effective management of our tree plantations and development of our value-added wood products businesses. These businesses are supported by a substantial technological infrastructure of biotechnology, wood utilization and processing, information and logistics, and e-commerce.

Sino-Forest's establishment in China's forestry sector six years ago means that it is uniquely positioned to profit from the opportunities offered by China's rapidly growing economy. Our investment in plantations, using biotechnology supported forestry techniques, has placed Sino-Forest at the forefront — producing fast-growing, high quality plantation timber.

Our investments in wood utilization and processing technology will enable us to engage in whole tree utilization, which is both cost effective and efficient. Our further investment in downstream value-added processing technologies will

enable us to turn engineered wood panels into a wide range of products.

Linking this efficient production of timber and advanced processing technology is our information and logistics technology. With our advanced supply chain management, we are able to source products from our own facilities and from other providers (both domestic and international) to provide procurement solutions that efficiently meet the demands of our customers.

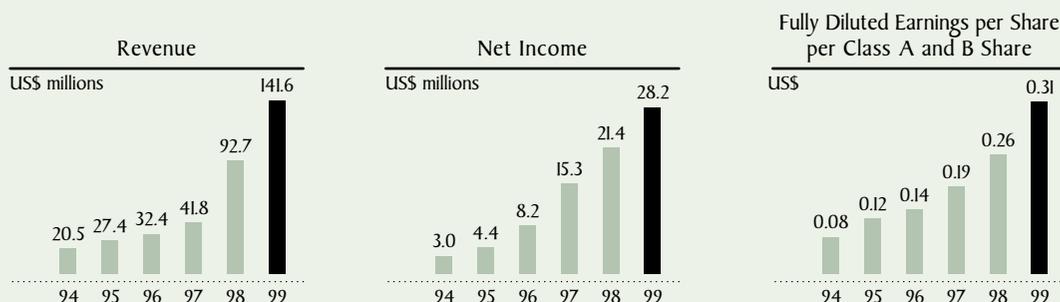
Unlike traditional manufacturing, the forestry business, and in particular the forest plantation business, is somewhat less risky and more flexible in market downturns. Trees don't cost a lot to maintain — they grow free from available light and water and continue to increase their yield until harvested — an activity that can be delayed if market conditions are not ideal to do so.

Thus, as economic conditions improve in other parts of Asia such as Japan, Sino-Forest can leverage its established business position and relationships in China to develop new businesses throughout the Asian region.

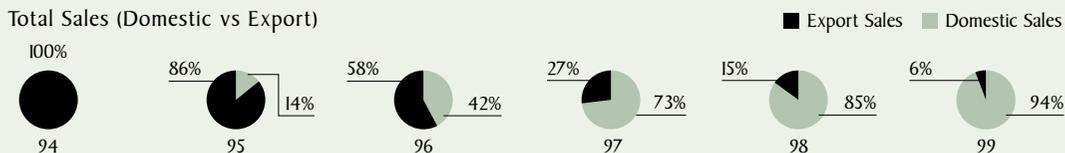
Sino-Forest will continue to deliver returns for investors in the 21st century by growing our business sustainably to take advantage of the burgeoning market for forest products in Asia.

HIGHLIGHTS AND SIX-YEAR OVERVIEW

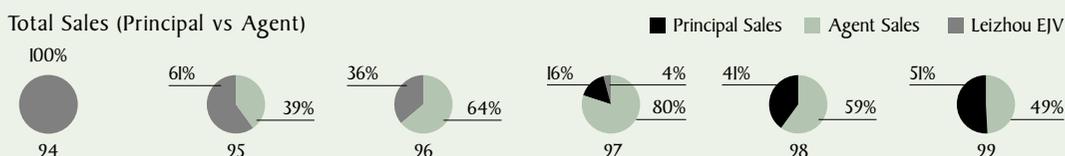
- Sino-Forest's six-year record of profitability continued through 1999 as the Company delivered record revenue and earnings results and extended our record of meeting or exceeding financial targets for 24 consecutive quarters.
- Sino-Forest's core plantation business continued to grow significantly, producing 2,045,200 Bone Dry Metric Tonnes (BDMT) of wood chips in 1999, an increase of 28 per cent over 1998 and an increase of 1,209 per cent over 1994.
- Sino-Forest's diversification into value-added lumber and wood products trading continued in 1999 with a resulting 219 per cent increase in revenue over 1998 and an increase of 1,591 per cent over 1994.
- Sino-Forest began construction of a particle board mill in 1999, which will commence production in the second quarter of 2000 and expand the Company's capabilities in the growing wood processing market.
- Sino-Forest's share of the Asian pulp wood and engineered wood products market continued to increase in 1999 as the region continued to experience the world's largest fiber deficit and highest net growth in fiber demand.



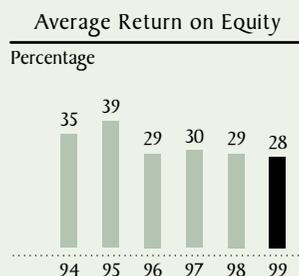
Total Sales (Domestic vs Export)



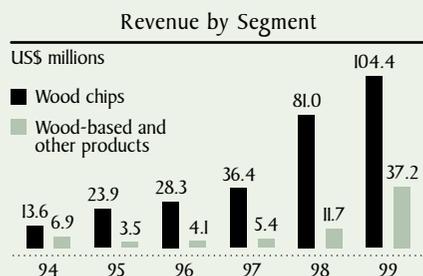
Total Sales (Principal vs Agent)



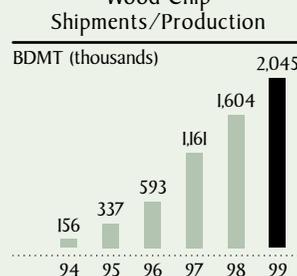
Average Return on Equity



Revenue by Segment



Wood Chip Shipments/Production



Allen T.Y. Chan

管仲連

Chairman and Chief Executive Officer



報告

REPORT TO SHAREHOLDERS

(All amounts are expressed in U.S. dollars, unless otherwise indicated.)

SUSTAINING GROWTH

In 1999, Sino-Forest continued its six-year record of profitability and concluded the year with record revenue and earnings results. We continued to increase our share of the Asian pulp wood and engineered wood products market as the region continued to experience the world's largest fiber deficit and highest net growth in fiber demand.

Sino-Forest's business strategy remained focussed in 1999 on our new paradigm for the forestry industry in China. That paradigm, merging traditional forestry practices with modern technology, is captured by the "TTT" acronym, which represents the three "Ts" of our business: trees, technology and trading. Simply, we are using technology to increase the productivity of our tree plantations, which in turn become the trading currency by which we increase profits.

FINANCIAL PERFORMANCE MET OR EXCEEDED TARGETS FOR 24 CONSECUTIVE QUARTERS

Over the past six years, since our inception as a public company, Sino-Forest has met or exceeded financial performance targets for 24 consecutive quarters.

With 1999 revenues of \$141.6 million and net income of \$28.2 million, we have delivered increases of more than 590 per cent and 835 per cent, respectively, since 1994. In turn, this has produced fully diluted earnings per share of \$0.31 in 1999, a 288 per cent increase over 1994.

Comparing these results to 1998, we achieved a 53 per cent increase in revenue (from \$92.7 million in 1998 to \$141.6 million in 1999); a 32 per cent increase in net income (from \$21.4 million in 1998 to \$28.2 million in 1999); and a 19 per cent increase in fully diluted earnings per share from \$0.26 in 1998 to \$0.31 in 1999.

PLANTATIONS AND ENGINEERED WOOD
PRODUCTS TRADING INCREASES MARKET SHARE

Sino-Forest's focus on two primary objectives continued in 1999: to build our strong core plantation business by growing and further improving our timber asset base, and to expand our lumber and engineered wood products trading activities.

Plantations

Through the phase-in of additional plantation lands, Sino-Forest reached our 1999 goal of shipping at least 2,000,000 BDMT of wood chips and logs, of which approximately 51 per cent were sold on a principal basis.

In total, we sold 2,045,200 BDMT of wood chips in 1999, an increase of 28 per cent over 1998 and an increase of 1,209 per cent over 1994.

Sino-Forest remains on schedule to phase in the remaining 454,000 hectares of plantation lands over the next five years. We expect to increase wood chip and log production by at least 400,000 to 500,000 BDMT per year until we reach a sustainable level of production of 4,000,000 BDMT of wood chips annually.

In 1999, Sino-Forest made even greater in-roads into the Chinese market as our domestic wood

chip shipments increased to 1,922,200 BDMT, (94 per cent of our production) from 1,358,400 BDMT (85 per cent of our production) in 1998.

