



玖源生態農業科技（集團）有限公司

Ko Yo Ecological Agrotech (Group) Limited

(incorporated in the Cayman Islands with limited liability)

Annual Report 2004

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## DIRECTORS

### Executive directors

Mr. Li Weiruo  
Mr. Yuan Bai  
Ms. Chi Chuan  
Ms. Man Au Vivian  
Mr. Li Shengdi

### Independent non-executive directors

Mr. Hu Xiaoping  
Mr. Woo Che-wor, Alex  
Mr. Qian Laizhong

## COMPANY SECRETARY

Mr. Fung Wai Shing, *HKICPA, ACCA*

## QUALIFIED ACCOUNTANT

Mr. Fung Wai Shing, *HKICPA, ACCA*

## AUDIT COMMITTEE

Mr. Hu Xiaoping  
Mr. Woo Che-wor, Alex  
Mr. Qian Laizhong

## AUTHORIZED REPRESENTATIVES

Mr. Li Weiruo  
Ms. Man Au Vivian

## COMPLIANCE OFFICER

Ms. Chi Chuan

## REGISTERED OFFICE

Century Yard  
Cricket Square  
Hutchins Drive  
P.O. Box 2681 GT  
George Town  
Grand Cayman  
British West Indies

## HEAD OFFICE AND PRINCIPAL PLACE OF BUSINESS IN HONG KONG

Suite No. 02, 31st Floor, Sino Plaza  
255-257 Gloucester Road  
Causeway Bay  
Hong Kong

## SHARE REGISTRAR

Standard Registrars Limited  
G/F., Bank of East Asia Harbour View Centre  
No. 56, Gloucester Road  
Wanchai  
Hong Kong

## COMPLIANCE ADVISER

Guotai Junan Capital Limited  
27th Floor, Low Block  
Grand Millennium Plaza  
181 Queen's Road Central  
Hong Kong

## AUDITORS

PricewaterhouseCoopers  
*Certified Public Accountants*  
22nd Floor  
Prince's Building  
Central  
Hong Kong

## PRINCIPAL BANKERS

Industrial and Commercial Bank of China  
-Chengdu City Xindu Branch  
Agricultural Bank of China  
-Chengdu City Wuhou Branch  
Standard Chartered Bank  
-Central Branch

## GEM STOCK CODE

8042

## WEBSITE

[www.koyochem.com](http://www.koyochem.com)

- For the year ended 31 December 2004, the profit attributable to shareholders of the Group increased to approximately RMB33 million, which represents a growth of 36% as compared to 2003.
- Basic earnings per share of the Group was approximately RMB7.8 cents for the year ended 31 December 2004.
- For the year ended 31 December 2004, audited turnover and sale quantities increased by approximately 50% and 31% respectively as compared to 2003.
- The sale quantities of BB Fertilizers of the Group increased to 107,605 tonnes, which represents a growth of 59% as compared with 2003.
- The Group completed the first export business of urea to Vietnam during the first quarter of 2004.
- The Group acquired a urea production line through auction in April 2004.
- The Group acquired the production facilities of ammonia and ammonium bicarbonate in Dazhu District, Sichuan Province, the PRC in December 2004.
- The Directors have proposed to pay a final dividend of HK1.15 cents per share for the year ended 31 December 2004, which represents a growth of 58% as compared with 2003.

## TO SHAREHOLDERS

I am pleased to present the annual report of Ko Yo Ecological Agrotech (Group) Limited (the "Company") and its subsidiaries (collectively the "Group") for the year ended 31 December 2004.

## ACCOMPLISHMENT

BB Fertilizers of the Group achieved significant growth in terms of sale quantities and unit selling prices, which represented by 59% and 21% respectively compared that of last year. Also, the Group successfully acquired production plants of urea, ammonia and ammonium bicarbonate through auction and acquisition during the year under review.

## BUSINESS REVIEW

The difficult times caused by the disease "SARS" were over. In the year under review, the Group was benefited by the growth of overall economy in the People's Republic of China (the "PRC") and achieved a substantial growth in both turnover and profit attributable to shareholders.

