Positioned to Unlock Shareholder Value

SINO-FOREST CORPORATION

2002 Annual Report

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

Loading particleboard at the Gaoyao mill.

CONTENTS

Market Potential

The massive populations of China and other Asian countries have created strong demand for industrial and consumer wood products. Governments in the region have had to ban logging of natural forests to protect their environments, causing huge shortages of wood. Renewable plantations have become a long-term solution, and Sino-Forest is uniquely positioned to reap value from this market opportunity.

Strategy

Sino-Forest's strategy is to satisfy strong demand for wood products by cultivating tree plantations and manufacturing and trading a broad range of products. The company is creating a new paradigm in the Chinese forest industry by combining traditional forestry practices with new investment and technology to increase plantation yields and generate higher-quality, value-added products for trade with domestic and international customers. This strategy will allow Sino-Forest to deliver sustainable and profitable growth, and increase market penetration and shareholder value.

Corporate Profile

Sino-Forest Corporation is the first foreign-owned, fully integrated forest products company in the People's Republic of China. The company's growing participation in the commercialization of China's vast forestry resources creates sustainable growth and value for Sino-Forest's various stakeholders. Combining its financial and technological resources with its business connections and entrepreneurial skills, the company is well positioned to become a forest industry leader in Asian and other global markets. Sino-Forest is a Canadian corporation with executive offices in Hong Kong. The company's Class A Subordinate-Voting shares are listed on the Toronto Stock Exchange under the symbol TRE.A.

2002 Highlights

- Sino-Forest phased in or is in the process of phasing in an additional **19,600** hectares of agro-forestry lands, bringing the total active plantation area to **232,600** hectares nationwide.

Eucalyptus plantation at the Gaoyao Cooperative Joint Venture (CJV).

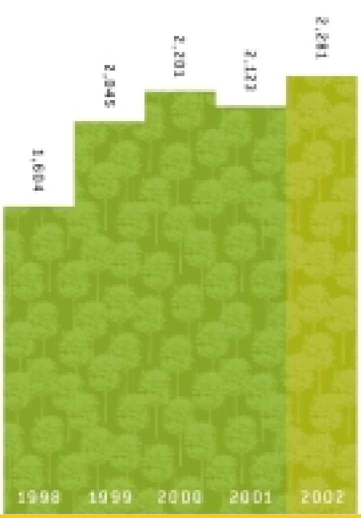
- Profitability improved substantially as diluted earnings per share increased **24%**, and average return on equity rose to **12%**.

- Sino-Forest increased revenue from the sale of wood chips by **40%**, and further diversified its sources of revenue.

(all amounts are expressed in US dollars unless otherwise indicated)

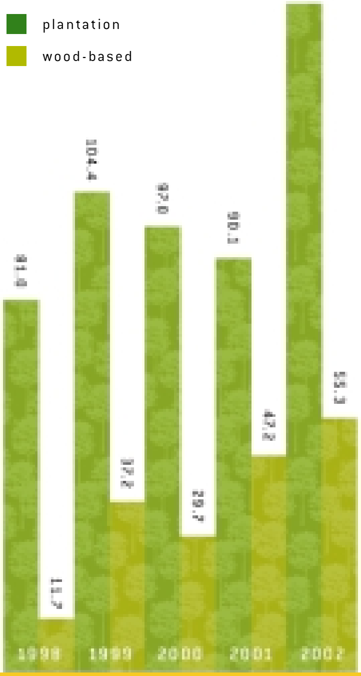
WOOD CHIP SHIPMENTS AND PRODUCTION

(BDMT/thousands)



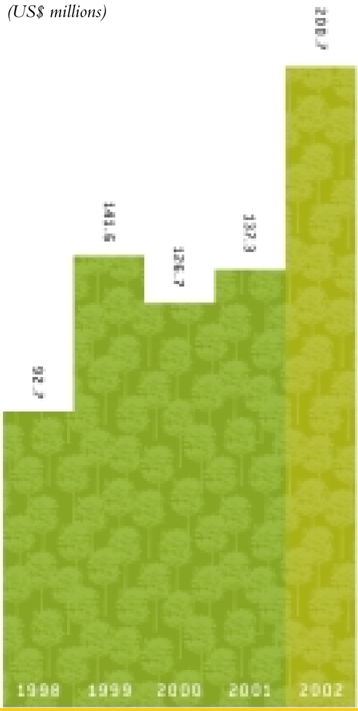
REVENUE BY SEGMENT

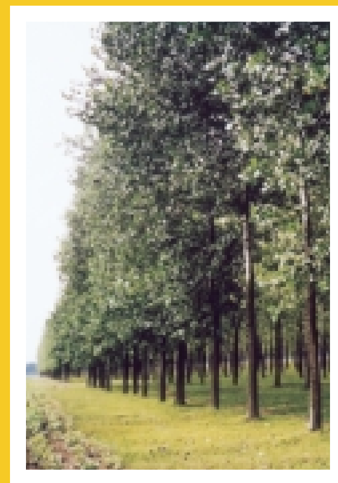
(US$ millions)



REVENUE

(US$ millions)



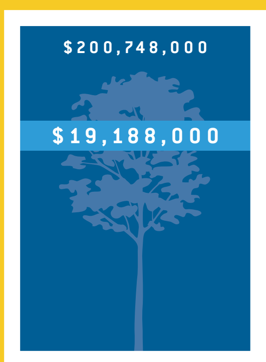


Mature eucalyptus trees ready to be harvested.

A subsidiary of Sino-Forest obtained updated certificates from the International Standards Organization for its **ISO 9001** Quality Management System and **ISO 14001** Environmental Management System.

2002 SALES

(US$)



standing timber sales

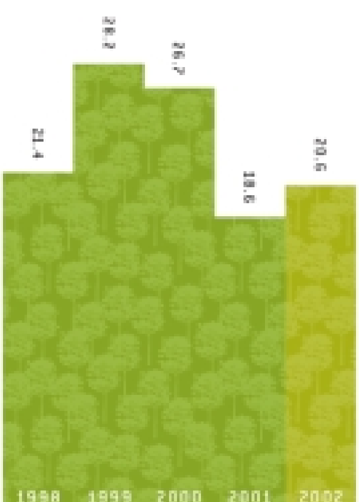
total sales

The company sold, for the first time, **8,100** hectares of standing timber, realizing a profit of **$9,100,000**.

(all amounts are expressed in US dollars unless otherwise indicated)

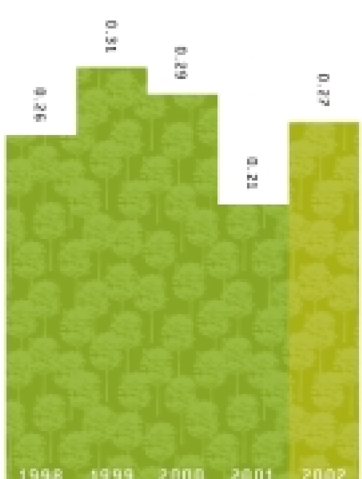
NET INCOME

(US$ millions)



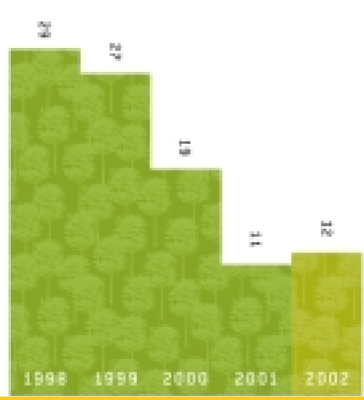
DILUTED EARNINGS PER CLASS A AND B SHARE

(US$ cents)



AVERAGE RETURN ON EQUITY

(Percent)



Message from the Chairman and CEO

Building the Foundation for Future Growth

Since we entered the China market as the first foreign and privately managed company in the forest-product industry, Sino-Forest has established a strong position. Despite many challenges, we have managed to produce nine years of growing and sustainable profitability. This has allowed us to invest in new plantations and further research & development, which are now delivering higher yield and better quality products, more reliably and cost-effectively than our competitors.

In 2002, we largely completed another important chapter in our relatively short history, bringing us closer to becoming the most successful, vertically integrated, forest product company in China. We invested substantial resources in the expansion of our plantation business and diversification of our operations and product line, but we have not changed our focus on profitability and sustainability.