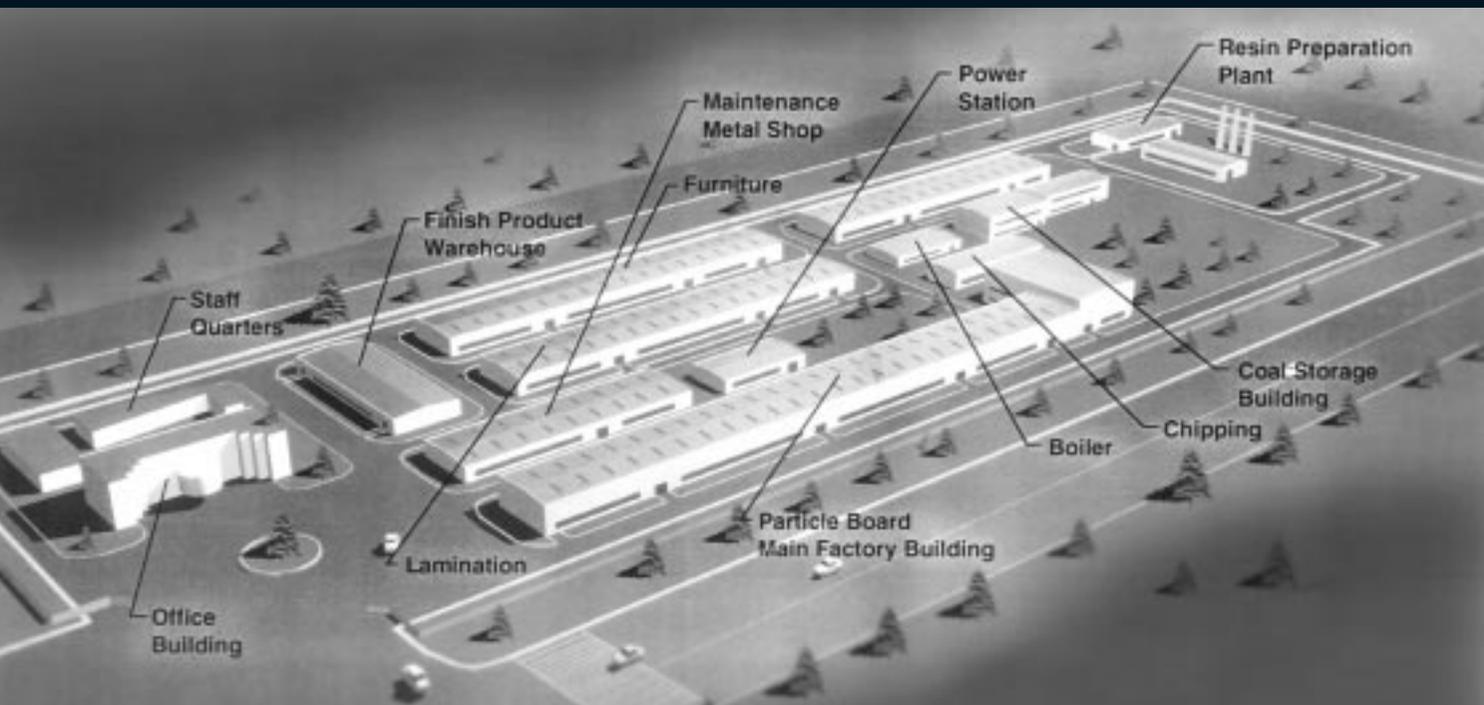
Sino-Forest is also realizing substantial benefits by applying modern biotechnology techniques to increase the productivity of our plantations; address environmental issues; improve our competitive position; and increase profits.

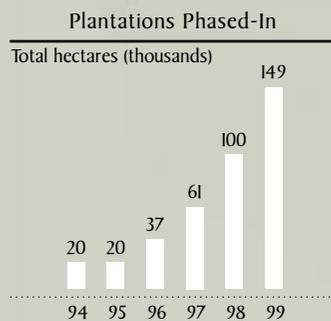
Lumber and engineered wood products trading

In 1999, in addition to significant growth from the continuing phase-in of our prime plantation lands, Sino-Forest increased earnings from our value-added wood products trading business.

To better serve the Asian market for engineered wood products, Sino-Forest is building a particle board mill. Situated in Guangdong Province (southern China), a major region for furniture manufacturing, the mill is expected to commence production in the second quarter of 2000. Outfitted with state-of-the-art Finnish equipment, the mill will be one of the most modern and largest engineered wood products processing facilities in China. With a production capacity of 100,000 cubic metres per year, the mill will serve as Sino-Forest's base for our wood-based panel production and

DESIGN CONCEPT FOR SINO-FOREST'S PARTICLE BOARD MILL IN GUANGDONG PROVINCE





expand our capabilities in the growing wood processing market.

The lumber and engineered wood products trading business diversifies Sino-Forest's revenue base; provides a high return; and further expands our position in the huge and rapidly growing Asian market for engineered wood products.

The Shanghai Timber Market provides us with a market for our wood products as well as being a source of a wide range of wood products from both Chinese and international markets. The market also facilitates networking opportunities for Sino-Forest and enables us to build new and beneficial industry relationships.

ASIAN MARKETS REMAIN STRONG

Pulp wood and engineered wood products demand in Asia is expected to remain strong in the next decade due to:

- projected economic growth;
- rising populations;
- higher living standards;
- increased literacy rates;
- further growth in office employment;
- increased demand for packaging products from manufacturing and agriculture sectors;
- aggressive housing development programs; and
- an increase in disposable income levels.

In fact, Asia has the greatest timber resource deficit of any region in the world as well as the highest growth in timber demand. This situation should mean increasing opportunities for Sino-Forest with our lower cost base plantations located near lucrative Asian markets.

In China in particular, over the past ten years, the Chinese government's Reform Program has transformed an old and inefficient state-controlled economy into a burgeoning, market-driven economy, which has created many profitable business opportunities.

GROWTH OPPORTUNITIES

Sino-Forest remains committed to becoming the dominant integrated forest products supplier and leader in practising sustainable forestry management throughout Asia. We plan to do this by vertically integrating our timber asset base (plantations) and our lumber and wood products trading business, and by leveraging our biotechnology, processing, information and logistics, and e-commerce capabilities.

Sino-Forest has consistently proven that it can successfully partner with China to combine considerable plantation management expertise; an understanding of the Chinese business culture and the society at large; as well as the application of Western business practices, into a co-operative and profitable business.



MARKET VALUATIONS

While Sino-Forest delivered yet another year of increased earnings and fully diluted earnings per share in 1999, the markets failed to recognize this value. To be frank, our Company is struggling as a resource investment in a “dot-com” world.

What we do offer that many of the dot-coms do not, however, is consistent earnings growth. In addition, as a Canadian listed public company, Sino-Forest offers Canadians an opportunity to hold a foreign investment in the growing Chinese and Asian economy without increasing the foreign content of their portfolios.

The market valuations that the Company has been experiencing have somewhat restricted the degree to which we have been able to expand our operations. For example, our plan to establish a wood-based panel manufacturing business has been delayed as we continue to explore options to develop this and other higher margin ventures.

With established contracts on prime plantation lands; a substantial technological infrastructure; skilled technical employees; fast-growing, renewable timber plantations; and low harvest and transportation costs, Sino-Forest meets all the requirements for long-term sustainable growth.

We remain committed to increasing shareholder value and are confident that the profitable growth that Sino-Forest has achieved is worthy of

recognition by the markets as we continue to focus on delivering solid results and impressive growth in the future.

THE TEAM

As a tree is only as strong as its roots, so too is Sino-Forest only as strong as its team. At Sino-Forest, I am proud to be part of an exceptional team of employees, management and corporate directors. I thank you all for your dedication and commitment to our common goals and recognize all that you have contributed to Sino-Forest's ongoing success.

As Sino-Forest enters the year 2000, which is also the Year of the Dragon, I would like to thank our shareholders and employees, for their continued support. The Dragon is believed to be a symbol of life and growth and is said to have the four blessings of virtue, riches, harmony and longevity. We wish these blessings for all of you in the year ahead.



Allen T.Y. Chan

Chairman and Chief Executive Officer



PRESIDENT'S MESSAGE

Launching from the plantation foundation established over the first six years of our operation, Sino-Forest has made the first step of whole tree utilization and value-added processing. Our particle board mill, which is situated in Guangdong Province (southern China), will commence production in the second quarter of year 2000. The mill will use state-of-the-art Finnish equipment to produce 100,000 cubic metres of particle board per year and will be one of the most modern and largest engineered wood products processing facilities in China. The mill will serve as Sino-Forest's development base for integration of trees and technology.

Kai Kit Poon
President

嘉漢在第五年成功建立了營林的基礎之後，過去一年，我們以此為基礎，踏上了全株利用、木材加工的第一步——位於廣東的嘉漢刨花板廠將於本年下半年正式生產。這個設備來自芬蘭，年產量十萬立方米的刨花板廠，中國最現代化、最大規模的木材加工廠之一，亦是嘉漢開展林工之林之新局的基地。

總裁
潘家偉
年

中國 業務回顧

CHINA

24 小時
BANKING
銀行服務

REVIEW OF OPERATIONS

It is not by chance that Sino-Forest chose Asia in which to establish its operations. Six years ago, Sino-Forest's management team recognized the growing demand for lumber and wood products by China, Japan, Taiwan and other parts of Asia.

Once China's forestry sector became open to foreign investment in 1993, Sino-Forest moved quickly to acquire the rights to prime plantation lands in China. In doing so, Sino-Forest became China's first foreign joint venture plantation operator. Sino-Forest has done this through the establishment of innovative Co-operative Joint Venture (CJV) partnerships in three provinces of southern China.

Sino-Forest chose China as the base for our plantations in order to capitalize on a growing demand for wood and wood products that far exceeds the supply.

We chose China for a number of other reasons as well:

- China's population of 1.2 billion is one of the largest and fastest growing populations in the world;
- Over the past 10 years, the Chinese government's Reform Program has transformed an old

and inefficient state-controlled economy into a burgeoning, market-driven economy;

- Over the past 20 years, China has established a solid commercial and industrial forest plantation base and infrastructure;
- China has increased its investments in infrastructure development (roads, railways, etc.) that will improve the efficiency and lower the cost of moving timber and wood products to market;
- Rising literacy rates and increased living standards have resulted in a growing demand for better quality housing, paper and other forest products;
- China has historically been a major importer of wood. Recently, supplies have been further restricted due to extensive flooding and the resulting 1998 ban on the logging of natural forests;
- Recent legislation that allows the Chinese to own their own homes will further support the market for building supplies; and
- China has indicated a strong commitment to accelerate economic reform with the signing of an agreement with the United States in late 1999 that will pave the way for China's entry into the World Trade Organization (WTO).



生 長 G R O W I N G

Sino-Forest's operations are structured around our "TTT" paradigm of trees, technology and trading. This paradigm merges traditional forestry practices with biotechnology techniques to produce products that are traded for resulting profits.

Sino-Forest's operations can be compared to the life cycle of the trees that are the foundation of our business. In three stages, this life cycle might be described as: growing, harvesting and sustaining.

Sino-Forest's operations consist of two main businesses: plantations (growing) and wood products trading (harvesting). Sustaining is the stage of the business cycle that ensures there is growth for the future — both the growth of trees and the growth of Company and shareholder investments.

Sino-Forest has the advantage of being the first foreign integrated forestry company established in China since the sector was opened to foreign investment in 1993. As such, the Company has put down roots in some of the prime plantation locations – with low labour costs and low transportation costs due to their close proximity to markets.