For the year ended 31 December 2004, the Group's turnover amounted to approximately RMB423 million, which represented a growth of approximately 50% as compared to the corresponding year in 2003. The sale quantities of the Group increased to approximately 401,000 tonnes, an increase of 31% compared with approximately 307,000 tonnes last year. While audited profit attributable to shareholders amounted to approximately RMB33 million, which represented a growth of 36% as compared to last year. A final dividend of HK1.15 cents per share for the year ended 31 December 2004 was recommended.

The year 2004 is another year of challenges as well as opportunities. The continuous shortage of electricity and natural gas supply in the country, coupled with the implementation of Road Safety and Traffic Act on 1 May 2004, resulted in a surge in production costs and transportation costs. However, the increase in the prices of the products far offset the surge in costs. During the year, the selling prices of chemical fertilizers and chemical products increased significantly due to increase in oil prices globally as well as the incentives put forward by the central government of the PRC to the peasants by implementing measures such as increased tax allowances for peasants and provided more subsidies for peasants growing food crops. Also, the rise in food price led to increasing demand for fertilizers. The increase in raw materials price was driven by the insufficient transport capacity and the corresponding shortage of resources.

In addition, owing to the increased marketing effort in the brand name of the Group as well as the products, the BB Fertilizers sales grew significantly during the year and had become a star product and the major revenue stream of the Group. The listing on the Stock Exchange of Hong Kong Limited (the "Stock Exchange") in 2003 raised the profile of the Group. The Group expanded its production capacity through acquisition of production plants and established Dazhou City Dazhu Ko Yo Chemical Industry Co., Limited ("Dazhu Ko Yo Chemical") which is believed to be the future growth momentum of the Group.

## PROSPECTS

### Industry Overview

It is the PRC government's policy to boost the agricultural industry. The Prime Minister of the PRC has announced a series of policies and tax exemption to assist the domestic agricultural sector in the National Assembly held in March 2004. Under the direction laid by the Central Government, the Group is optimistic about the future growth of consumption in chemical fertilizers.

At the Rural Works Conference of the CPC Central Committee concluded in Beijing on 29 December 2004, it stated that the relevant authorities would maintain its strong effort at agricultural and rural works in 2005, continue to strive to increase the food production in 2005 as compared to 2004. The measures include expanding the cultivated area for food crops, broadening the base of the tax allowance base and increasing the tax allowance for peasants and agricultural industries and providing more subsidies for peasants growing food crops.

The resumption of the 50% refund of value-added tax of urea sale, which was stated in the Emergency Notice Regarding the Production and Supply and Stabilizing the Price of Fertilizers issued on 2 January 2004 by six ministries of the State, would remain unchanged until 31 December 2005.

The directors of the Company ("Directors") believe that the above policies put forward by the central government would have a positive impact on the demand for and purchasing power of fertilizers.

### Forward Objectives and Strategies

For the year 2005, BB Fertilizers will continue to be the star product of the Group and more resources will be allocated to broaden the distribution channel and strengthen the brand name on a national basis. Other than advertising and marketing works, the Group will increase the number of agricultural teams to build a nationwide agricultural service network system to support the post-sale services. Also, the directors expect that the price of BB Fertilizers will remain competitive.

Another principal product of the Group, urea will be the major revenue contributor in 2005. The Group's urea production plant in Dazhu District, Sichuan Province, the PRC has commenced operation in January 2005, which could achieve maximum production capacity of around 150 tonnes per day.

The Directors expect that the increase in export of domestic fertilizers, as caused by the impact of oil price in international markets and tight domestic supply of electricity and natural gas will continue to drive up the domestic market prices of chemical fertilizers and chemical products. The Group believes that such market conditions will not be altered in near future, which will provide an impetus on the market price of the Group's products.

### **PROSPECTS** *(Continued)*

#### **Forward Objectives and Strategies** *(Continued)*

The Group will continue to enhance its production capacity, particularly the newly acquired production plants in Dazhu District, which is expected to be the growth momentum of the Group in terms of chemical products business.

The Group will further implement post-acquisition integration and technological improvement for production plants in Dazhu District. It will leverage on its foundation of the existing production capacity of ammonium bicarbonate and urea and aim at realizing the objective of production management in 2005. It will strive to become another major production base in addition to Chengdu Ko Yo Chemical Industry Co., Limited ("Chengdu Ko Yo Chemical"). This would also provide opportunities for growth of the Group's profit.

The Group will continue to carry out technological modification, equipment renovation and repair projects such as the "Energy-saving modification project" and "Sodium carbonate equipment repair project", with an aim to maximize the growth of the production capacity, sale and profit of the Group.