Sino-Forest continues to execute its strategy of satisfying strong demand for wood products, by growing plantations, diversifying our manufacturing capabilities and product line, and increasing market penetration. As demand exceeds supply, prices of wood products are rising, and that has increased our margins.

Having taken giant steps, we are now beginning to reap the rewards of our commitments and investments.

Unlocking Shareholder Value

Sino-Forest has built the foundations for generating accelerated growth in sales and earnings.

Over the past year, Sino-Forest has taken advantage of its prolific plantations to fulfill part of the enormous and surging demand for wood chips, logs and standing timber. Sales of these raw materials to manufacturers jumped 62% in 2002. This strengthened our plantation business and boosted total company revenues by 46%.

Due to improved pricing of wood chips, and higher operating margins, net income last year increased 11% from 2001 to $20.6 million, while cash flows from operations remain approximately the same as 2001 at $12.6 million. We managed to produce these excellent results while maintaining a strong balance sheet with a debt-to-equity ratio of 0.75:1.

With a sound business plan and excellent financial results, we readily obtained funding in the first quarter of 2003 to finance future growth. Through its subsidiary Sino-Wood Partners, the company issued $14 million of convertible instruments to a broad base of Asian investors. Simultaneously, we have made substantial progress toward building a sound base of investors — another important step toward positioning ourselves to unlock shareholder value.

ALLEN CHAN, CHAIRMAN & CEO

The China market appears increasingly promising.

Favourable Outlook

Along with strong projected economic growth in China, private investment is helping to create a more open market. The country is facing a chronic shortage of wood, and Sino-Forest is uniquely positioned to meet the demand for its products from existing and future customers.

In addition to selling wood chips at higher prices to the recovering global pulp market, we expect to sell significantly more logs this year, at higher returns. But we will also focus on completing the construction of our new manufacturing facilities for producing higher-margin wood products and profitability.

Sino-Forest is successfully implementing an ambitious plan to grow its business. We expect that our operations and product line diversification will allow our bottom line to grow at an even faster pace than sales in the medium term. As a result, we expect Sino-Forest's return on equity to further improve.

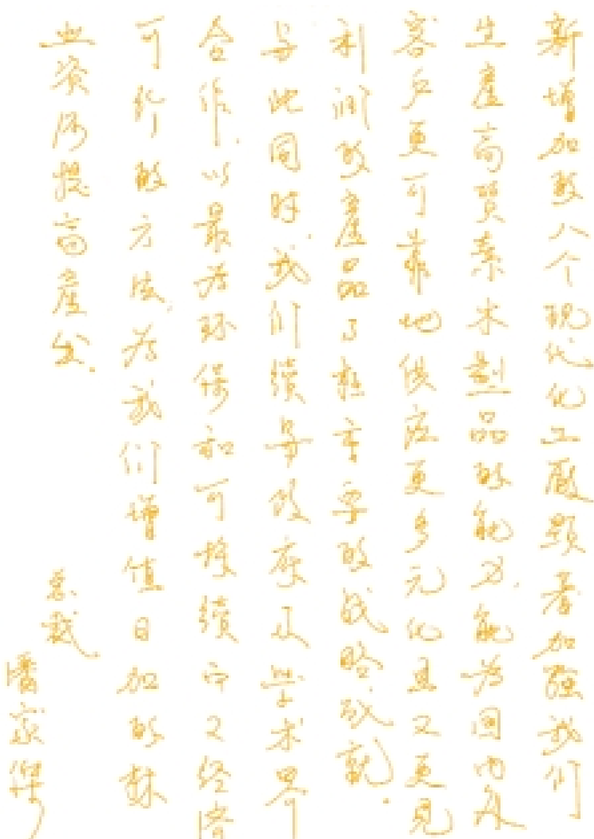
We have set the foundations for strong growth in sales and earnings over the next several years, and we expect to reap the benefits from our commitment as our share price appreciates along with the value we create. On behalf of Sino-Forest management, I express sincere gratitude for our success: to our investors and lenders, specifically the International Finance Corporation (IFC) — a member of the World Bank Group, Nederlandse Financierings-Maatschappij Voor Ontwikkelingslanden N.V. (FMO) and DEG-Deutsche Investitions-Und Entwicklungsgesellschaft MbH (DEG), for their financial support and loyalty, to our Board of Directors for their wise guidance, and to our employees for their dedication and diligence.

Allen Chan
Chairman and Chief Executive Officer

Message from the President

The addition of eight new mills currently under construction, with state-of-the-art technology, are expected to significantly increase our capacity to manufacture and deliver high-quality wood products. It is a major strategic achievement to provide a broader range of higher-margin products, more dependably, to our domestic and international customers.

At the same time, we continue to work with government, academic and local authorities to augment the yield of our increasingly valuable forestry resources, using the most environmentally sustainable and economically viable methods.



Kai Kit Poon
President

KAI KIT POON, PRESIDENT

Supplying Vast Global Markets

Uniquely Positioned in a Globally Important Marketplace

SINO-FOREST IS THE FIRST FOREIGN AND PRIVATELY MANAGED COMPANY INVOLVED IN FOREST PRODUCTS IN CHINA, AND ONE OF THE MOST MODERN MANUFACTURERS OF FINISHED WOOD PRODUCTS. AS SUCH, IT IS IN AN EXCELLENT POSITION TO RESPOND TO THE MASSIVE WOOD SHORTAGE.

China is a colossal and growing market for wood products — the world's third largest. Despite socio-economic challenges, the country's Gross National Product is growing rapidly at over 7% per year. China has entered the World Trade Organization, and strong inflows of foreign direct investment together with public investment and export growth are strengthening domestic demand. Regional economies are becoming more flexible and dynamic.

There is huge demand for Sino-Forest's engineered wood in China's construction industry.

Approximately 575 million people live in the 14 provinces and municipalities surrounding the Guangdong and Greater Shanghai areas where Sino-Forest is strategically located to cultivate plantations and manufacture finished goods for trading. Within these heavily populated regions, and overseas, the company's products are in great demand: wood chips for the pulp and paper industry; and logs, lumber and engineered wood products for the housing, building materials, furniture and decoration sectors. With the increasing prosperity of China's emerging middle class, demand for quality furniture, flooring, paneling and other household wood products is growing steadily.

Sino-Forest faces no serious threat of competition in the Chinese industry which is characterized by small-to-medium-size operations with relatively low productivity. The company has built key competitive advantages such as scale and breadth of operations, sufficient access to capital, superior technological capabilities, exporting relationships with Asian and North American customers, and entrepreneurial management. All these advantages give Sino-Forest the capabilities to provide better service more efficiently and reliably to its customers. Several foreign companies have expressed interest in partnering with Sino-Forest due to its market intelligence and experience operating in China, geographically strategic locations, secure supply of raw materials, and bilingualism.

Sino-Forest operations are strategically positioned near major transportation routes and wood product markets.

Cultivating Plantations for Superior Yield

Tree Plantations Increase in Value

China produces only half the timber it consumes. Since the government cracked down on deforestation, manufacturers of wood products are increasingly obtaining their raw material from more environmentally friendly wood, harvested at managed plantations.

Sino-Forest specializes in cultivating plantation trees — the long-term solution to China's severe wood deficit. Over the past several years, it has established several nurseries and phased in or begun phasing in 232,600 hectares of plantation lands. In order to secure a plentiful supply of trees, Sino-Forest participates in cooperative joint ventures (CJVs) with local authorities, typically owning a 70% interest in the trees, over authorized terms of 50 years. The company has CJVs strategically located mainly in Guangdong, Guangxi and Jiangxi, near major population centres with low transportation and labour costs. These plantations cover a total area of 583,000 hectares of land. Sino-Forest can phase into operation additional lands as needed, providing important flexibility for responding to fluctuating market demand.

Tree seedlings are carefully nurtured at Sino-Forest nurseries.

Sino-Forest works with local foresters and ecology experts to professionally manage the plantations. It uses research and bioengineering to maximize yield over subsequent years. The next planting cycle of trees by Sino-Forest is expected to produce a much higher yield as a result of better gene selection, cloning, spacing, non-chemical fertilization and improved resistance to disease and fire.

The company cultivates fast-growing species of eucalyptus, aspen (poplar) and pine, with growth cycles of only 5 to 12 years. The result is higher-quality trees, cultivated at lower cost, with minimal impact on the environment. Sino-Forest's professional management quickly and appreciably increases the market value of its plantations.