Sino-Forest's roots include five Co-operative Joint Ventures (CJVs) within the three southern Chinese provinces of Guangxi, Jiangxi, and Guangdong. All are strategically located close to the coast for ease of transportation of timber to market.

Sino-Forest was founded in 1994 with 20,000 hectares of plantation lands. By the end of 1998, part one of our plantation program had been com-

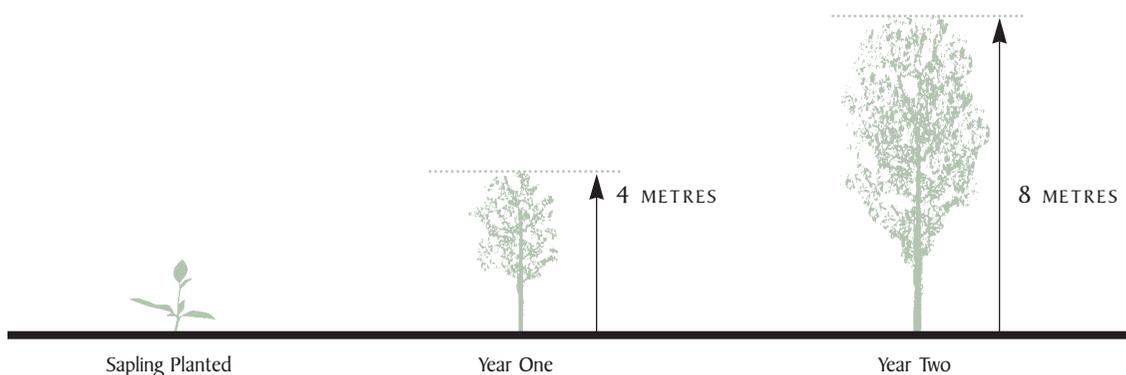
pleted, establishing a total of 100,000 hectares of plantation lands of genetically improved trees. Over the next few years, the remaining 503,000 hectares will be phased in so that by 2005, Sino-Forest will have a total of 603,000 hectares (approximately 1.5 million acres) of plantation lands under development.

These 603,000 hectares of plantation lands are expected to be fully productive by 2010, with one-sixth of the hectares available for harvesting each year. These plantations should then be able to generate a sustainable 10 million cubic metres of commercial/industrial wood fiber and logs, representing approximately 10 per cent of China's estimated potential requirement per year.

Sino-Forest's plantation program includes fast-growing aspen, eucalyptus and pine trees.

AVERAGE GROWTH RATE OF A EUCALYPTUS TREE IN CHINA

This illustration represents the growth rate to maturity of Sino-Forest's eucalyptus plantation trees.



Plantation forests have several advantages over natural forests; they have:

- much shorter growing seasons;
- more uniform timber;
- lower access and harvesting costs;
- better environmental performance; and
- better disease and fire protection.

The reason that plantation forests have these advantages is primarily due to the use of biotechnology techniques.

Sino-Forest's biotechnology expertise ensures that the plantation trees developed in laboratories and nurseries grow with improved quality, reduced cost, increased yield and environmentally positive results.

Biotechnology encompasses a range of technologies including genetic mapping, genetic engineering and propagation.

Genetic mapping allows commercially important characteristics such as growth rate, wood quality or drought tolerance to be identified and controlled. Similarly, genetic engineering allows for the introduction of a characteristic from another tree species in order to increase the level of plant tolerance to environmental stresses such as drought and salinity.

As well, since the improvements made to a single plant through genetic mapping or genetic engineering would be lost if that plant was propagated by seed, vegetative propagation provides the means to multiply a single elite plant many millions of times, so that it can be used for wide scale plantation establishment. Sino-Forest is using a micro-cutting propagation technique to rapidly multiply a single, genetically improved plant to provide millions of robust plants for plantation establishment in a relatively short time period and at competitive costs.

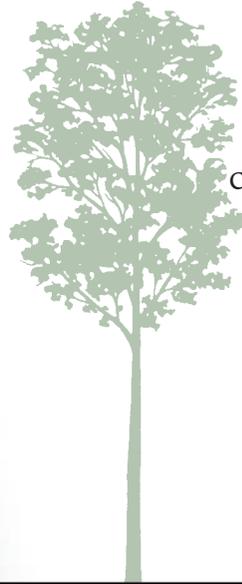
In short, biotechnology can produce larger size trees with better wood more quickly and more consistently. By growing more timber per hectare, the cost of production is reduced and profit increased. Also, less land is required to produce a given volume of timber, and this may allow sufficient timber supplies to be grown nearer to the mill, reducing the cost of log transportation, which represents a significant proportion of the cost of timber.

More uniform plantations increase harvesting efficiency; reduce waste; and provide higher quality timber for market. These improvements provide the basis for increased company profits, improved market competitiveness, and better use of resources.



收成 HARVESTING

Plantation Trees - Specifications and Characteristics



EUCALYPTUS

PLANTATION CYCLE:
5 years

COST OF PLANTATION PROGRAM:
US\$767 per hectare

STANDING TIMBER YIELD PER
HECTARE PER CYCLE:
90 cubic metres

AVERAGE ANNUAL GROWTH
RATE PER YEAR:
18 cubic metres

WOOD CHIP YIELD PER
HECTARE PER CYCLE:
40.2 BDMT

Sino-Forest will achieve greater profitability in the near future as its own plantations become harvestable and as its business becomes fully integrated to provide value-added products to the Chinese and the greater Asian marketplace. This is because the cost of wood from our plantations is approximately 20 per cent lower than the cost of logs purchased from the Co-operative Joint Venture (CJV) partners, and because wood products have higher profit margins than raw pulp or wood chips.

Sino-Forest's sustainable growth will come from our increasing capability to supply China and other Asian nations with:

- wood chips for pulp and paper production; and
- downstream, value-added, higher margin wood products such as particle board, doors, flooring and panelling for the construction and interior decoration market.

Integrating genetically improved and sustainably managed plantations with advanced wood utilization and processing technology is the right formula to optimize Sino-Forest's wood resources. Over the past six years, Sino-Forest has not only been selecting strategically located lands to phase

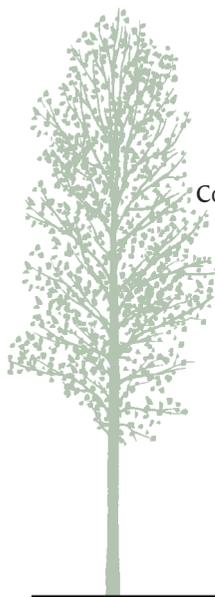
in; planting and harvesting trees; but also working quickly to establish all necessary sales, processing and distribution logistical support.

As a result, Sino-Forest has exceeded its 1999 target production of 2,000,000 BDMT of wood chips. The total 2,045,200 BDMT shipped in 1999 represents an increase of 1,209 per cent over 1994 production levels of 156,300 BDMT of wood chips shipped and an increase of 28 per cent over the 1,603,900 BDMT of wood chips shipped in 1998. The 2,045,200 BDMT of wood chips shipped by Sino-Forest in 1999 generated revenue of \$104.3 million, 74 per cent of total revenues.

There are also promising growth opportunities as Sino-Forest's investment in Shanghai Jin Xiang Timber Ltd. (SJXT or the Shanghai Timber Market), develops. The Company also continues to explore opportunities to establish and reinforce ties with other international forestry companies and to bring our e-commerce technology into operation.

Sino-Forest's investment in the Shanghai Timber Market — the first national forest products sub-market in eastern China — has provided a strong foundation for the Company's lumber and wood products trading business.

To date, the timber market has been a significant



ASPEN

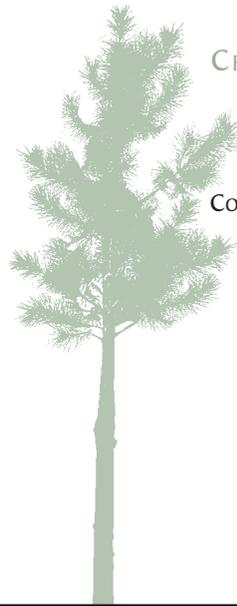
PLANTATION CYCLE:
5 years

COST OF PLANTATION PROGRAM:
US\$1,005 per hectare

STANDING TIMBER YIELD PER
HECTARE PER CYCLE:
128 cubic metres

AVERAGE ANNUAL GROWTH
RATE PER YEAR:
25.6 cubic metres

WOOD CHIP YIELD PER
HECTARE PER CYCLE:
42 BDMT



CHINA SOUTHERN PINE

PLANTATION CYCLE:
12 years

COST OF PLANTATION PROGRAM:
US\$704 per hectare

STANDING TIMBER YIELD PER
HECTARE PER CYCLE:
135 cubic metres

AVERAGE ANNUAL GROWTH
RATE PER YEAR:
11.25 cubic metres

WOOD CHIP YIELD PER
HECTARE PER CYCLE:
52 BDMT

source of new revenue for Sino-Forest, both as a way to market our products and a way to source a wide range of other wood products from inside China and internationally. Sino-Forest's lumber and wood products trading business generated revenue of \$37.2 million for the Company in 1999. This represents an increase of 219 per cent over the \$11.7 million in revenues generated in 1998 and an increase of 1,591 per cent over the \$2.2 million in revenues generated in 1994.

Going forward, Sino-Forest will continue to diversify our revenue base by vertically integrating our operations; growing our timber asset base; and by increasing our activities in the higher margin lumber and wood products processing and trading business.

One of the most significant opportunities emerging in the forestry industry in China is the use of eucalyptus timber for production of high value, solid wood products such as lumber and veneers for plywood. Globally, solid wood products represent one of the fastest growing segments of the wood trade market. And, with the reduced availability and acceptability of logs from tropical rain forests, there is an increasing demand for timber produced from sustainably managed plantations.

This new application for eucalyptus timber presents a major opportunity for Sino-Forest to capture a substantial proportion of the emerging market for solid wood products and to increase profits through conversion of timber to higher value applications.