### **APPRECIATION**

I wish to express my appreciation to all shareholders for their trust and continuous support for the Company, and my sincere thanks to all staff for their dedication and efforts throughout the year and valuable contribution to the Group's operating results for the year. The board of Directors (the "Board"), the management and all staff will continue to work diligently to achieve greater success for the Group and to provide shareholders with returns.

**Li Weiruo**

Chairman

Hong Kong, 23 March 2005



## FINANCIAL PERFORMANCE

### Results

For the year ended 31 December 2004, the Group continued its principal activities of manufacture and distribution of chemical fertilizers and chemical products, including BB Fertilizers, sodium carbonate, urea, ammonium chloride, and ammonia.

Through assets acquisition during the year, ammonium bicarbonate was added into the product line of the Group, which generated turnover of RMB23 million for the year ended 31 December 2004. During the year under review, the Group achieved net sales record of approximately RMB423 million, an increase of 50% as compared to previous year. Such increase was due to significant increase in both selling price and sales volume of the Group's products. Compared to previous year, the selling prices of the Group's products increased by approximately 12% to 23%, which was due to surge in raw materials cost. The total sale volume of the Group increased from 307,000 tonnes in 2003 to 401,000 tonnes in 2004, which was attributable to the significant growth of sales of BB Fertilizers and exporting urea to Vietnam. The profit attributable to shareholders of the Group amounted to approximately RMB33 million, representing a growth of approximately 36% as compared to last year. Basic earnings per share amounted to approximately RMB7.8 cents.

### Dividends

The Directors proposed a final dividend of HK 1.15 cents per share (2003: HK 0.73 cent per share) for the year ended 31 December 2004. A total of HK 1.45 cents per share were declared for the year ended 31 December 2004 (2003: HK1.33 cents per share).

### Cost and Profit Margin

Cost of sales of the Group amounted to approximately RMB337 million, representing an increase of 52% as compared to the figure in 2003. The reasons of increase in cost of sale were increase in sale volume of the Group and unit cost of raw materials. The Road Safety and Traffic Act of the PRC became effective on 1 May 2004, which imposed strict control on overloading vehicles. Under this Act, transportation cost of raw materials dramatically increased, which increased the overall unit cost of industrial salts and coals procured by the Group. Tight electricity and natural gas supply increased the unit cost of electricity and natural gas, which surged the cost of sales.

Gross profit margin of the Group decreased slightly from 21.5% in 2003 to 20.4% in 2004. The overall decrease in gross profit margin was due to new businesses of ammonium bicarbonate and exporting urea operating at lower gross profit margin. Excluding gross profit portion of ammonium bicarbonate and export business, the Group's gross profit margin increased to 24.1%, which indicated the efforts of cost control during the year.

### FINANCIAL PERFORMANCE *(Continued)*

#### Cost and Profit Margin *(Continued)*

During the year under review, distribution costs and administrative expenses of the Group experienced relatively substantial increase as compared to last year. Distribution costs increased by 46% compared with last year as the growth in sale volume of the Group. The distribution costs over sale ratio decreased from 0.054 in 2003 to 0.052 in 2004. Even though the implementation of Road Safety and Traffic Act of the PRC increased the transportation cost of the Group, the effect was eliminated by the establishment of Dezhou Ko Yo Compound Fertilizer Co., Limited (“Dezhou Ko Yo Compound”) in Shandong province, the PRC which shortened the transportation routes through direct distribution of BB Fertilizers from Shandong province to northern China.

In comparison with last year, there was a substantial increase in administrative expenses of the Group by 30% from RMB22 million in 2003 to RMB28 million in 2004. The increase was mainly attributable to the professional fee of approximately RMB4 million incurred by the Company in connection with its application for listing by way of introduction on the Main Board of the Stock Exchange.

Starting from the year under review, Chengdu Ko Yo Chemical and Chengdu Ko Yo Compound Fertilizer Co., Limited (“Chengdu Ko Yo Compound”) accrued provision of Enterprise Income Tax amounting to approximately RMB1.3 million, which charged at 7.5% of their assessable profits.