Standing Timber, Log and Wood Chip Sales Accelerate

Following recent logging or log export bans in China and elsewhere in south-east Asia, there has been a surge in demand for renewable plantation wood. As a result, Sino-Forest has significantly stepped up its sales of logs and standing timber. Production and shipments of Sino-Forest's core product — wood chips — increased 7.5% last year as the global pulp market began to improve from a cyclical low. The company produces a wood chip fibre suitable to make quality papers. Wood chip and pulp prices are increasing with demand for higher inventory.

Sino-Forest's renewable tree plantations are part of a long-term solution to China's wood shortage.

There has been a surge in demand for plantation logs in China.

The use of biotechnology helps enhance the yield of Sino-Forest plantations.

Broadening Our Capabilities

Completing Eight New Mills

WITH THE SCARCITY OF NATURAL WOOD IN CHINA FOR MANUFACTURING PURPOSES, ENGINEERED WOOD HAS BEEN REPLACING TRADITIONAL SOLID WOOD PRODUCTS. HAVING THE FORESIGHT TO ACCELERATE AND CAPITALIZE ON THIS TREND, SINO-FOREST DECIDED TO BUILD ITS OWN MANUFACTURING FACILITIES AND INCREASE THE QUALITY AND DEPENDABILITY OF PRODUCT SUPPLY TO ITS CUSTOMERS.

New manufacturing facilities give Sino-Forest additional competitive advantages.

The construction of the company's modern facilities has been financed by the International Finance Corporation (member of the World Bank Group) and by two European lenders. After some delays, Sino-Forest expects to open eight mills for production later this year, further diversifying its product line and moving down the supply stream to higher-value, higher-margin products. The company's goal is to reach approximately 50% capacity in the first year of operating the facilities, then 80% the following year, significantly improving profitability.

The mills use state-of-the-art technology to cut lumber, and manufacture a variety of engineered products, including laminated particleboard, finger joints, blockboards, etc.

Augmenting Wood Products Trading

China's wood product exports are rapidly expanding, most of them destined for the United States and Europe. Sino-Forest also acts as an agent for trading logs, wood chips and value-added products.

Since the company started business in China nine years ago, it has established valuable trading relationships with many suppliers and domestic or international customers. This is increasing the sales volumes and income generated from this aspect of the business. Over the past year, Sino-Forest has opened two more offices for trading representatives to satisfy the service requirements of a growing customer base. Sino-Forest also has adequate financial resources in place to allow the company to source wood products for its demanding marketplaces.

New manufacturing facilities will enhance Sino-Forest's product offering and competitive position in the market.

Sino-Forest operates its mills using modern equipment and manufacturing techniques.

Sino-Forest's mills in operation and under construction

	Location	Annual Capacity	Production Commencement
Gaoyao particleboard mill	Guangdong	100,000 m^3	In operation
Suzhou oriented strand board mill	Greater Shanghai	10,000 m^3	Fourth quarter 2003
Gaoyao sawmill	Guangdong	32,000 m^3	Fourth quarter 2003
Suzhou sawmill	Greater Shanghai	68,000 m^3	Fourth quarter 2003
Gaoyao finger-joint board mill	Guangdong	20,000 m^3	Fourth quarter 2003
Suzhou finger-joint board mill	Greater Shanghai	20,000 m^3	Fourth quarter 2003
Suzhou blockboard mill	Greater Shanghai	20,000 m^3	Fourth quarter 2003
Gaoyao door plant	Guangdong	100,000 pieces	Fourth quarter 2003
Gaoyao cabinet plant	Guangdong	150,000 pieces	Fourth quarter 2003
Gaoyao particleboard lamination plant	Guangdong	6,000,000 m^2	Second quarter 2004

Leading Sustainable Management

Practicing Sustainability

Sino-Forest believes in sustainable development — using, developing and protecting resources in a manner that meets the environmental, economic and community needs of current and future generations. The company is proud to be a leader in practicing sustainable development in its forest management operations, and is publicly recognized for its commitments.

Last year, a Sino-Forest subsidiary received upgraded certificates from the International Standards Organization for its ISO 14001 Environmental Management System and ISO 9001 Quality Management System, which are valid for three and four years respectively. Sino-Forest plans to expand these systems for additional ISO certification.

Sino-Forest's cultivation of trees in a sustainable manner helps preserve China's natural resources and rural employment.

In 2002, Sino-Forest invited the Rainforest Alliance to assess the plantation management of its Jiayao Forestry Development Company in Guangdong Province for potential SmartWood Program certification. The Alliance is credited by the Forestry Stewardship Council, and SmartWood is the oldest and most extensive, "gold standard" certification program in the world. Jiayao's plantation sites are also environmentally monitored for water quality, soil fertility, pollution and tree condition.

Sino-Forest supports the Public Welfare Forests under government management in China by sharing experiences in ecological protection, research results, technical expertise, and forest protection patrol. In 2002, company employees received government awards for their research on the impacts of eucalyptus on the ecology in China, and organized an international symposium on eucalyptus plantations with the Chinese Academy of Forestry. Sino-Forest also participated in an Industrial Environmental Management seminar in cooperation with Shanghai Jiao Tong University and Yale University, covering industrial ecology, which optimizes the use of resources, energy and capital throughout a wood product's life cycle.

In the spirit of sustainability, the company tends to harvest in a region no more than the number of trees that grow to maturity during the year. Sino-Forest also spreads out its harvesting throughout a plantation, and uses manpower rather than machinery if need be, to avoid widespread soil degradation.

Sustainable business practices are integral to Sino-Forest's plantation and manufacturing processes.

A strong believer in sustainability, the company plants more seedlings each year than the number of trees it harvests.

Sino-Forest protects natural resources on or adjacent to its plantations.

2002 Consolidated Financial Statements

Tree saplings in one of Sino-Forest's nurseries.

CONTENTS

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, 2002 and 2001 is as follows:

(thousands of U.S. dollars)	Year ended December 31, 2002 PLANTATION $	WOOD-BASED $	TOTAL $	Year ended December 31, 2001 PLANTATION $	WOOD-BASED $	TOTAL $
REVENUE						
Sale from wood chips	113,554	–	113,554	76,816	–	76,816
Sale of wood-based products	–	55,254	55,254	–	44,635	44,635
Sale from standing timber	19,188	–	19,188	–	–	–
Commission income	12,752	–	12,752	13,262	2,600	15,862
	145,494	55,254	200,748	90,078	47,235	137,313
INCOME (LOSS) FROM OPERATIONS	33,396	(2,109)	31,287	20,614	831	21,445

Income from operations for the year ended December 31, 2002 was $31.3 million, an increase of 46% compared to income from operations of $21.4 million for 2001. Earnings per share on a diluted basis increased 29% to $0.27 per share compared to $0.21 per share attained in 2001. Income for the plantation operation increased by 62% from $20.6 million in 2001 to $33.4 million in 2002 as a result of higher wood chip prices, higher shipments and the sale of 8,100 hectares of standing timber holdings. Loss from the wood-based business was $2.1 million compared to an income of $0.8 million in 2001 as a result of losses incurred from the operation of the particleboard mill in Gaoyao, which is still operating below planned normal capacity and depreciation charges on the mill. The particleboard mill is expected to operate at planned normal capacity by the end of 2003.

Sales from principal wood chip shipments increased 48% from $76.8 million in 2001 to $113.6 million in 2002. Commission income from wood chip sales decreased 4% from $13.3 million in 2001 to $12.8 million in 2002. The increase in revenue for wood chip sales was attributable to the increase in wood chip price and shipments of approximately 18% and 24%, respectively in 2002. Revenue in 2002 was also increased by the sale of standing timber holdings of $19.2 million. Revenue from the wood-based business has increased 17% from $47.2 million to $55.3 million in 2002 primarily due to an improved environment in the market for lumber and wood-based products in China. The increase in revenue in 2002 can be summarized as follows:

	$
Increase in volume (260,600 BDMT) of shipments for principal sales	22,219,000
Increase in wood chip prices of approximately 19%	14,523,000
Decrease in volume (102,410 BDMT) of shipments for agency sales	(1,376,000)
Increase in agency fees of approximately 6%	862,000
Increase in revenue from the sale of 8,100 hectares of standing timber	19,188,000
Increase in wood products trading	8,019,000
INCREASE IN REVENUE FOR THE YEAR	**63,435,000**

In 2002, wood chip shipments totaled 2,281,200 bone dry metric tonnes ("BDMT") compared to 2,123,000 BDMT shipped in 2001, an increase of 7%. Of the total wood chips shipped in 2002, 128,700 BDMT were export and 2,152,500 BDMT were sold in China. Export and domestic shipments for 2001 were 151,900 BDMT and 1,971,100 BDMT, respectively. For the year ended December 31, 2002, the Company acted as principal on 1,332,400 BDMT compared to 1,071,800 BDMT in 2001, an increase of 24%. Shipments in which the Company acted as an agent decreased just below 10% from 1,051,200 BDMT in 2001 to 948,800 BDMT in 2002. Export shipments have decreased 15% from 151,900 BDMT in 2001 to 128,700 BDMT in 2002.