To better serve this market, Sino-Forest is building a particle board mill, which is expected to commence production in the second quarter of 2000. Situated in Guangdong Province (southern China), a major region for furniture manufacturing, the mill will have a production capacity of 100,000 cubic metres and serve as Sino-Forest's base from which to expand our capabilities in the growing wood processing market.

For the year 2000, which is also the Year of the Dragon symbolizing life and growth, Sino-Forest will further develop our information technology capacity, including significant e-commerce technology, to bring our operations and products closer to our customers. By applying modern biotechnology techniques to its plantation operations, Sino-Forest will lead China's forestry industry in today's technological revolution as we continue to expand our plantations and processing operations.

持續

S U S T A I N I N G



Just as a healthy forest is sustainable when managed properly, Sino-Forest's management team is ensuring that the business it is growing is a sustainable one for the community, the environment and investors.

Sino-Forest's employees are an essential part of the Sino-Forest team – this dedicated team ensures the continuity and excellence necessary to maintain a viable long-term business.

Sino-Forest has Co-operative Joint Venture (CJV) agreements with various state-owned forestry bureaus in the three southern Chinese provinces of Guangxi, Jiangxi and Guangdong whereby the bureaus provide the land use rights and planting, maintenance and harvesting services, and Sino-Forest provides the capital to plant and manage the plantations.

The agreements include 50-year plantation

leases that give Sino-Forest the right to 70 per cent of the timber and first right of refusal on the remaining 30 per cent of timber.

Sino-Forest's approach with each CJV is to work with the best and most knowledgeable staff of the local forestry bureaus. This partnership combines the bureaus' expertise with Sino-Forest's equipment, money and modern techniques to produce high standards, long-term relationships and impressive results.

As well as making the best use of existing expertise, Sino-Forest is actively introducing up-to-date international research to our operations in order to maintain our leadership position in the forestry industry in China.

Sino-Forest's ISO 9002 Quality Management System certification for its Guangxi CJV plantation operation further confirms our high standards in managing and operating our plantations.



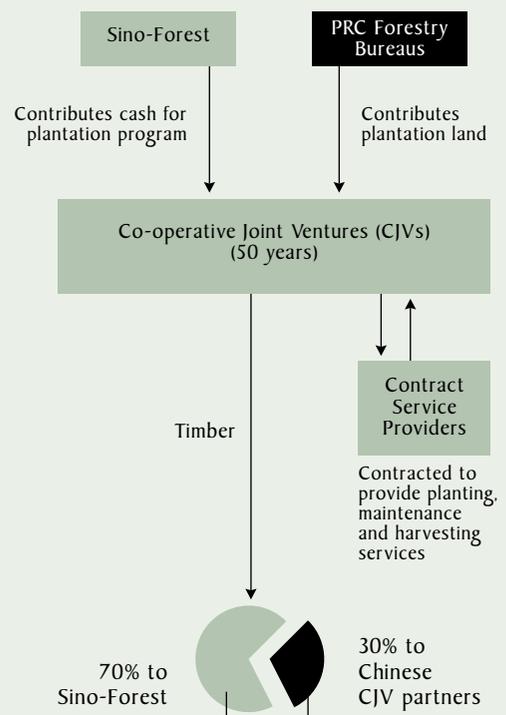
In turn, as we draw our success from the environment, Sino-Forest has been following sound environmental practices.

Recognizing that the continuing profitability and prosperity of the Company, its employees and the community in which we operate is dependent upon long-term environmental health sustained by sound economic development, Sino-Forest has established an environmental management system (EMS).

The objective of Sino-Forest's EMS is to strive for excellence, leadership, sustainability and continuous improvement in environmental performance.

With established prime plantation leases; a substantial technological infrastructure; skilled technical employees; fast-growing, renewable timber plantations; and low harvest and transportation costs, Sino-Forest has all the elements in place for long-term sustainable growth — of its trees, its people and its business.

Sino-Forest's Co-operative Joint Venture (CJV) Structure





1999 FINANCIAL REPORT

MANAGEMENT'S DISCUSSION AND ANALYSIS

[All amounts are expressed in U.S. dollars, unless otherwise indicated.]

REVIEW OF OPERATING RESULTS

A summary of the results of operations of the Company by segment for the years ended December 31, 1999 and 1998 is as follows:

	Year ended December 31, 1999			Year ended December 31, 1998		
	[Thousands of U.S. dollars]					
	Wood Chips \$	Wood- Based & Other \$	Total \$	Wood Chips \$	Wood- Based & Other \$	Total \$
Revenue						
Sales	89,503	34,162	123,665	66,793	9,368	76,161
Commission income	14,827	3,085	17,912	14,228	2,321	16,549
	104,330	37,247	141,577	81,021	11,689	92,710
Income from operations	28,463	5,168	33,631	21,213	2,833	24,046

Income from operations for the year ended December 31, 1999 was \$33.6 million, an increase of 40% compared to income from operations of \$24.0 million for 1998. Earnings per share on a fully diluted basis, which assumed the full conversion of the Exchangeable Notes, also increased 19% to \$0.31 per share compared to \$0.26 per share attained in 1998. Income for the wood chip operations increased by 34% from \$21.2 million in 1998 to \$28.5 million in 1999. Income from wood-based and other business increased by 86% to \$5.2 million compared to \$2.8 million in 1998 as a result of the increase in business from principal trading of lumber and wood products. The significant increase in earnings for the wood chip operations is primarily attributable to the continuing increase in wood chip shipments in 1999, which is in line with the Company's planned phase-in of the contractual plantation lands and an increase in principal sales. Sales from lumber and wood products trading increased 264% to \$34.2 million compared to \$9.4 million in 1998. The increase in lumber and wood

products trading is attributable largely to the increase in new business generated from our investment in Shanghai Jin Xiang Timber Ltd. (SJXT) and a larger sales force in 1999. Lumber and wood products trading on an agency basis has increased 35% from \$2.3 million in 1998 to \$3.1 million in 1999. The increase in commission income on lumber and wood products trading is attributable to approximately \$1.8 million of fees earned from a new customer.

In 1999, wood chip and log shipments totalled 2,045,200 Bone Dry Metric Tonnes (BDMT) compared to 1,603,900 BDMT shipped in 1998, an increase of approximately 28%. Of the total wood chips and logs shipped in 1999, 123,000 BDMT were exported to Japan and Taiwan and 1,922,200 BDMT were sold in the domestic PRC market. Export and domestic shipments for 1998 were 245,500 BDMT and 1,358,400 BDMT, respectively. For the year ended December 31, 1999, the Company acted as principal on 1,036,500 BDMT compared to 664,500 BDMT in 1998, an increase of 56%. Export shipments have decreased approximately 50% from 245,500 BDMT in 1998 to 123,000 BDMT in 1999 as a result of the continuing weak economy in Japan. Demand for wood chips and logs in China remains strong and was the reason for the increase in shipments from 1,358,400 BDMT in 1998 to 1,922,200 BDMT in 1999, an increase of 42%.

A summary of the wood chip and log shipments for the year ended December 31, 1999 compared to 1998 is set out in the table below.

Wood Chip and Log Shipments for the Year Ended December 31						
[Thousands of BDMT]						
Market	Principal		Agency		Total	
	1999	1998	1999	1998	1999	1998
Export	12.0	—	111.0	245.5	123.0	245.5
PRC domestic	1,024.5	664.5	897.7	693.9	1,922.2	1,358.4
Total	1,036.5	664.5	1,008.7	939.4	2,045.2	1,603.9

Included in the 1,036,500 BDMT of wood chip shipments made on a principal basis in 1999 were 325,420 BDMT of wood chips that were sold to a new customer. Under the sales arrangement with this new customer, transportation and delivery charges were to be borne by the customer resulting in a reduction in the selling price to approximately \$78.50 per BDMT compared to the average selling price in 1999 of approximately \$95.00 per BDMT. Although revenue recorded by the Company for this new customer in 1999 is lower by approximately \$5.4 million, the profit has remained the same at approximately \$20.00 per BDMT.

The average price of wood chips, net of VAT, in 1999 was reduced to \$95.00 per BDMT from \$100.00 per BDMT attained in 1998. With respect to sales in which the Company acted as an agent, the Company earned an average of \$14.70 per BDMT in 1999 compared to \$15.15 per BDMT earned in 1998.

Investment in SJXT

The Company held a 34.4% equity interest in SJXT, an equity joint venture (EJV) that was formed by the Ministry of Forestry in China. The purpose of the investment is to establish strategic partnerships with key local wood products suppliers and to build a strong distribution network for the lumber and wood products trading and the wood-based panel businesses. The total capital investment of SJXT is \$1,509,000 [Chinese renminbi 12.5 million] of which the Company's required capital contribution is \$519,000. As at December 31, 1999, the Company's required capital contribution of \$519,000 was fully made.

The operation of SJXT is to organize and manage the first and only national sub-market for timber and log trading in eastern China. The investment in SJXT will provide the Company with accessibility to a large base of potential customers and companies in the timber and log businesses in eastern China. The investment in SJXT has contributed to the significant growth of the lumber and wood products trading business, which has recorded an increase in sales of 219% from \$11.7 million in 1998 to \$37.2 million in 1999.

Investment in wood-based panel

The Company is in the process of establishing a wood-based panel manufacturing business for the sale of value-added wood products in the PRC. These operations, when implemented, will be carried out through Sino-Panel (Gaoyao) Limited ["Sino-Panel"], a wholly owned subsidiary of the Company. Sino-Panel has established an EJV with a local PRC company in which Sino-Panel's equity interest in this EJV is 85%. Under the EJV agreement, the EJV is formed for a 50-year period and Sino-Panel is required to contribute \$10,064,000 for its 85% equity interest, of which \$1,510,000 was required to be made within three months from the date of issue of business licence. The remaining capital contribution of \$8,554,000 is to be contributed depending on the needs of the EJV operation. Sino-Panel's capital contribution commitment was fully satisfied in 1998 by the contribution of certain machinery and equipment to the EJV with an aggregate value of approximately \$11,021,000.