### PRODUCTS

#### BB Fertilizers

There has been a significant recovery in growth trend of BB Fertilizers of the Group. Net sales of BB Fertilizers of the Group amounted to RMB155 million, representing a growth of 92% as compared to last year, and accounted for 37% of the Group’s aggregate net sales. The growth of BB Fertilizers was attributable to the efforts of the marketing teams of the Group, which strived to develop the market and strengthen the brand name.

#### Sodium Carbonate and Ammonium Chloride

The net sales of sodium carbonate and ammonium chloride amounted to RMB84 million and RMB45 million, which increased by 19% and 11% respectively as compared to previous year, which accounted for approximately 20% and 11% of the Group’s aggregate net sales respectively.

#### Urea

The net sales of urea increased by 27% to RMB105 million in 2004 as compared to last year, which accounted for 25% of the Group’s aggregate net sales. During the year under review, the Group exported urea to Vietnam as the first overseas sale of the Group.

## PRODUCTS *(Continued)*

### Ammonia and Ammonium Bicarbonate

The net sales of ammonia increased by 58% to RMB10 million in 2004 as compared to last year, which accounted for 2% of the Group's aggregate net sales. Through acquisition during the year under review, net sales of RMB23 million of ammonium bicarbonate was added to the Group's turnover, which accounted for 5% of the Group's aggregate net sales.

## MARKETS

During the year under review, the selling price of the Group's products increased continuously due to the domestic market trend. Through acquisitions during the year, the Group increased its production capacity and product portfolio including ammonium bicarbonate, which is low-value chemical fertilizer and not competing with the Group's urea in the chemical fertilizers market.

The Group's distribution network of BB Fertilizers expanded to the Autonomous Regions of Ningxia and Inner Mongolia. New series of BB Fertilizers for onion and ramie were launched during the year.

## PRODUCTION CAPACITY

During the year under review, the Group carried out various production facilities overhaul to enhance the production efficiency and boost the production capacity.

In April 2004, Chengdu Ko Yo Chemical acquired a urea production line in Dazhou City, Sichuan Province, the PRC by way of auction.

In the same month 2004, Chengdu Ko Yo Chemical leased the production facilities of Dazhu Hongsen Chemical Industry Co., Limited ("Dazhu Hongsen Chemical"). The Group subsequently acquired the assets of Dazhu Hongsen Chemical in December 2004 and set up Dazhu Ko Yo Chemical. The trial production of the urea production line was successfully carried out on 12 January 2005, with an annual production capacity of approximately 40,000 tonnes. Such acquisition represents a successful expansion in the production scale, production capacity and sale of the Group.

## AWARDS & RECOGNITIONS

During the year under review, BB Fertilizers of the Group was awarded the "Green Product Award" by China Environmental Protection Foundation in March 2004. Chengdu Ko Yo Compound had passed the ISO9001:2000 accreditation on 14 June 2004. Chengdu Ko Yo Chemical had also accredited as the "Outstanding Private Chemical Enterprises of Sichuan Province" in January 2004, the "50 Largest Industrial Enterprises of Chengdu" by the People's Government of Chengdu in April 2004 and the "Private Enterprise with Outstanding Contribution" by the People's Government of Xindu County in November 2004.

### LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE

As at 31 December 2004, the Group had net current assets of approximately RMB1,046,000. Current assets as at 31 December 2004 comprised cash and bank deposits of approximately RMB13,926,000, pledged bank deposits of approximately RMB53,940,000, inventories of approximately RMB51,037,000, trade receivables of approximately RMB10,642,000 and prepayments and other current assets of approximately RMB36,160,000. Current liabilities as at 31 December 2004 comprised short-term bank loans of approximately RMB95,430,000, trade and notes payables of approximately RMB27,566,000, deposits from customers of approximately RMB17,225,000 and accrued charges and other payables of approximately RMB24,438,000.

### CAPITAL COMMITMENTS

As at 31 December 2004, the Group had outstanding capital commitments of approximately RMB4,342,000.

### FINANCIAL RESOURCES

As at 31 December 2004, the Group had cash and bank deposits of approximately RMB13,926,000 and pledged bank deposits of approximately RMB53,940,000. The Company intends to finance the Group's future operations, capital expenditure and other capital requirements with the existing bank balances and the listing proceeds.

As at 31 December 2004, the total bank loans and notes payable balances of the Group amounted to RMB141,400,000 and bank facilities of approximately RMB20,000,000 were not utilised.