A summary of the wood chip shipments for the year ended December 31, 2002 compared to 2001 is set out in the table below:

WOOD CHIP SHIPMENTS FOR THE YEAR ENDED DECEMBER 31
[thousands of BDMT]

	Principal		Agency		Total	
MARKET	2002	2001	2002	2001	2002	2001
Export	**14.1**	32.8	**114.6**	119.1	**128.7**	151.9
PRC domestic	**1,318.3**	1,039.0	**834.2**	932.1	**2,152.5**	1,971.1
TOTAL	**1,332.4**	1,071.8	**948.8**	1,051.2	**2,281.2**	2,123.0

The average price of wood chips, net of VAT, transportation and delivery charges, in 2002 was approximately $85 per BDMT. The average price of wood chips, net of VAT, attained in 2001 was $72 per BDMT. With respect to sales in which the Company acted as an agent, the Company earned an average of $13.44 per BDMT in 2002 compared to $12.60 per BDMT earned in 2001.

QUARTERLY FINANCIAL INFORMATION

The following table is a summary of selected quarterly financial information of the Company for each of the eight quarters ended December 31, 2002:

	REVENUE $	NET INCOME $	NET INCOME PER SHARE BASIC $	NET INCOME PER SHARE DILUTED $
FISCAL 2002	[in thousands of U.S. dollars]			
December 31	**66,044**	**6,621**	**0.09**	**0.08**
September 30	**57,587**	**7,751**	**0.10**	**0.10**
June 30	**43,962**	**3,579**	**0.05**	**0.05**
March 31	**33,155**	**2,641**	**0.03**	**0.03**
FISCAL 2001				
December 31	49,602	7,378	0.10	0.08
September 30	42,099	4,151	0.06	0.05
June 30	29,775	3,588	0.05	0.04
March 31	15,837	3,456	0.04	0.04

INVESTMENT IN WOOD-BASED BUSINESS

The Company is in the process of establishing a wood-based business for the sale of value-added wood products in the People's Republic of China (PRC). These operations will be carried out through companies of the Sino-Panel group.

In November 2000, the Company completed the construction of its first particleboard mill in Gaoyao. The particleboard mill is one of the largest facilities in China and is capable of producing international quality board. The production facility is expected to have a capacity to produce 100,000 m^3 of particleboard per annum, utilizing equipment and production technology imported from Finland. Although the mill was completed in November 2000, commercial production of the mill did not commence until May 2001. Under the initial Implementation Schedule Plan, the particleboard mill was expected to be operating at 70% to 80% by the end of 2002. However, during the year, several operating issues were identified which required the particleboard mill to be shut down in the fourth quarter of 2002. These operating issues related primarily to the need to recondition and modify the equipment to enable the particleboard mill to produce products with a certain level of quality and operating capacity. These operating issues are expected to be resolved by the second quarter of 2003. As a result of the operating problems encountered in 2002, lamination equipment will not be installed until, at the earliest, the second quarter of 2004. As the particleboard mill is still operating at below planned normal capacity, it incurred operating losses before depreciation charges of approximately $0.6 million for the year ended December 31, 2002.

In addition to the particleboard mill, the Company has commenced the construction of several wood-based manufacturing facilities in 2001 in the province of Guangdong and the Greater Shanghai Region. A summary of these wood-based manufacturing projects currently under development, which were partly funded by the International Finance Corporation (IFC), part of The World Bank Group, the Nederlandse Financierings-Maatschappij Voor Ontwikkelingslanden N.V. (FMO) and DEG – Deutsche Investitions – und Entwicklungsgesellschaft mbH (DEG) is as follows:

MILL	LOCATION	CAPACITY	EXPECTED COMPLETION DATE
Gaoyao lamination plant	Guangdong	6,000,000 m^2	Second quarter 2004
Gaoyao sawmill	Guangdong	32,000 m^3	Fourth quarter 2003
Suzhou sawmill	Greater Shanghai Region	68,000 m^3	Fourth quarter 2003
Gaoyao finger-joint board mill	Guangdong	20,000 m^3	Fourth quarter 2003
Suzhou finger-joint board mill	Greater Shanghai Region	20,000 m^3	Fourth quarter 2003
Suzhou blockboard mill	Greater Shanghai Region	20,000 m^3	Fourth quarter 2003
Gaoyao door plant	Guangdong	100,000 pieces	Fourth quarter 2003
Gaoyao cabinet plant	Guangdong	150,000 pieces	Fourth quarter 2003

These projects were initially expected to be completed by the end of 2002. However, due to delay in the final disbursement from the lenders above which in turn resulted in a delay in the shipment of the equipment ordered, most of these projects are currently expected to be completed by the end of 2003. Accordingly, these mills are not expected to make any significant contributions to the Company's revenue and bottom line until 2004.

Liquidity and Capital Resources

Cash flows from operations in 2002 were $12.6 million, which together with cash in hand and the financing facilities from the IFC, FMO and DEG were sufficient to finance investment in capital assets of $44.2 million in 2002. Investment in capital assets is made up of plantation costs, acquisition of young trees, and construction of plants.

As at December 31, 2002, the Company has cash and short-term deposits of $27.8 million and approximately $3.5 million of unutilized bank credit facilities. As at December 31, 2002, the Company's total debt was $135.7 million, compared with $99.4 million (including the equity component of debt) at the end of 2001. The increase in debt was primarily due to the increase in bank borrowings to fund working capital for the wood-based business and the second drawdown on the IFC financing of $19.0 million, which is included in long-term debt. On December 31, 2002, the debt to equity ratio was 0.75:1 compared with 0.62:1 (assuming that the equity component of the debt has been reclassified as long-term debt) at the end of 2001.

Cash and short-term deposits on hand at the year-end of $27.8 million, the unutilized credit facilities, the remaining draws from the IFC, FMO and DEG and the proceeds of $14.0 million received from the financing completed in March 2003 will be sufficient to meet all planned capital expenditures for the year 2003.

COMMITMENTS

As at December 31, 2002, the Company has various capital and operating lease commitments. The detail of these commitments are disclosed in notes 3 and 15 to the consolidated financial statements.

ENVIRONMENTAL MATTERS

Sino-Forest has established an Environmental Management System ("EMS"), with specific policies for social and environmental aspects of its operations. The Company is committed to applying sustainable management to its plantation operation and to achieving continuous improvement in its environmental performance. Sino-Forest's funding by the IFC, FMO and DEG is an endorsement of the Company as one of the leaders in sustainable forestry management in China. Sino-Forest is committed to upholding the high standards of The World Bank Group with respect to environmental, labour relations and workplace safety. The Company's particleboard mill in Gaoyao and all the other production facilities currently under construction are designed to meet The World Bank Group's environmental and health and safety guidelines. Some of the Company's environmental and social initiatives can be found in the 2002 Annual Report under the heading "Leading Sustainable Management" on page 14.

OUTLOOK

The demand for logs in China is expected to be strong in the foreseeable future as China continues to enforce its logging ban and exporting log countries implement zero export policy or reduces significantly the volume of logs available for export. This recent development has resulted in the wood supply deficit in China to increase significantly to approximately 50%. Plantation logs will provide part of the answer in solving the wood deficit problem experienced in China.

The demand for wood products in China is expected to be strong as the Chinese economy is projected to grow at an average annual rate of 7%–8% per annum over the next 10 years. 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 products in China over the next decade will lag behind the projected strong growth in demand for wood products.

The demand for wood chips in China is expected to remain stable in the near term. Prices of wood chip have increased significantly in 2002 and are expected to remain at $85 per BDMT to $90 per BDMT in 2003.