Subsequent to the year-end, the EJV was converted to a wholly foreign-owned enterprise (WFOE) as a result of the PRC EJV partner's voluntary withdrawal of its entire equity interest in the EJV. The conversion from an EJV to a WFOE was approved by the Commission of Foreign Trade and Economic Co-operation (CFTEC) in February 2000.

The establishment of the wood-based panel manufacturing facility is expected to be completed by the end of the second quarter of 2000.

During the fourth quarter of 1999, the Company has also acquired certain machinery and equipment in the amount of approximately \$8,500,000 for the purpose of establishing a flooring factory with a production capacity of approximately 100,000 m²

per annum, a sawmill with a production capacity of 100,000 m³ per annum, and an oriented strand board (OSB) mill with a production capacity of 15,000 m³ per annum. This machinery and equipment is presently being refurbished before installation and is expected to be installed and operational by the end of the second quarter of 2000.

LIQUIDITY AND CAPITAL RESOURCES

Cash flows from operations in 1999 were \$27.1 million, which together with the net proceeds of approximately \$37.3 million from financing activities were sufficient to finance cash investment in capital assets of \$27.5 million in 1999. Investment in capital assets is largely made up of plantation costs, acquisition of young trees, and purchase of machinery and equipment.

As at December 31, 1999, the Company had cash of \$39.6 million and approximately \$11.1 million of unutilized bank credit facilities. As at December 31, 1999, the Company's total debt (excluding the equity component of the Exchangeable Notes) was \$35.1 million, compared with \$5.7 million at the end of 1998. The increase in debt was primarily due to the issuance of the Exchangeable Notes and an increase in long-term debt and bank borrowings. On December 31, 1999, the Company's debt to equity ratio was 0.28:1 compared with 0.07:1 at the end of 1998.

Cash in hand of \$39.6 million and the unutilized credit facilities available at year-end will be sufficient to meet all the planned capital expenditures for the year 2000, including the announced share repurchase program.

Capital contribution commitments

Sino-Wood (a subsidiary of Sino-Forest) has subsidiaries that are committed to contribute an aggregate of \$14,200,000 of capital to the five existing co-operative joint ventures (CJVs), which was subsequently increased to \$17,650,000 upon approval by the CFTEC in 1999. As at December 31, 1999, a total capital contribution of \$10,825,000 had been made. Accordingly, the remaining capital contribution outstanding as at December 31, 1999 is \$6,825,000. During the year, the Company decided not to proceed with its investment in one of the CJVs. The Company is in the process of dissolving this CJV and accordingly, the required capital contribution of \$1,375,000 to this CJV was not made.

In 1999, a subsidiary of the Company established a WFOE to facilitate the establishment of the wood-based manufacturing business in the Greater Shanghai Region. The WFOE is formed for a period of 30 years and the subsidiary is required to contribute \$10.0 million for its 100% equity interest, of which \$1.5 million was required to be made within three months from the date of issue of business licence. The remaining capital contribution of \$8.5 million is required to be made within one year. The initial capital contribution of \$1.5 million was made within the required time frame.

In 1999, Leizhou EJV was converted to a WFOE as a result of the Leizhou

Forestry Bureau's [the "LFB"] voluntary withdrawal of its entire equity interest in Leizhou EJV. The conversion from an EJV to a WFOE was approved by the CFTEC in May 1999. Sino-Wood is required to contribute \$10.0 million for its 100% equity interest, of which \$1.5 million is required to be made within three months from the issue of business licence. Sino-Wood has applied to reduce the original total capital contributions of \$10.0 million to \$1.4 million. As at December 31, 1999, no capital contributions have been made by the Company pending approval of the reduction in total capital contributions.

Outlook

The Company enters the year 2000 with strong fundamentals and is well positioned to continue meeting its plantation program of phasing in the remainder of the 603,000 hectares of contractual plantation lands by year 2005.

The demand for wood chips in the domestic market (PRC) remains strong despite an economic slowdown in 1999. Paper and board consumption in China will continue to increase as a result of population growth, increasing literacy rates and the conversion of non-wood pulp to traditional wood pulp. It is expected that the supply of wood chips in China over the next decade will lag behind the projected strong growth in demand for wood chips.

China's average annual paper consumption per capita is only 26 kg, which is less than half the global average of 55 kg and far less than the over 300 kg per person in the United States. Over the last ten years, China's consumption of paper and paper-based products has increased by more than 10% annually, which is more than twice the average global growth rate of 3.1%. In 1998, China produced 28 million tons of wood-based paper and cardboard, the third largest output in the world. According to a recent study by Japan's Paper and Pulp Industry, China's paper demand in the year 2000, based on the growth rate of its current gross domestic product, is estimated to reach 36.5 million tons, surpassing Japan's demand of 32.9 million tons. Even at this estimated level of 36.5 million tons, average annual paper consumption per person in China is only 28 kg, far less than the average consumption per person in developed countries.

As our trees begin to mature in the next few years, the Company expects to realize higher margins on its wood chip sales. The Company also plans to find "value-added" uses for the increasingly large volume of timber that it produces. The plan to establish the wood-based panel manufacturing business is a natural extension of our plantation business. The establishment of the wood-based panel manufacturing business will allow Sino-Forest to capitalize on the fast growing panel business in China and become a major player in China's forestry industry.

MANAGEMENT'S REPORT

The consolidated financial statements contained in this Annual Report have been prepared by management in accordance with generally accepted accounting principles. The financial information contained elsewhere in the Annual Report is consistent with the consolidated financial statements.

Management maintains systems of internal accounting and administrative controls to provide reasonable assurance as to the reliability of the financial records and the safeguarding of the Company's assets.

The Audit Committee, which is mainly comprised of outside directors, meets periodically with management to discuss the adequacy of the system of internal controls and the integrity of the Company's financial reporting.

The consolidated financial statements have been reviewed by the Audit Committee prior to submission to the Board of Directors. The consolidated financial statements have also been audited by Arthur Andersen LLP, who have full access to the Audit Committee, with and without the presence of management, to discuss the scope of their audit, the adequacy of the system of internal controls and the adequacy of financial reporting.



Allen T. Y. Chan

Chairman and
Chief Executive Officer



Kee Y. Wong

Executive Vice-President and
Chief Financial Officer

AUDITORS' REPORT

To the Shareholders of
Sino-Forest Corporation

We have audited the consolidated balance sheets of **Sino-Forest Corporation** as at December 31, 1999 and 1998, and the consolidated statements of income, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1999 and 1998, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Toronto, Canada
April 28, 2000



Chartered Accountants

CONSOLIDATED BALANCE SHEETS

[Expressed in thousands of U.S. dollars]

As at December 31	1999	1998
	\$	\$
ASSETS		
Current		
Cash and cash equivalents	39,591	912
Accounts receivable [note 3]	15,926	2,643
Due from PRC CJV partners [note 6]	3,275	11,748
Other receivables and prepaid expenses	1,819	1,929
Total current assets	60,611	17,232
Capital assets, net [note 4]	113,907	78,880
Deferred financing costs	1,783	—
SJXT Investment [note 2(b)]	1,315	1,037
Jiangxi Investments [note 2(c)]	624	1,070
Goodwill, net	31	32
Deposits [note 5]	—	2,250
	178,271	100,501
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities	9,222	5,396
Income taxes payable	7,764	4,227
Bank indebtedness [note 7(d)]	4,127	1,997
Current portion of long-term debt [note 7]	742	370
Total current liabilities	21,855	11,990
Long-term debt [note 7]	30,218	3,340
Total liabilities	52,073	15,330
Commitments [notes 2 and 12]		
Shareholders' equity		
Share capital [note 8]	46,273	32,989
Retained earnings	79,925	52,182
Total shareholders' equity	126,198	85,171
	178,271	100,501

See accompanying notes

On behalf of the Board:



Allen T. Y. Chan
Director



William Rosenfeld
Director

CONSOLIDATED STATEMENTS OF INCOME

[Expressed in thousands of U.S. dollars, except for earnings per share information]

Years ended December 31	1999	1998
	\$	\$
Revenue	141,577	92,710
Costs and expenses		
Cost of sales	101,794	62,675
Selling, general and administration	6,065	5,898
Depreciation and amortization	87	91
	107,946	68,664
Income from operations	33,631	24,046
Interest expense, net	(1,424)	(9)
Equity in losses of Jiangxi Investments [note 2(c)]	(235)	(430)
Write-off of Jiangxi Investments [note 2(c)]	(211)	—
Amortization of deferred financing costs	(69)	—
Income before income taxes	31,692	23,607
Provision for income taxes - current [note 9]	(3,537)	(2,243)
Net income for the year	28,155	21,364
Earnings per share [note 10]		
Basic	\$0.37	\$0.29
Fully diluted	\$0.31	\$0.26

See *accompanying notes*

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

[Expressed in thousands of U.S. dollars]

Years ended December 31	1999	1998
	\$	\$
Retained earnings, beginning of year	52,182	30,818
Net income for the year	28,155	21,364
Interest on equity component of Exchangeable Notes	(412)	—
Retained earnings, end of year	79,925	52,182

See *accompanying notes*

CONSOLIDATED STATEMENTS OF CASH FLOWS

[Expressed in thousands of U.S. dollars]

Years ended December 31	1999	1998
	\$	\$
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income for the year	28,155	21,364
Add (deduct) items not affecting cash		
Reduction in amount due from CJV partners		
in exchange for timber holdings	(10,134)	(7,770)
Depletion of timber holdings included in cost of sales	2,526	—
Accretion of Exchangeable Notes	1,402	—
Interest on equity component of Exchangeable Notes	(412)	—
Equity in losses of Jiangxi Investments	235	430
Write-off of Jiangxi Investments	211	—
Depreciation and amortization	87	91
Amortization of deferred financing costs	69	—
	22,139	14,115
Net change in non-cash working capital balances	4,913	1,202
Cash flows from operating activities	27,052	15,317
CASH FLOWS FROM FINANCING ACTIVITIES		
Issuance of share capital, net	18	687
Issuance of equity component of Exchangeable Notes, net	13,266	—
Issuance of long-term debt, net	24,738	—
Repayment of long-term debt	(742)	—
Cash flows from financing activities	37,280	687
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment in capital assets	(27,505)	(22,880)
Investment in SJXT	(278)	—
Cash flows used in investing activities	(27,783)	(22,880)
Effect of exchange rate changes on cash	—	108
Net increase (decrease) in cash and cash equivalents during the year	36,549	(6,768)
Cash, cash equivalents and bank indebtedness, beginning of year	(1,085)	5,683
Cash, cash equivalents and bank indebtedness, end of year	35,464	(1,085)
SUPPLEMENTAL DISCLOSURE		
Cash payment for interest charged to income	845	60
Cash payment for interest capitalized	216	254

See accompanying notes

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

[Tabular figures expressed in thousands of U.S. dollars, unless otherwise indicated]

I. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements of Sino-Forest Corporation [“Sino-Forest” or the “Company”] have been prepared in U.S. dollars and in accordance with accounting principles generally accepted in Canada. The significant accounting policies are as follows:

Basis of consolidation

These consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated on consolidation.