### GEARING RATIO

The Group's gearing ratios were approximately 58% and 54% as at 31 December 2004 and 31 December 2003 respectively. The gearing ratios were calculated based on total liabilities over total assets as at the respective balance sheet dates.

### CONTINGENT LIABILITIES

The Group had no significant contingent liabilities as at 31 December 2004.

### MATERIAL ACQUISITION/DISPOSAL

Other than the acquisition of production plants of Dazhu Hongsen Chemical as per announcement dated 7 January 2005, there was no other material acquisition in the year 2004 which would have been required to be disclosed under the Rules Governing the Listing of Securities on Growth Enterprise Market of the Stock Exchange ("GEM Listing Rules").

### SEGMENTAL INFORMATION

All the Group's activities are primarily conducted in the PRC and are within the same business segment. Accordingly, neither analysis by geographical segments nor analysis by business segments is presented.

## DETAILS OF FUTURE PLANS FOR MATERIAL INVESTMENT OR CAPITAL ASSETS

The Directors do not have any future plans for material investment or capital assets.

## EXPOSURE ON EXCHANGE RATE FLUCTUATION

Since most of the income and expenditure of the Group were received and paid in RMB, the local currency of the place where the Group primarily operates in, the Directors do not consider that the Group was significantly exposed to any foreign currency exchange risk.

## CHARGES ON THE GROUP'S ASSETS

As at 31 December 2004, certain land use rights and buildings with a total net book value of approximately RMB69,116,000 (2003: RMB70,962,000), plant and machinery with a total net book value of approximately RMB23,675,000 (2003: RMB29,248,000) and bank deposits approximately RMB53,940,000 (2003: RMB13,032,000) were pledged as collateral for the Group's bank loans and notes payable.

## DIVIDEND

The Directors recommend the payment of a final dividend of HK1.15 cents per share to the shareholders whose names appear on the register of members of the Company as at the close of business on 26 April 2005. The dividend will be payable on 24 May 2005. The register of members of the Company will be closed from 21 April 2005 to 26 April 2005, both days inclusive, during which period no share transfer shall be effected. In order to qualify for the final dividend, all instruments of transfers accompanied by the relevant share certificates must be lodged with the Company's share registrar, Standard Registrars Limited, at G/F., Bank of East Asia Harbour View Centre, 56 Gloucester Road, Wanchai, Hong Kong for registration by no later than 4:00 p.m. on 20 April 2005.

## NUMBER OF EMPLOYEES AND REMUNERATION

As at 31 December 2004, the Group had 1,857 (2003: 1,368) employees, comprising 8 (2003: 11) in management, 115 (2003: 70) in finance and administration, 1,651 (2003: 1,212) in production, 76 (2003: 68) in sales and marketing and 7 (2003: 7) in research and development. 1,851 (2003: 1,362) of these employees were located in the PRC and 6 (2003: 6) were located in Hong Kong.

Pension schemes of the Group are set out in Note 2(k)(ii) to accounts.

## COMPARISON OF BUSINESS OBJECTIVES WITH ACTUAL BUSINESS PROGRESS

On 10 July 2003, the Company obtained net proceeds, after deducting all relevant share issue expenses, of approximately HK\$28.4 million from the new issue of shares by way of public offer and placing. Up to 31 December 2004, the Group has applied the net proceeds as follows:

	Use of proceeds extracted from the prospectus <i>HK\$ Million</i>	Actual amount used up to 31 December 2004 <i>HK\$ Million</i>	Remaining net proceeds <i>HK\$ Million</i>
Establishment of additional production facilities, purchase of equipment for BB Fertilizers and working capital of BB Fertilizers	18	18	—
Development of new products, product research and assessment	5	1.7	3.3
Advertising and promotion of new products and expansion of the Group's sales force	5	5	—
Total	<u>28</u>	<u>24.7</u>	<u>3.3</u>

The remaining net proceeds as at 31 December 2004 amounted to approximately RMB3.3 million, which have been placed as interest bearing deposits in banks in the PRC.