Risks and Uncertainties

FAILURE TO MAKE CAPITAL CONTRIBUTIONS

The CJV Law stipulates that the first instalment of the capital contribution by a joint venture party shall not be less than 15% of the portion of the registered capital subscribed to by the joint venture party and must be within three months of the issuance date of the business licence of the CJV. In the event of a breach of the statutory requirement, the CJV may automatically cease to exist and all prior approvals are automatically revoked.

Where joint venture parties have met their obligations on payment of the first instalment on capital contribution, the CJV Law provides that where a joint venture party fails to meet its subsequent obligation to make capital contributions three months after it becomes due, relevant government authorities shall issue a notice to the joint venture parties demanding that the capital contribution be made within one month. Failure to comply with the demand will give government authorities the right to revoke the business licence of the CJV and all prior approvals, thereby forcing the CJV into wind-up proceedings. The risk of governmental action in the event of the Company's inability to meet its contribution commitments is a significant risk. However, the delay of capital contribution under certain conditions can be negotiated among the parties and if the reasons for delay are rational and agreed upon by the parties, the contract can be revised and approval can be obtained from the relevant authority.

FLUCTUATIONS IN SELLING PRICE OF WOOD CHIPS AND WOOD PRODUCTS

The operating results of the Company can be significantly affected by fluctuations in the selling price of wood chips and wood products. Wood chips produced by the Company are primarily supplied to pulp manufacturers in Japan, Taiwan and China. The pulp market industry is cyclical in nature. World pulp prices are affected by a number of factors including the world's economic growth rate and the demand for paper products. By developing wood product manufacturing facilities, the Company is able to consume some of its own timber and increase the value of its plantation assets. Demand for wood-based panels in China is driven primarily by population growth and other demographic factors. Economic growth in China has a significant effect on panel demand because the strength of an economy has implications for building and construction activity and furniture production. By locking in long-term supply contracts with key customers and by differentiating its higher quality products and service from its Chinese competitors, the Company hopes to protect against temporary over-supply from, or lower prices of, other Chinese manufacturers of particleboard and other wood products.

JOINT VENTURE ARRANGEMENTS

Co-operation and agreement among the Company's joint venture partners are important factors for the operational and financial success of the joint ventures. In certain circumstances, the Company is not able or will not be able to control the decision making process of the joint ventures without the concurrence of the joint venture partners. The Company does or will, however, through contractual provisions and representatives appointed by it, have the ability to control most material decisions. Disputes among the partners over joint venture obligations or other matters, or the early termination or non-renewal of the joint venture agreements, could materially adversely affect the business of the Company. However, the Company has not experienced any significant disagreements with its partners to date.

LIMITED OPERATING HISTORY OF THE WOOD PRODUCT MANUFACTURING BUSINESS

The Company's wood product manufacturing business is in the early stages of development and has no operating history. The wood product manufacturing business is subject to all of the risks inherent in the establishment and maintenance of a new business enterprise, such as competition and viable operations management. The expansion of the wood product manufacturing business will also depend upon the ability of management to implement and successfully manage expansion, as well as its ability to raise any required capital. There can be no assurance that the wood product manufacturing business will grow and be profitable.

EXCHANGE CONTROL

The usage, movement and conversion of foreign currency in the PRC are subject to legislative and administrative restriction and control. The Chinese government imposes control over the conversion of its national currency RMB into foreign currencies and remittance thereof out of the PRC must be conducted through the Bank of China or other authorized financial institutions to deal in foreign currencies or, for conversion only, through the authorized banks or foreign exchange adjustment centres. No approvals are needed in order to acquire foreign exchange for a current account transaction, including profit distributions, interest payments and receipts and expenditures from trade and labour. Strict controls, primarily prior approval by the State Administration for Foreign Exchange, continue for capital account transactions in foreign exchange. Capital account items include loans, direct capital investments and investments in negotiable securities. The Company believes that the implementation of these measures will allow the PRC enterprises in which they have interests to access foreign exchange for remittance of profits without prior regulatory approval. Under the current foreign exchange control system, however, there is no guarantee that sufficient foreign currency will be available at a given exchange rate to satisfy the demands of a particular enterprise in full.

Management's Report

The consolidated financial statements contained in this Annual Report have been prepared by management in accordance with Canadian 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 Ernst & Young, 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, 2002 and 2001, and the consolidated statements of income and 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, 2002 and 2001, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Toronto, Canada,
April 30, 2003

Chartered Accountants

Consolidated Balance Sheets

(Expressed in thousands of United States dollars)

As at December 31	2002	2001
	$	$
ASSETS		
Current		
Cash and cash equivalents	1,178	1,709
Short-term deposits [note 8]	26,606	29,003
Accounts receivable [note 4]	40,190	19,209
Due from LFB [note 6]	10,202	–
Due from PRC CJV partners [note 7]	9,072	7,250
Other receivables and prepaid expenses	6,412	8,936
Deposit for the purchase of logs	6,041	–
Inventories [note 5]	878	983
Total current assets	100,579	67,090
Capital assets, net [note 6]	233,321	211,243
Deferred financing costs	2,445	2,644
Other assets	550	624
	336,895	281,601
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Bank indebtedness [note 8]	48,064	37,927
Accounts payable and accrued liabilities	10,635	11,804
Income taxes payable	10,426	10,924
Current portion of long-term debt [note 9]	5,370	941
Total current liabilities	74,495	61,596
Long-term debt [note 9]	82,289	47,220
Total liabilities	156,784	108,816
Commitments [notes 3 and 15]		
Shareholders' equity		
Share capital [note 10]	32,758	46,024
Retained earnings	147,353	126,761
Total shareholders' equity	180,111	172,785
	336,895	281,601

See accompanying notes

On behalf of the Board:

Allen T.Y. Chan
Director

Edmund Mak
Director

Consolidated Statements of Income and Retained Earnings

(Expressed in thousands of United States dollars, except for earnings per share information)

Years ended December 31	2002	2001
	$	$
Revenue		
Sales	187,996	121,451
Commission income	12,752	15,862
	200,748	137,313
Costs and expenses		
Cost of sales	158,089	107,094
Selling, general and administration	9,747	7,572
Depreciation and amortization	1,625	1,202
	169,461	115,868
Income from operations	31,287	21,445
Interest expense	(8,632)	(4,174)
Exchange (loss) gain on long-term debt	(3,060)	1,064
Interest income	792	916
Amortization of deferred financing costs	(199)	(199)
Write-off of other assets	(74)	–
Income before income taxes	20,114	19,052
Recovery of (Provision for) income taxes [note 11]	478	(479)
Net income for the year	20,592	18,573
Retained earnings, beginning of year	126,761	108,188
Retained earnings, end of year	147,353	126,761
Earnings per share [notes 2 and 12]		
Basic	0.27	0.25
Diluted	0.27	0.21

See accompanying notes

Consolidated Statements of Cash Flows

(Expressed in thousands of United States dollars)

Years ended December 31	2002	2001
	$	$
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income for the year	20,592	18,573
Add (deduct) items not affecting cash		
Depletion of timber holdings included in cost of sales	10,282	–
Accretion of Exchangeable Notes	4,643	1,484
Exchange loss (gain) on long-term debt	3,060	(1,064)
Depreciation and amortization	1,625	1,202
Amortization of deferred financing costs	199	199
Write-off of other assets	74	–
	40,475	20,394
Net change in non-cash working capital balances [note 13]	(27,882)	(7,541)
Cash flows from operating activities	12,593	12,853
CASH FLOWS FROM FINANCING ACTIVITIES		
Increase in bank indebtedness	10,137	19,699
Issuance of long-term debt	19,000	19,000
Increase in deferred financing costs	–	(1,023)
Repayment of long-term debt	(471)	(940)
Cash flows from financing activities	28,666	36,736
CASH FLOWS USED IN INVESTING ACTIVITIES		
Investment in capital assets	(44,187)	(45,250)
Decrease (Increase) in short-term deposits	2,397	(20,874)
Cash flows used in investing activities	(41,790)	(66,124)
Net decrease in cash and cash equivalents	(531)	(16,535)
Cash and cash equivalents, beginning of year	1,709	18,244
Cash and cash equivalents, end of year	1,178	1,709
Supplemental cash flow information		
Cash payment for interest charged to income	3,885	2,731
Cash payment for interest capitalized	2,735	805

See accompanying notes

Notes to Consolidated Financial Statements

(Tabular figures expressed in thousands of United States dollars, unless otherwise indicated.)