The Company’s investments in Sino-foreign co-operative joint ventures [each a “PRC CJV”, collectively, the “PRC CJVs”] are accounted for on the proportionate consolidation basis. Accordingly, the accounts reflect the Company’s pro-rata share of the assets, liabilities, revenue, expenses and cash flows of its PRC CJVs.

The Company’s investments in wholly foreign-owned enterprises [“WFOEs”] and Sino-foreign equity joint ventures and equity joint ventures [collectively, the “EJVs”], which are controlled by the Company, are accounted for on the consolidation basis. Investments in EJVs over which the Company exercises significant influence are accounted for under the equity method.

Translation of foreign currencies

Foreign currency transactions and balances, and the financial statements of integrated foreign operations, are translated into U.S. dollars using the temporal method. Under this method, monetary items are translated at the rate of exchange in effect at the consolidated balance sheet dates. Non-monetary items are translated at the historical exchange rate. Revenue and expense items are translated at the average exchange rates prevailing during the year, except for depreciation, amortization and depletion which are translated at the same exchange rates as the assets to which they relate. Exchange gains and losses are included in income in the current year.

Capital assets

Timber holdings include acquisition costs for young trees and standing timber and planting, maintenance and harvesting costs, which are capitalized over a period of 5 to 12 years based on the growth cycle of the type of trees. Timber holdings are depleted when the trees are harvested on the basis of the volume of timber cut.

Other capital assets are recorded at cost including interest capitalized on assets under construction. Repairs and maintenance expenditures are charged to income; major betterments and replacements are capitalized. Depreciation and amortization are provided on a straight-line basis to reduce the original cost of capital assets to estimated residual values over the following estimated useful lives:

Machinery and equipment	15 years
Office furniture and equipment	5 to 10 years
Vehicles	5 to 10 years

Deferred financing costs

Financing costs relating to the issuance of Exchangeable Notes and Plantation Loan are deferred and amortized over the lives of the Notes or Loan on a straight-line basis.

Goodwill

Goodwill is amortized over 40 years on a straight-line basis.

Revenue recognition

Revenue from the sale of wood chips and other products is recognized when the products are shipped. Commission income relating to wood chip and other product sales is recognized as revenue when the products are shipped and services rendered.

Income taxes

Income taxes are accounted for using the deferral method. Under this method, timing differences between accounting and taxable income result in deferred income taxes.

Use of estimates

The preparation of consolidated financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses for the period reported. Actual results could differ from those estimates.

Fair value of financial instruments

The Company estimates the fair value of its financial instruments based on current interest rates, market value and the current price of financial instruments with similar terms. Unless otherwise disclosed herein, the carrying value of financial instruments, especially those with current maturities such as cash, accounts receivable and accounts payable, is considered to approximate their fair value.

Stock-based compensation plan

The Company has a stock option plan, which is described in note 8. No compensation expense is recognized for this plan when stock options are issued. Any consideration paid on the exercise of stock options is credited to share capital.

Interest rate and currency contracts

The differentials to be received or paid under interest rate and currency contracts are recognized in income as adjustments to interest expense. Premiums paid on contracts are deferred and amortized to income over the remaining life of the contracts.

2. ORGANIZATION AND OPERATIONS

The Company's principal business activities include the management and operation of tree plantations in the People's Republic of China [the "PRC"] and sales and trading of logs, lumber, wood chips and wood-based products in the PRC, and other Asia-Pacific markets. Apart from these, the Company also provides agency services for the sale of logs, lumber and wood chips in the PRC and other Asia-Pacific markets. Details of the Company's principal business activities are as follows:

[a] Tree plantation and wood chip operations

In 1995, the Company, through wholly-owned subsidiaries of Sino-Wood Partners, Limited ["Sino-Wood"], entered into agreements to form five PRC CJVs. Under the terms of the agreements, the CJV partners are required to provide the PRC CJVs with land use rights for up to 603,000 hectares of land for tree plantations. The land use rights are for a period of 50 years and will be phased in over a number of years. Sino-Wood's subsidiaries are responsible for providing funds to the PRC CJVs for all planting, maintenance and harvesting costs incurred on the phased-in land. The subsidiaries are entitled to 70% of the timber harvested on the phased-in land and the CJV partners are entitled to the balance. The CJV partners retain ownership of the land use rights and, accordingly, no value is assigned to the land use rights for accounting purposes.

Sino-Wood's subsidiaries were committed to contribute an aggregate of \$14,200,000 of capital to the five PRC CJVs, which was subsequently increased to \$17,650,000. The increase in capital contribution was approved by the Commission of Foreign Trade and Economic Co-operation in 1999. Up to December 31, 1999, the Company had made capital contributions of \$10,825,000 to meet costs for planting, maintenance and harvesting of the PRC CJVs' tree plantations. Accordingly, the outstanding capital contribution required with respect to these five PRC CJVs as at December 31, 1999 is \$6,825,000. In 1999, the Company decided not to proceed with its investment in one of the PRC CJVs. The Company is in the process of dissolving this PRC CJV and accordingly, the required capital contribution of \$1,375,000 was not made.

The major components of the Company's interests in these five PRC CJVs are as follows:

	1999	1998
	\$	\$
Consolidated balance sheets		
Current assets	11,090	1,848
Long-term assets	13,644	8,621
Current liabilities	(4,182)	(1,000)
Long-term liabilities	(8,000)	—
Consolidated statements of income		
Revenue	—	—
Costs and expenses	—	—
Net income	—	—
Consolidated statements of cash flows		
Cash flows from financing activities	12,234	1,678
Cash flows used in investing activities	(3,792)	(1,928)

A subsidiary of the Company has made an arrangement with its CJV partner in Heyuan [the “Partner”] pursuant to which the subsidiary purchased timber from the Partner and contracted the Partner to process the timber into wood chips. As part of the arrangement, the Partner agreed to act as the subsidiary's agent to sell wood chips in the PRC for a fee equal to 15% of the net profit of the sales. During 1999, the sale of wood chips and the purchase of timber and chipping charges under this arrangement totalled \$57,386,000 [1998 – \$66,793,000] and \$45,242,000 [1998 – \$53,819,000], respectively.

This subsidiary of the Company also purchased wood chips from its CJV partners in Guangxi and Heyuan amounting to approximately \$8,510,000 [1998 – \$nil] and \$13,109,000 [1998 – \$nil], respectively.

In addition, the Company also earned commission income from a PRC CJV partner in Guangxi amounting to approximately \$14,827,000 [1998 - \$14,228,000].

During the year, Leizhou EJV was converted to a WFOE as a result of the Leizhou Forestry Bureau's [the “LFB”] voluntary withdrawal of its entire equity interest in Leizhou EJV. The conversion from an EJV to a WFOE was approved by the Commission of Foreign Trade and Economic Co-operation in May 1999. Sino-Wood is required to contribute \$10,000,000 for its 100% equity interest, of which \$1,500,000 is required to be made within three months from the issue of business licence. Sino-Wood has applied to reduce the original total capital contributions of \$10,000,000 to \$1,400,000. As at December 31, 1999, no capital contributions have been made by the Company pending approval of the reduction in total capital contributions.

[b] Wood-based panel and other operations

In June 1997, Sino-Panel (Gaoyao) Limited [“Sino-Panel”], a wholly-owned subsidiary of the Company, established an EJV with a local PRC company. Sino-Panel has an 85% equity interest in this EJV. The principal business activity of this EJV is

to be the manufacture of wood-based panels. Under the EJV agreement, the EJV is formed for a period of 50 years and Sino-Panel was required to contribute \$10,064,000 for its 85% equity interest in the EJV, of which \$1,510,000 was required to be made within three months from the date of issue of business licence. The remaining capital contribution of \$8,554,000 has to be contributed depending on the needs of the EJV operation. Sino-Panel's capital contribution commitment was fully satisfied in 1998 by the contribution of certain machinery and equipment to the EJV with an aggregate value of approximately \$11,021,000. Subsequent to year-end, the EJV was converted to a WFOE as a result of the PRC EJV partner's voluntary withdrawal of its entire equity interest in the EJV. The conversion from an EJV to a WFOE was approved by the Commission of Foreign Trade and Economic Co-operation in February 2000.

During the year, Shanghai Jin Xiang Timber Ltd. ["SJXT"] applied to increase the original total capital contributions of \$868,000 [Chinese renminbi 7.2 million] to \$1,509,000 [Chinese renminbi 12.5 million]. Sino-Wood is required to make an additional contribution of \$278,000 as a result of the increase in total capital contributions. The additional capital contribution of \$278,000 was made in 1999 increasing its equity interest in SJXT from 27.8% to 34.4%. The principal activity of SJXT is to organize trading of timber and logs in the PRC market.

As at December 31, 1999, \$796,000 [1998 – \$796,000] advances to SJXT remained outstanding. The advances to SJXT were unsecured, non-interest bearing and without a fixed repayment date.

In July 1999, SFR (China) Inc. ["SFR China"], a wholly-owned subsidiary of the Company, established a WFOE. The principal business activity of the WFOE is to manufacture wood-based panels. The WFOE is formed for a period of 30 years and SFR China is required to contribute \$10,000,000 for its 100% equity interest, of which \$1,500,000 was required to be made within three months from the date of issue of business licence. The remaining capital contribution of \$8,500,000 has to be contributed within one year. As at December 31, 1999, the Company has made contributions in the amount of \$1,500,000 [1998 – \$nil].