**COMPARISON OF BUSINESS OBJECTIVES WITH ACTUAL BUSINESS PROGRESS** *(Continued)*

Comparison of the business objectives set out in the prospectus of the Company dated 30 June 2003 with the actual business progress for the period from 10 July 2003 to 31 December 2004 are as follows:

**Business objectives as stated in prospectus**

**Actual business progress**

*Expansion of production capacity/upgrading of its production facilities*

To increase the production volume of BB Fertilizers through new production plant with total production capacity of 600,000 tonnes per annum

The current production capacity of BB Fertilizers are 400,000 tonnes per annum. The Board has decided to temporarily postpone the plan of new production plant of BB Fertilizers as the existing production capacity of BB Fertilizers can satisfy the foreseeable growth of sales volume. The resources have been utilized as working capital of Chengdu Ko Yo Compound to increase the raw material inventories of BB Fertilizers.

To upgrade the production line of urea by purchasing additional compressor machines, pumps and heat exchangers, with the aim of producing larger granules of urea

Instead of upgrading the existing urea production line, the Group acquired a production plant of urea to increase the production capacity of urea of the Group. The Board has decided to temporarily postpone the plan of upgrading a larger granules production line of urea.

To look for opportunities to acquire a suitable state-owned chemical fertilizer manufacturer

The Group acquired a production plants of ammonia and ammonium bicarbonate during the year under review.

*Research and development of new products*

To develop and launch a new series of BB Fertilizers

New series of BB Fertilizers for onion and ramie are launched into the market in the second half of 2004. The new series of BB Fertilizers for flowers have not yet developed during the year 2004.

To cooperate with research team of Soil and Fertilizers Institute of Sichuan Academy of Agricultural Science

Evaluation of existing species of BB Fertilizers and modification research of formulae of BB Fertilizers has completed.

To identify new research projects

The Board has decided to postpone the plan in order to concentrate the resources on marketing BB Fertilizers.

### COMPARISON OF BUSINESS OBJECTIVES WITH ACTUAL BUSINESS PROGRESS *(Continued)*

#### **Business objectives as stated in prospectus**

To conduct research and development of multi-purpose BB Fertilizers

#### **Actual business progress**

The Board has decided to postpone the plan in order to concentrate the resources on marketing BB Fertilizers.

#### ***Marketing and brand building of the Group's products***

To expand the Group's distribution network, promotion of brand name of BB Fertilizers

The Group distribution network expanded to Autonomous Regions of Ningxia and Inner Mongolia.

To establish a database on nation-wide information on soil texture and crops distributions, supply of raw materials, product formulae and customer information

The database on nation-wide information has completed.

To establish representative offices

Instead of establishing representative offices, the Group has allocated more resources to communication with distributors, which achieved satisfactory result during the year under review. Therefore, the Board has decided to postpone the plan of establishing representative offices.

#### ***Human resources***

To increase production staff, marketing staff, technical staff and agricultural service staff

Compared with 2003, the Group additionally recruited 439 production staff, 8 marketing staff and 1 agricultural service staff.



### EXECUTIVE DIRECTORS

Mr. Li Weiruo, aged 51, is the Chairman of the Board, Executive President and the founder of the Group. He graduated from Sichuan Institute of Finance and Economics with a certificate in economics in 1985. Mr. Li has over 20 years' experience in corporate management in the PRC. He was awarded a certificate for "Chief Economists of Large-to-Medium Sized Enterprises in the PRC" after completing "The Study Course for Chief Economists of Large-to-Medium Sized Enterprises" commissioned by the State Economics Commission at the Southwest University of Finance and Economics in 1986. He is one of the authors of "Modern Corporate Management" which was published by the Sichuan Education Publisher. Mr. Li was the former Vice-director of China Nonferrous Metal Corporation in Chengdu. Mr. Li moved to Hong Kong in 1994 and became a permanent resident of Hong Kong in 2001. He was appointed as an invited member of the Chinese People's Political Consultative Conference of Sichuan Province in 2003. Mr. Li is responsible for the overall management, strategic planning and business development of the Group.

Mr. Yuan Bai, aged 46, is the Executive Vice President of the Group. Mr. Yuan is responsible for the cost management and general operations and research and development of the Group. Mr. Yuan graduated from Northeast Institute of Technology with a bachelor degree in engineering in 1982 and obtained a certificate as Senior Engineer in 1992. Mr. Yuan studied economy management in Qinghua University from September 1995 to March 1996. Prior to joining the Group in August 1999, Mr. Yuan was the Deputy General Manager of Chongqing Sanjiu Industrial Co., Ltd., which focused on the manufacture and trading of non-ferrous metal. Mr. Yuan was elected as a people's delegate of the first session of the People's Congress of Chongqing in 1997.