1. *Significant Accounting Policies*

The consolidated financial statements of Sino-Forest Corporation ["Sino-Forest" or the "Company"] have been prepared in United States dollars and in accordance with Canadian generally accepted accounting principles. 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 the PRC CJVs.

The Company's investments in wholly foreign-owned enterprises [the "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 United States 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.

INVENTORIES

Wood products are valued at the lower of average cost and net realizable value. Raw materials are valued at average cost or the greater of net realizable value and replacement cost if lower than average cost.

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 tree. 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:

Land-use rights	Over the term of the land-use rights
Buildings	20 years
Machinery and equipment	15 years
Office furniture and equipment	5 to 10 years
Vehicles	5 to 10 years

DEFERRED FINANCING COSTS

Financing costs are deferred and amortized over the term of the related long-term debt on a straight-line basis.

REVENUE RECOGNITION

Revenue from the sale and trading of wood chips and other products is recognized when the products are shipped. Revenue from the sale of standing timber is recognized when the significant risks and rewards of ownership have been transferred to the buyer. Commission income relating to wood chip and other product sales is recognized as revenue when the products are shipped and services rendered.

INCOME TAXES

The Company follows the liability method of accounting for income taxes. Under this method, future tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the substantially enacted tax rates and laws that will be in effect when the differences are expected to reverse.

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, quoted market values or 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 and cash equivalents, accounts receivable and accounts payable and accrued liabilities and long-term liabilities with interest rates based on LIBOR, are considered to approximate their fair values.

STOCK-BASED COMPENSATION PLAN

The Company has a stock option plan, which is described in Note 10. 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 CONTRACTS

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

CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of cash on hand and balances with banks and short-term deposits with original maturities of less than three months.

2. Change in Accounting Policy

Effective January 1, 2002, the Company changed its method of accounting for its stock option plan in accordance with recommendations promulgated by the Canadian Institute of Chartered Accountants. These recommendations required that stock options that can be settled in cash should be applied retroactively.

There is no impact to current and prior periods as the Company's stock option plan does not permit stock options to be settled in cash. In addition, as allowed by the new recommendations, the Company will apply the new standards prospectively for new awards of stock granted after January 1, 2002.

3. Capital Contributions and Commitments

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, and wood-based products [collectively "wood-based"] and wood chips in the PRC, and other Asia-Pacific markets. Apart from these activities, the Company also provides agency services for the sale of wood-based products and wood chips in the PRC and other Asia-Pacific markets from which it earns commission income. Capital contributions and commitments for 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 contributions was approved by the Commission of Foreign Trade and Economic Co-operation ["CFTEC"] in 1999. Up to December 31, 2002, the Company had made capital contributions of $16,275,000 [2001 – $16,275,000] to meet costs for planting, maintenance and harvesting of the PRC CJVs' tree plantations. Accordingly, the outstanding capital contributions required with respect to these five PRC CJVs as at December 31, 2002 are $1,375,000 [2001 – $1,375,000]. 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:

	2002 $	2001 $
Consolidated balance sheets		
Current assets	**5,601**	14,597
Long-term assets	**41,811**	30,267
Current liabilities	**(13,335)**	(7,670)
Long-term liabilities	**(12,582)**	(18,907)
Consolidated statements of cash flows		
Cash flows (used in) from financing activities	**(11,633)**	8,211
Cash flows used in investing activities	**(4,289)**	(7,446)

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 in April 1998. The conversion from an EJV to a WFOE [the "Leizhou WFOE"] was approved by the CFTEC 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 obtained approval to reduce the original total capital contribution of $10,000,000 to $1,400,000 in April 2000. As at December 31, 2002, Sino-Wood has made capital contributions of $1,000,000. The remaining capital contribution of $400,000 has to be contributed by May 2002. In 2002, the Company decided to dissolve the Leizhou WFOE and accordingly, the remaining capital contribution was not made. Upon dissolution of the Leizhou WFOE, the assets will be distributed to Sino-Wood.

In September 2001, Sino-Wood, through its wholly-owned subsidiaries, established a WFOE ["Jiamin WFOE"]. The principal business activity of the Jiamin WFOE is a tree plantation. The Jiamin WFOE was formed for a period of 50 years and Sino-Wood is required to contribute $1,500,000 for its 100% equity interest. As at December 31, 2002, Sino-Wood has made total contributions of $225,000 [2001 – nil]. The remaining capital contribution of $1,275,000 has to be made by September 2004.

[B] WOOD-BASED OPERATIONS

In July 1999, SFR (China) Inc. ["SFR China"], a wholly owned subsidiary of the Company, established a WFOE [the "Jiasu WFOE"]. The principal business activity of the Jiasu WFOE is to manufacture wood-based products. The Jiasu WFOE was formed for a period of 30 years and SFR China is required to contribute $10,000,000 for its 100% equity interest. As at December 31, 2002, the Company has made total contributions of $1,500,000 [2001 – $1,500,000]. The remaining capital contribution of $8,500,000 was to be contributed by July 2002. The Company is currently in the process of dissolving this Jiasu WFOE and accordingly, the remaining capital contribution was not made. Upon dissolution of the Jiasu WFOE, the assets will be distributed to SFR China.

In March 2000, SFR China established a WFOE [the "SFR WFOE"]. The principal business activity of the SFR WFOE is to manufacture wood-based products. The SFR WFOE was formed for a period of 30 years and SFR China is required to contribute $10,000,000 for its 100% equity interest. As at December 31, 2002, the Company has made total contributions of $1,908,000 [2001 - $1,795,000]. The remaining capital contribution of $8,092,000 has to be contributed by March 2003. Subsequent to the year-end, the Company has decided to apply to the government authority to extend the contribution period to June 2004.

In January 2001, SFR China established another WFOE [the "Jiafeng WFOE"] to undertake certain projects in Suzhou that will be funded by the International Finance Corporation ["IFC"], part of the World Bank Group, and other lenders. The Jiafeng WFOE was formed for a period of 50 years and SFR China is required to contribute $15,000,000 for its 100% equity interest. As at December 31, 2001, the Company has made total contributions of $2,630,000. Of the remaining capital contributions, $8,370,000 has to be contributed by July 2003 and the balance of $4,000,000 by January 2004.

4. Accounts Receivable

The Company reviews its outstanding accounts receivable and records an allowance for doubtful accounts when accounts are determined to be uncollectable. Accounts receivable are substantially from companies located in the PRC. Accounts receivable as at December 31, 2002 included $28.5 million due from three customers [2001 – $13.4 million due from three customers].

5. Inventories

Inventories consist of the following:

	2002 $	2001 $
Wood products	344	718
Raw materials	534	265
	878	983

6. Capital Assets

Capital assets consist of the following:

	2002		2001	
	COST $	ACCUMULATED DEPRECIATION AND AMORTIZATION $	COST $	ACCUMULATED DEPRECIATION AND AMORTIZATION $
Timber holdings	172,448	–	156,120	–
Machinery and equipment	50,678	2,425	44,870	959
Buildings	7,272	301	6,226	119
Land-use rights	5,277	249	4,614	109
Office furniture and equipment	740	497	674	481
Vehicles	684	306	652	245
	237,099	3,778	213,156	1,913
Less accumulated depreciation and amortization	3,778		1,913	
Net book value	233,321		211,243	

In 2001, timber holdings included the rights to 602,289 cubic meters of standing timber valued at $10.2 million acquired from the LFB as part of an agreement executed in April 1998 to exchange Sino-Wood's interest in the net assets of Leizhou EJV [note 3 (a)]. In 2002, Sino-Wood entered into an agreement with the LFB whereby it exchanged its right in the standing timber for $10.2 million. This amount will be settled by the delivery of logs to Sino-Wood in 2003 at the then current market price. Accordingly, the amount due from LFB has been included in current assets. There was no gain or loss recognized as a result of this transaction.

Land-use rights, buildings, and machinery and equipment amounting to approximately $24,566,000 [2001 – $27,978,000] are not being depreciated as the production facilities are under construction and have not yet been put into commercial operation.

7. 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 and for reimbursement of office expenses. The amounts are unsecured and non-interest bearing. Amounts due from PRC CJV partners are expected to be settled in the next twelve months.