[c] Forestry chemical operations

Sino-Wood held a 30% equity interest in each of the four forestry chemical and one wood-based panel EJVs [collectively, the "Jiangxi Investments"]. As a result of continuous losses in two of the Jiangxi Investments in the forestry chemical business, the Company decided to write off the remaining value of these two investments totalling \$211,000 [1998 – \$nil]. The carrying value of the remaining three Jiangxi Investments amounted to approximately \$624,000 [1998 – \$859,000] as at December 31, 1999.

3. ACCOUNTS RECEIVABLE

The Company reviews its outstanding accounts receivable and records an allowance for doubtful accounts when accounts are determined to be uncollectable. As at December 31, 1999 and 1998, no allowance had been recorded by the Company. Accounts receivable as at December 31, 1999 included \$11.7 million due from one customer [1998 – \$1.7 million].

4. CAPITAL ASSETS

Capital assets consist of the following:

	1999		1998	
	Cost	Accumulated depreciation and amortization	Cost	Accumulated depreciation and amortization
	\$	\$	\$	\$
Timber holdings	91,684	—	67,332	—
Machinery and equipment	21,710	—	11,021	—
Office furniture and equipment	529	264	520	192
Vehicles	362	114	255	56
	114,285	378	79,128	248
Less accumulated depreciation and amortization	(378)		(248)	
Net book value	113,907		78,880	

Timber holdings include 664,333 cubic metres [1998 – 730,440 cubic metres] of standing timber valued at \$11,305,000 [1998 – \$12,430,000] to be provided by the LFB to Sino-Wood as part of an agreement executed in April 1998 to exchange Sino-Wood's interest in the net assets of Leizhou EJV. The standing timber is to be provided by the LFB over a three-year period as required by Sino-Wood. Sino-Wood is responsible for harvesting and transportation costs. During the year, 66,107 cubic metres of standing timber were delivered to Sino-Wood by the LFB.

Machinery and equipment amounting to approximately \$21,710,000 [1998 – \$11,021,000] is not being depreciated as the production facilities are under construction and installation and have not yet been put into operation.

5. DEPOSITS

In 1998, the Company, through two of its PRC CJV partners, entered into an agreement with chipping plant operators to acquire equity interests in their facilities. Under the terms of the agreement, the Company provided a deposit of \$2,250,000, to be applied against the Company's future investment. In 1999, the Company decided not to proceed with the investment in these facilities. The deposits were applied against the Company's purchase of logs and wood chips from these PRC CJV partners.

6. DUE FROM PRC CJV PARTNERS

The amounts due from PRC CJV partners relate primarily to commission income and accounts receivable related to wood chip trading and sales [see note 2(a)] and for reimbursement of office expenses. The amounts are unsecured, non-interest bearing and without pre-determined terms of payment.

7. LONG-TERM DEBT

	1999	1998
	\$	\$
Equipment Loan	2,968	3,710
Debt component of Exchangeable Notes	7,992	—
Plantation Loan	20,000	—
	30,960	3,710
Less: Long-term debt due within one year	(742)	(370)
	30,218	3,340

[a] Equipment Loan

In November 1997, Sino-Wood entered into two loan agreements for credit facilities in the amount of \$4,505,000 to purchase certain machinery and equipment in connection with the construction of two particle board mills in the PRC. As at December 31, 1999, \$3,710,000 [1998 – \$3,710,000] has been disbursed under the facilities. The balance of \$795,000 [1998 – \$795,000] will be disbursed upon the issuance of Certificates of Acceptance after installation of the machinery and equipment. The loans are repayable in ten equal consecutive semi-annual installments commencing on June 15, 1999. Sino-Wood may repay the loans at any time with 30 days written notice. The loans bear interest at LIBOR plus 0.625% payable semi-annually. As at December 31, 1999, the interest rate on the long-term debt was approximately 5.8% [1998 – 6.6%].

Interest capitalized as part of the cost of assets under development for the year amounted to approximately \$216,000 [1998 – \$254,000].

Principal repayments on the debt for the next five years are as follows:

	\$
2000	742
2001	742
2002	742
2003	742
2004	—
	2,968

[b] Debt component of Exchangeable Notes

During the year, Sino-Wood entered into an agreement to issue an aggregate of \$20 million Guaranteed Exchangeable Redeemable Notes [“Exchangeable Notes”]. The Exchangeable Notes are for a period of five years from January 29, 1999 to January 28, 2004, and bear interest at a rate of 5% per annum payable semi-annually in arrears.

The Exchangeable Notes are exchangeable in minimum amounts of \$1 million into Class A Subordinate-Voting Shares of the Company at a price of \$1.11 [equivalent of CDN\$1.72] per share during the period from January 29, 2000 to January 28, 2002

and at a price of \$1.21 [equivalent of CDN\$1.88] during the period from January 29, 2002 to January 28, 2004. Sino-Wood is entitled, at any time between January 29, 2000 to January 28, 2002, to require the Noteholders to exchange no more than \$10 million of the Exchangeable Notes into Class A Subordinate-Voting Shares provided that the weighted average price per share of the Company on The Toronto Stock Exchange for the 60 trading days and the 7 trading days immediately preceding the date of such exchange shall both exceed 2.0 times the exchangeable price then in effect. Exchangeable Notes not exchanged into Class A Subordinate-Voting Shares of the Company that are outstanding on the maturity date are entitled to interest for the entire five-year period at a rate of 15% per annum compounded annually less any interest already paid.

The Exchangeable Notes are being accounted for in accordance with their substance and are presented in the financial statements in their component parts, measured at their respective fair values at the time of issue. The debt component has been calculated as the present value of the required interest payments discounted at a rate approximating the interest rate that would have been applicable to non-convertible debt at the time the Exchangeable Notes were issued. Interest expense is determined on the debt component, with such component being reduced by the required semi-annual interest payments. The difference between the debt component and the face value of the Exchangeable Notes is classified as equity, net of issue costs. The equity component of the Exchangeable Notes is increased over their term to the full face value by charges to retained earnings.

[c] Plantation Loan

During the year, Sino-Wood entered into a loan agreement for a long-term loan of Euro 18,970,710 [\$20 million] to fund part of its plantation program.

The loan is for a period of ten years. Principal repayment of the loan will commence on May 15, 2005 in ten equal semi-annual installments. Sino-Wood may repay the loan at any time with 45 days written notice. The loan bears interest at the six-month EUR LIBOR rate plus 3.5% p.a. (as at December 31, 1999, the six-month EUR LIBOR rate was 3.5%). Interest expense for the period amounted to approximately \$208,000 [1998 – \$nil].

The Company pays certain of its interest expenses in Euro and enters into various foreign currency options in managing its foreign exchange risk. The Company does not hold financial instruments for trading purposes. As at December 31, 1999, the Company held Euro 2,920,000 [1998 – \$nil] in currency options at an exchange rate of Euro 1.2 to US\$1 expiring at various dates to November 2001. Premiums of Euro 63,000 were paid for the currency options. There is no market risk of loss beyond the premiums paid. The premiums paid are amortized over the life of the options.

The Company also pays certain of its interest expenses at floating EUR LIBOR interest rate and enters into an interest rate cap agreement in managing its interest rate risk. The cap agreement reduces the Company's exposure to EUR LIBOR movements by fixing the EUR LIBOR at a maximum of 7% per annum. The

counterparty will pay to Sino-Wood the excess of EUR LIBOR over 7% on the notional amount of the debt. Premiums of Euro 565,000 were paid for the interest rate cap. There is no market risk of loss beyond the premiums paid. The premiums paid are amortized over the life of the options.

[d] Other credit facilities

In addition to the above, subsidiaries of the Company have established several revolving lines of bank credit facilities to a maximum of approximately \$17,081,000. These credit facilities bear interest at the prevailing prime rate in Hong Kong and are repayable on demand. Each of Sino-Forest and Sino-Wood has provided guarantees in an amount equal to the facilities. As at December 31, 1999, credit facilities for trust receipt loans and letter of credits in the amount of approximately \$4,127,000 [1998 – \$1,997,000] and \$1,857,000 [1998 – \$nil], respectively, were utilized.

[e] Covenants

Under the terms of the above various debt agreements, the Company and Sino-Wood must meet certain financial and non-financial covenants. These covenants include the maintenance of certain financial ratios and certain restrictions and limitations, including those on changing the nature of its business and payment of dividends. Management considers that respecting these covenants will not affect the normal operations of the Company.

8. SHARE CAPITAL

Share capital consists of the following:

	1999	1998
	\$	\$
Authorized		
Unlimited Class A Subordinate-Voting Shares		
6,000,000 Class B Multiple-Voting Shares		
Unlimited Preference Shares, issuable in series		
Issued		
74,827,228 [including 4,619,000 issued under share purchase loans] Class A Subordinate-Voting Shares [1998 – 74,677,228, including 4,519,000 issued under share purchase loans]	33,007	32,989
6,000,000 Class B Multiple-Voting Shares [1998 - 6,000,000]	—	—
	33,007	32,989
Equity component of Exchangeable Notes [note 7(b)]	13,266	—
	46,273	32,989

The legal stated capital of the Company's Class A Subordinate-Voting Shares differs from the carrying value reflected in these consolidated financial statements. The legal stated capital as at December 31, 1999 is CDN\$66,828,829 [1998 – CDN\$66,801,329].