8. Bank Indebtedness

Subsidiaries of the Company have established several revolving lines of credit facilities to a maximum of approximately $51,561,000 [2001 – $49,310,000]. These credit facilities bear interest at 4.20% to 6.44% as at December 31, 2002 [2001 – 5.02% to 6.44%] and are repayable on demand. Interest capitalized as part of the cost of assets under construction and planting for the year amounted to $923,000 [2001 – $274,000].

As at December 31, credit facilities for the following were utilized:

	2002 $	2001 $
Trust receipt loans	16,355	13,734
Bank loans	31,709	24,193
	48,064	37,927

Certain of the Company's banking facilities are secured by:
[a] charges over certain of the Company's land-use right and timber holdings which have an aggregate net book value at the balance sheet date of $9,049,000 [2001 – $nil]; and
[b] certain bank deposits at the balance sheet date of $6,469,000 [2001 – $16,572,000].

In respect of the timber holdings pledged, the PRC CJV partners have undertaken to fully counter-indemnify the Company from their 30% share of the harvested timber.

9. Long-term Debt

Long-term debt consists of the following:

	2002 $	2001 $
Equipment loan	1,411	1,882
Exchangeable Notes	28,385	10,476
Plantation loan	19,863	16,803
IFC Projects loan	38,000	19,000
	87,659	48,161
Less: long-term debt due within one year	5,370	941
	82,289	47,220

Principal repayments on the long-term debt over the next five years are as follows:

	$
2003	5,370
2004	36,302
2005	11,890
2006	11,889
2007	11,889
Thereafter	10,319
	87,659

[A] EQUIPMENT LOAN

In November 1997, Sino-Wood entered into two loan agreements for credit facilities of $4,505,000 to purchase certain machinery and equipment in connection with the construction of two particleboard mills in the PRC. 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, 2002, the interest rate on the Equipment loan was 2.5% [2001 – 2.5%].

Interest capitalized as part of the cost of assets under construction for the year amounted to $24,000 [2001 – $156,000].

[B] EXCHANGEABLE NOTES

In 1999, 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 $1.21 [equivalent of Cdn. $1.88] during the period from January 29, 2002 to January 28, 2004. Prior to January 28, 2002, Sino-Wood also had the right to require the Noteholders to exchange up to $10 million of the Exchangeable Notes in Class A Subordinate-Voting Shares under certain circumstances. The 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 consolidated 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 was classified as equity, net of issue costs.

During the year, the equity component of the Exchangeable Notes of $13,266,000 was reclassified to long-term debt as Sino-Wood's entitlement to require the Noteholders to exchange no more than $10 million of the Exchangeable Notes into Class A Subordinate-Voting Shares provided certain conditions were met had expired. As a result of this reclassification, additional interest expense of approximately $1,600,000 in each of 2002 and 2003 will be charged to operations. This additional interest expense reflects the higher guaranteed interest rate of 15% per annum that was not recognized on the equity component of the Exchangeable Notes prior to the reclassification.

Interest expense for the year was $5,643,000 [2001 – $2,484,000].

Subsequent to the year-end, Sino-Wood entered into an exchange agreement whereby the holder of the Exchangeable Notes exchanged approximately $9.8 million in principal amount of the Exchangeable Notes (having an accrued value of approximately $15.5 million) for approximately $15.5 million of convertible notes on substantially the same terms and conditions as the Convertible Instruments described in note 16. As part of the terms and conditions of the Convertible Instruments, the holder of the Exchangeable Notes was also issued 66,325 Class B shares of Sino-Wood. In the event of a listing of the shares of Sino-Wood on The Hong Kong Stock Exchange ["HKSE"] before the maturity date of the Exchangeable Notes, the Company agreed to pay the holders of the Exchangeable Notes an amount in lieu of foregone interest of approximately $2.3 million. There will not be any gain or loss recognized as a result of this transaction.

[C] PLANTATION LOAN

In 1999, 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% per annum. As at December 31, 2002, the six-month EUR LIBOR rate was 3.625% [2001 – 3.3%]. Interest expense for the year amounted to $1,367,000 [2001 – $1,345,000].

The Company has entered into an interest rate cap agreement to manage 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 of Euro 18,970,710 adjusted in accordance with the repayment schedule of the debt. The interest rate cap agreement expires in May 15, 2008.

As at December 31, 2002, the amount of the plantation loan outstanding was $19,863,000 [2001 – $16,803,000].

[D] IFC PROJECTS LOAN

During 2001, two of the Company's wholly-owned subsidiaries entered into loan agreements with the IFC and other lenders for long-term loan facilities totaling $47.5 million. First and second disbursements of the loans of $19.0 million each were received by the subsidiaries in September 2001 and February 2002, respectively. The final disbursement of $9.5 million is expected to be made before the end of the second quarter of 2003.

Proceeds from these loans are used to invest in new plantations and wood-based manufacturing facilities. The loans will be repaid in twelve equal semi-annual installments commencing on December 15, 2003, with the final installment due on June 15, 2009. The loans will bear interest at six-month LIBOR plus 3% per annum. As at December 31, 2002, the six-month LIBOR rate was 2.03%. These loans are secured by pledges over the land-use rights, buildings, machinery and equipment which have an aggregate net book value at the balance sheet date of approximately $23,830,000 [2001 – $24,477,000].

Interest capitalized as part of the cost of assets under construction for the year amounted to $1,812,000 [2001 – $375,000].

[E] COVENANTS

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

10. Share Capital

Share capital consists of the following:

	2002 $	2001 $
Authorized		
Unlimited Class A Subordinate-Voting Shares		
6,000,000 Class B Multiple-Voting Shares		
Unlimited Preference Shares, issuable in series		
Issued		
74,330,228 [including 4,649,000 issued under share purchase loans]		
Class A Subordinate-Voting Shares [2001 – 74,300,228, including		
4,649,000 issued under share purchase loans]	32,758	32,758
6,000,000 Class B Multiple-Voting Shares [2001 – 6,000,000]	–	–
	32,758	32,758
Equity component of Exchangeable Notes [note 9(b)]	–	13,266
	32,758	46,024

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, 2002 is Cdn.$66,466,253 [2001 – Cdn.$66,466,253].

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
- the registered holders of the Class B Multiple-Voting Shares have executed a Coattail Agreement under which the holders 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 attached 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 Shares and the Class B Multiple-Voting Shares.

SHARE PURCHASE LOANS

The Company had provided interest free loan to employees pursuant to the terms of the Stock Option Plan to finance the acquisition of Class A Subordinate-Voting Shares. In accordance with the terms of the Plan, the shares acquired under share purchase loans 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, 2002, $4,295,100 [2001 – $4,295,100] of these loans remained outstanding.

STOCK OPTIONS

The Company's Plan provides for the issuance of up to a maximum of 10,000,000 Class A Subordinate-Voting Shares at an exercise price equal to the market price of the Company's Class A Subordinate-Voting Shares on the date of the grant. The option period for the Plan is five years. Options granted may be vested over certain time periods within the option period, which will limit the number of options exercisable during each option year. As at December 31, 2002, options to purchase 600,000 Class A Subordinate-Voting Shares have been granted and options to purchase 9,400,000 Class A Subordinate-Voting Shares remain available to be granted under the Plan.

The following table summarizes the changes in stock options outstanding during the year:

	2002		2001	
	SHARES	WEIGHTED AVERAGE EXERCISE PRICE	SHARES	WEIGHTED AVERAGE EXERCISE PRICE
Balance, beginning of year	**925,000**	**Cdn.$1.77**	1,279,000	Cdn.$1.72
Options granted	**–**	**–**	–	–
Options exercised	**–**	**–**	(30,000)	Cdn.$0.60
Options cancelled	**(325,000)**	**Cdn.$2.21**	(324,000)	Cdn.$1.54
Balance, end of year	**600,000**	**Cdn.$1.54**	925,000	Cdn.$1.77
Exercisable at year-end	**600,000**	**Cdn.$1.54**	715,000	Cdn.$1.83

The following table summarizes the weighted average exercise prices and the weighted average remaining contractual life of the options outstanding and exercisable at December 31, 2002:

RANGE OF EXERCISE PRICES	OPTIONS OUTSTANDING	WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED AVERAGE EXERCISE PRICE	OPTIONS EXERCISABLE	WEIGHTED AVERAGE EXERCISE PRICE
Cdn.$1.50–Cdn.$1.75	600,000	2.5 years	Cdn.$1.54	600,000	Cdn.$1.54

11. Income Taxes

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

	2002 $	2001 $
Income before income taxes	20,114	18,788
Expected statutory tax rate	43.95%	43.95%
Expected income tax provision	8,840	8,257
Increase (decrease) in income taxes resulting from		
Unrecognized income tax losses arising from losses of the Company and its subsidiaries	7,799	4,828
Income tax at different rates in foreign jurisdictions	(16,161)	(12,606)
	478	(479)

The PRC WFOEs and CJVs 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% [2001 – 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, 2002, the Company has income tax losses of approximately $4,655,000, 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 $217,000 of these tax losses will expire in 2003, $705,000 in 2004, $905,000 in 2005, $825,000 in 2006, $631,000 in 2007, $680,000 in 2008 and the remainder will expire in 2009. The benefit of these losses, if realized, will be at the Canadian tax rates at the time the benefit is realized.

In addition, the Company's subsidiaries, PRC WFOEs and CJVs have incurred tax losses in Hong Kong and the PRC for which no benefit has been recognized in these consolidated financial statements. The ultimate recovery of these losses is not determinable.

12. Earnings per Share

Basic earnings per share is based on the weighted average number of Class A Subordinate-Voting and Class B Multiple-Voting Shares outstanding during the year. The Class A Subordinate-Voting Shares pledged under the Company's share purchase loans are deducted from the weighted average number of Class A Subordinate-Voting Shares outstanding in calculating basic earnings per share. Fully diluted earnings per share is based on the weighted average number of Class A Subordinate-Voting and Class B Multiple-Voting Shares outstanding, adjusted for stock options outstanding and shares acquired under share purchase loans and assumes the full conversion of the Exchangeable Notes described in Note 9 [b]. The weighted average number of Class A Subordinate-Voting and Class B Multiple-Voting Shares outstanding were as follows:

	WEIGHTED AVERAGE	
	BASIC	DILUTED
December 31, 2002	**75,682,000**	**96,468,500**
December 31, 2001	75,652,000	97,940,000

13. Change in Non-Cash Working Capital

The net change in non-cash working capital balances comprises:

	2002 $	2001 $
Cash provided by (used for):		
Accounts receivable	**(20,981)**	(4,091)
Deposit for the purchase of logs	**(6,041)**	–
Due from PRC CJV partners	**(1,822)**	(4,081)
Other receivables and prepaid expenses	**2,524**	(5,469)
Inventories	**105**	1,421
Accounts payable and accrued liabilities	**(1,169)**	4,178
Income taxes payable	**(498)**	501
	(27,882)	(7,541)

14. Segmented Information

BY INDUSTRY SEGMENT

			2002			2001
	PLANTATION $	WOOD-BASED $	TOTAL $	PLANTATION $	WOOD-BASED $	TOTAL $
Revenue from external customers						
Sale of wood chips	**113,554**	**–**	**113,554**	76,816	–	76,816
Sale of wood-based products	**–**	**55,254**	**55,254**	–	44,635	44,635
Sale of standing timber	**19,188**	**–**	**19,188**	–	–	–
Commission income	**12,752**	**–**	**12,752**	13,262	2,600	15,862
	145,494	**55,254**	**200,748**	90,078	47,235	137,313
Income (loss) from operations	**33,396**	**(2,109)**	**31,287**	20,614	831	21,445
Identifiable assets	**229,270**	**107,625**	**336,895**	189,880	91,721	281,601
Interest income	**47**	**745**	**792**	583	333	916
Interest expense	**1,367**	**7,265**	**8,632**	1,345	2,829	4,174
Depreciation and amortization	**68**	**1,557**	**1,625**	102	1,100	1,202
Additions to capital assets	**36,888**	**7,299**	**44,187**	37,625	7,625	45,250

Revenue from the Company's largest customer for the year amounted to approximately 30% [2001 – 29%] of total revenue. During the year, there were three [2001 – two] customers each individually accounted for more than 10% of the Company's revenue and this revenue in aggregate represented approximately 72% [2001 – 57%] of total revenue.

Purchases from the Company's largest vendor for the year accounted for approximately 31% [2001 – 30%] of total purchases. During the year, three [2001 – two] vendors each individually accounted for more than 10% of the Company's purchases and these purchases in aggregate represented approximately 71% [2001 – 57%] 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 countries amounted to approximately $186,546,000 [2001 – $118,673,000] and $ 1,450,000 [2001 – $2,778,000], respectively.

At December 31, 2002, approximately $944,000 [2001 – $825,000] of the Company's cash and cash equivalents and $nil [2001 – $121,000] of its short-term deposits were denominated in Chinese renminbi.

15. Commitments

As at December 31, 2002, the Company has various commitments to make capital contributions to the PRC CJVs and WFOEs, the details of which are disclosed in note 3. In addition, the Company has capital commitments, in respect of buildings, timber holdings, plant and machinery of $17,176,000 [2001 – $8,864,000]. Commitments under operating leases for land and building are as follows:

	$
2003	331
2004	338
2005	221
2006	197
2007	217
Thereafter	18,526
	19,830

16. Subsequent Event

On March 10, 2003, Sino-Wood issued $14 million of convertible instruments ("Convertible Instruments") comprised of $12 million of convertible notes and $2 million of convertible preference shares. The Convertible Instruments were issued at par value, bear interest or dividends at a rate of 4% per annum payable in semi-annual installments and have a maturity of 18 months. In the event of a listing of the shares of Sino-Wood on the HKSE before the maturity date, the Convertible Instruments will either be redeemed at the time of the listing or be converted into ordinary shares of Sino-Wood at the listing price at the option of the holders of the Convertible Instruments. If no listing takes place prior to the maturity date, the Convertible Instruments will be redeemed on the maturity date at 106.24% of their subscription price plus unpaid interest or dividends. In addition, subscribers of the Convertible Instruments were issued 59,906 Class B shares of Sino-Wood. The Class B shares have the identical attributes as the ordinary shares of Sino-Wood except that holders of Class B shares are not entitled to dividends. The Class B shares are convertible into ordinary shares on a one-for-one basis at the option of the Holders. See also note 9[b].

17. Comparative Financial Statements

The comparative consolidated financial statements have been reclassified from statements previously presented to conform to the presentation of the 2002 consolidated financial statements.

Directors and Officers

Directors

Allen T.Y. Chan

Chairman and
Chief Executive Officer,
Sino-Forest
Hong Kong

Committees:
Audit, Compensation

Director since 1994

Kai Kit (K.K.) Poon

President,
Sino-Forest
Hong Kong

Director since 1994

Kee Y. Wong, F.C.A.

Executive
Vice-President and
Chief Financial Officer,
Sino-Forest
Toronto

Committees:
Corporate Governance

Director since 1997

John (Jack) Lawrence

Chairman,
Lawrence & Company
Toronto

Committees: Audit,
Compensation (Chair)

Director since 1997

Edmund Mak

Real Estate Marketing,
Re/Max Select
Properties
Vancouver

Committees:
Audit (Chair),
Compensation,
Corporate Governance

Director since 1994

Simon Murray

Chairman,
GEMS
(General Enterprise
Management Services
Limited)
Hong Kong

Director since 1999

Officers

Allen T.Y. Chan

Chairman and
Chief Executive Officer

Kai Kit (K.K.) Poon

President

Kee Y. Wong, F.C.A.

Executive
Vice-President and
Chief Financial Officer

Hua Chen

Chief Financial Officer,
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Wei Mao Zhao

Vice-President, China

Jay Lefton

Corporate Secretary

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

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ANNUAL SHAREHOLDER MEETING
4 p.m., Friday, June 27, 2003
The Royal York Hotel
Upper Canada Room, 18th Floor
100 Front Street West
Toronto, Ontario
Canada M5J 1E3

PRODUCTION CO-ORDINATION BY STORY COMMUNICATIONS DESIGN BY RAVEI DESIGN INC.

Please Note: This report contains projections and forward-looking statements regarding future events. Such forward-looking statements are not guarantees of future performance of Sino-Forest and are subject to risks and uncertainties that could cause actual results and company plans and objectives to differ materially from those expressed in the forward-looking statements. Such risks and uncertainties include, but are not limited to, changes in the PRC and international economies; changes in currency exchange rates; changes in worldwide demand for the Company's products; changes in worldwide production and production capacity in the forest products industry; competitive pricing pressures for the Company's products; and changes in wood and timber costs.

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