Authorized

Except with respect to voting, dividends and the rights of conversion described below, each Class A Subordinate-Voting Share and each Class B Multiple-Voting Share have the same rights and are equal in all respects:

- each holder of Class A Subordinate-Voting Shares is entitled to one vote per share whereas each holder of Class B Multiple-Voting Shares is entitled to five votes per share;
- the Class A Subordinate-Voting Shares rank in priority to the Class B Multiple-Voting Shares as to the payment of dividends; however, no dividends may be declared or paid on the Class B Multiple-Voting Shares in any fiscal year unless in that fiscal year dividends shall have been declared or paid on Class A Subordinate-Voting Shares in an amount per share at least equal to or equivalent to the amount of the dividend per share proposed to be declared or paid on Class B Multiple-Voting Shares;
- each holder of Class B Multiple-Voting Shares is entitled at any time and from time to time to have all or any part of the Class B Multiple-Voting Shares held converted into Class A Subordinate-Voting Shares on a share-for-share basis; and
- as a condition of the issue of any Class B Multiple-Voting Share, the registered holder will be required to execute a Coattail Agreement under which the holder will agree not to effect a transfer of any Class B Multiple-Voting Share unless such transfer is made in accordance with the terms thereof and is a Permitted Transfer, as defined in the provisions attaching to the Class B Multiple-Voting Shares.

The Preference Shares may from time to time be issued in one or more series, each series of which will have the rights and other features determined by the Board of Directors of the Company. The Preference Shares of each series will rank equally with the Preference Shares of every other series with respect to priority in payment of dividends and return of capital in the event of the liquidation, dissolution or winding-up of the Company and have a preference over the Class A Subordinate-Voting and the Class B Multiple-Voting Shares.

Changes in issued share capital

During the year, options to purchase 150,000 [1998 – 915,000] Class A Subordinate-Voting Shares were exercised under the terms of the Company's stock option plan [the "Plan"]. The Company made an interest free loan during the year amounting to \$102,000 to a former director [1998 – \$699,000 to certain officers], pursuant to the terms of the Plan to finance the acquisition of 100,000 [1998 – 765,000] Class A Subordinate-Voting Shares. The average purchase price of the shares acquired subject to the share purchase loan was \$1.02 [1998 – \$0.91]. In accordance with the terms of the Plan, the shares acquired are pledged to the Company and the indebtedness is repayable upon the sale of the pledged shares. The Company has recorded the share purchase loans as a reduction in share capital. As at December 31, 1999,

\$4,719,000 [1998 – \$4,353,000] of these loans remained outstanding. Gross proceeds on the 50,000 [1998 – 150,000] options exercised in 1999 and not subject to share purchase loans were approximately \$18,000 [1998 – \$57,000].

Stock options

The Company has reserved 10,000,000 Class A Subordinate-Voting Shares for issuance under its stock option plan.

As at December 31, 1999, 479,000 options granted to certain officers and directors of the Company, as well as an employee of Sino-Wood, were outstanding. These options allowed the officers, directors and employee to purchase Class A Subordinate-Voting Shares of the Company at prices ranging from CDN\$0.60 to CDN\$2.79 per share. 254,000 of these options expire in 2001 and 225,000 options expire in 2002.

9. INCOME TAXES

The provision for income tax expense differs from that obtained by applying the statutory rates as a result of the following:

	1999	1998
	\$	\$
Income before income taxes	31,692	23,607
Expected statutory rate	44.6%	44.6%
Expected income tax provision	14,135	10,529
Increase (Decrease) in income taxes resulting from -		
Unrecognized income tax losses arising from losses		
of the Company and subsidiaries	2,523	1,933
Income tax at different rates in foreign jurisdictions	(13,337)	(9,999)
Permanent differences	216	(220)
	3,537	2,243

The PRC WFOEs, CJVs, Leizhou WFOE and Gaoyao EJV are governed by the Income Tax Laws of the PRC concerning Foreign Investment Enterprises and Foreign Enterprises and various local income tax laws [the “Income Tax Laws”]. Pursuant to the Income Tax Laws, WFOEs, Sino-foreign equity and co-operative joint venture enterprises are subject to income tax at an effective rate of 33% [30% state income taxes plus 3% local income taxes] on income as reported in their statutory financial statements. The PRC WFOEs, CJVs, Leizhou WFOE and Gaoyao EJV are eligible for an exemption from state and local income taxes for two years starting from the first profitable year of operations after offsetting losses carried forward, followed by a 50% exemption for the next three years.

Hong Kong profits tax has been provided at the rate of 16% [1998 – 16%] on the estimated assessable profits arising in Hong Kong during the year. Taxes on profits assessable elsewhere have been calculated at the rate of taxation prevailing in the countries in which the Company operates.

As at December 31, 1999, the Company has income tax losses of approximately \$3,073,000 which can be applied against future years' taxable income in Canada, the benefit of which has not been recorded in these consolidated financial statements. Approximately \$171,000 of these tax losses will expire in 2001, \$250,000 in 2002, \$217,000 in 2003, \$705,000 in 2004, \$905,000 in 2005 and the remainder will expire in 2006.

10. EARNINGS PER SHARE

Earnings per share are calculated using the weighted average number of Class A Subordinate-Voting and Class B Multiple-Voting Shares outstanding during each year. The fully diluted earnings per share calculation assumes the full conversion of the Exchangeable Notes described in note 7 [b]. The weighted average number of Class A Subordinate-Voting and Class B Multiple-Voting Shares outstanding were as follows:

	Weighted average	
	Basic	Fully diluted
December 31, 1999	76,198,000	97,593,000
December 31, 1998	74,221,000	81,260,000

II. SEGMENTED INFORMATION

By industry segment

	1999			1998		
	Wood Chips \$	Wood- Based & Other \$	Total \$	Wood Chips \$	Wood- Based & Other \$	Total \$
Revenue from external customers						
Sales	89,503	34,162	123,665	66,793	9,368	76,161
Commission income	14,827	3,085	17,912	14,228	2,321	16,549
	104,330	37,247	141,577	81,021	11,689	92,710
Income from operations	28,463	5,168	33,631	21,213	2,833	24,046
Identifiable assets	146,173	32,098	178,271	84,654	15,847	100,501
Interest income	692	—	692	51	—	51
Interest expense	2,116	—	2,116	60	—	60
Depreciation and amortization	87	—	87	91	—	91
Investment in capital assets	26,950	10,689	37,639	29,013	1,637	30,650

Revenue transactions with the Company's largest customer for the year amounted to approximately 30% [1998 – 15%] of total sales. During the year, there were four [1998 – three] customers each individually accounted for more than 10% of the Company's sales and these sales in aggregate represented approximately 61% [1998 – 51%] of total sales.

Purchase transactions with the Company's largest vendor for the year amounted to approximately 57% [1998 – 86%] of total purchases. During the year, there were two [1998 – one] vendors each individually accounted for more than 10% of the Company's purchases and these purchases in aggregate represented approximately 68% [1998 – 86%] of total purchases.

By geographic segment

The Company conducts substantially all of its operations in one geographic area – East Asia. During the year, sales in the PRC and to other Asian countries amounted to approximately \$122,072,000 [1998 – \$72,434,000] and \$1,593,000 [1998 – \$3,727,000], respectively.

12. COMMITMENTS

As at December 31, 1999, the Company has various commitments to make capital contributions to the CJVs and EJV, the details of which are disclosed in note 2.

As at December 31, 1999, the Company has incurred commitments totalling approximately \$1,179,000 [1998 – \$33,000] relating to the construction of the wood-based production facilities.

The Company's future annual commitment under operating leases is as follows:

	\$
2000	147
2001	116
2002	30
	293

13. COMPARATIVE FINANCIAL STATEMENTS

The comparative financial statements have been reclassified from statements previously presented to conform to the presentation of the December 31, 1999 financial statements.

DIRECTORS



Allen T.Y. Chan ^{1, 2}
Chairman and
Chief Executive Officer



John (Jack) Lawrence ²
Chairman
Lawrence & Company



Edmund Mak ^{1, 3}
Real Estate Marketing,
Re/Max Select Properties



Simon Murray
Chairman
GEMS
(General Enterprise Management
Services Limited)



K.K. Poon
President



William Rosenfeld ^{1, 2, 3}
Partner
Goodman Phillips & Vineberg



Kee Y. Wong, F.C.A.
Executive Vice-President and
Chief Financial Officer

¹ Member of the Audit Committee

² Member of the Compensation Committee

³ Member of the Corporate Governance Committee

OFFICERS



Allen T.Y. Chan
Chairman and
Chief Executive Officer



K.K. Poon
President



Leslie Chan
Executive Vice-President



Kee Y. Wong, F.C.A.
Executive Vice-President and
Chief Financial Officer



Jay Lefton
Corporate Secretary

CORPORATE AND SHAREHOLDER INFORMATION

CORPORATE HEAD OFFICE

Sino-Forest Corporation
90 Burnhamthorpe Road West
Suite 1208
Mississauga, Ontario
Canada L5B 3C3
Tel: 905.281.8889
Fax: 905.281.3338
E-mail: info@sinoforest.com
Web site: www.sinoforest.com

EXECUTIVE HEAD OFFICE

Sino-Forest Corporation
1409 Great Eagle Centre
23 Harbour Road
Wanchai, Hong Kong
Tel: 852.2877.0078
Fax: 852.2877.0062

AUDITORS

Arthur Andersen LLP
1200 – 45 St. Clair Avenue West
Toronto, Ontario
Canada M4V 3A7

ANNUAL SHAREHOLDER MEETING

Monday, June 26, 2000

4 p.m.

The Royal York Hotel
Upper Canada Room, 18th Floor
100 Front Street West
Toronto, Ontario
Canada M5J 1E3

LEGAL COUNSEL

Aird & Berlis
BCE Place
Suite 1800, Box 754
181 Bay Street
Toronto, Ontario
Canada M5J 2T9

EXCHANGE LISTING

The Class A Subordinate-Voting Shares of the Company are listed on The Toronto Stock Exchange under the symbol **TRE.A**

REGISTRAR AND TRANSFER AGENT

CIBC Mellon Trust Company
320 Bay Street, P.O. Box 1
Toronto, Ontario
Canada M5H 4A6
Tel: 416.643.5500
Toll-free North America: 1.800.387.0825

INVESTOR RELATIONS

Kee Y. Wong, F.C.A.
Executive Vice-President and
Chief Financial Officer
Tel: 905.281.8889
Fax: 905.281.3338

Allen T.Y. Chan
Chairman and Chief Executive Officer
Tel: 852.2877.0078
Fax: 852.2877.0062



Sino-Forest Corporation