Ms. Chi Chuan, aged 49, is the Compliance Officer and Executive Vice President of the Group. She graduated from Sichuan Normal College with a bachelor degree in science in 1982. Ms. Chi has over 10 years' experience in finance and accounting. Prior to joining the Group in July 1999, Ms. Chi was the finance manager of Leshan Economic and Trade General Company, a trading company in the PRC. Ms. Chi is primarily responsible for the financial management and general operations of the Group since she joined the Group in July 1999.

Ms. Man Au Vivian, aged 41, is responsible for business development and investment activities of the Group. Ms. Man graduated from the University of International Business and Economics with a bachelor degree in economics in 1986. Ms. Man has over 15 years' experience in international trade. She formerly worked for China National Light Industrial Products Import and Export Corporation of MOFTEC. She joined the Group in January 1997.

Mr. Li Shengdi, aged 52, is a Director of Chengdu Ko Yo Chemical and Chengdu Ko Yo Compound respectively. He graduated from Chinese Communist Party School with a degree majoring economics and was entitled as an economist. Prior to joining the Group, he was the deputy manager of China Nonferrous Huludao Zinc Corporation, from 1971 to 1993, general manager of Hainan Hui Yuantang Medicine Co., Ltd. from 1996 to 1999 and general manager of Shanghai Haos Water Rectified Co., Ltd., a Sino-US joint venture from 2002 to 2003. Mr. Li joined the Group in October 2003 and was appointed as a Director of the Company on 29 April 2004. He is currently responsible for the administration and production operations of the Group.

## DIRECTORS AND SENIOR MANAGEMENT

### INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Hu Xiaoping, aged 54, is an independent non-executive director. He obtained a bachelor degree in Economics from Sichuan Institute of Finance and Economics in 1982 and a master degree in Economics from Southwest University of Finance and Economics in 1987. Mr. Hu is currently the head of the Economics Research Centre of the Southwest University of Finance and Economics. Mr. Hu has been involved in various research projects at both the provincial and state level and has published numerous articles in financial and economics publications in the PRC. He was appointed as an independent non-executive director in June 2003.

Mr. Woo Che-wor, Alex, aged 53, is an independent non-executive director. Mr. Woo has been the Chairman and CEO of STI Certified Products Inc., a private company in California, U.S.A. since February 1998. From January 1986 to December 1987, Mr. Woo was the corporate treasurer of Fairchild Semiconductor Corporation, a multi-national semiconductor company with its headquarters in California, U.S.A.. Mr. Woo is qualified as Certified Management Accountant from Chartered Institute of Management Accountants of England and obtained an M.B.A. from San Jose State University of the U.S.A. in 1987. He was appointed as an independent non-executive director in June 2003.

Mr. Qian Laizhong, aged 62, is an independent non-executive director. Mr. Qian graduated from Sichuan Fine Arts Institute in 1968. Over the past 20 years, Mr. Qian actively participated in cultural and economical researches and publishes in Sichuan province, the PRC. Currently, Mr. Qian is a member of Sichuan Provincial Committee of Chinese Peoples Political Consultative Conference. He was appointed as an independent non-executive director on 16 August 2004.

### SENIOR MANAGEMENT

Mr. Zhu Changhou, aged 66, is the deputy general manager and chief engineer of Chengdu Ko Yo Chemical. He obtained a certificate of chemistry in Luzhou Chemical College and has over 18 years' experience in developing and analyzing chemical products. Mr. Zhu is also a director of Sichuan Chemical Association and the PRC Chemical Association. Prior to joining the Group, Mr. Zhu was the deputy chief engineer of Luzhou Natural Gas Chemical Corporation, which focused on the manufacture of chemical products. Mr. Zhu is primarily responsible for Chengdu Ko Yo Chemical's production and product research and development. He joined the Group in 1999.

Mr. Mai Zixun, aged 57, is the general manager of Chengdu Ko Yo Compound. He graduated from Sichuan Broadcasting and Television University. Mr. Mai was formerly the General Manager of Zhuhai Gree Magneto-Electronic Co., Ltd., which focused on the manufacture of electronics products. He joined the Group in June 2001 and is responsible for the sales and marketing activities of Chengdu Ko Yo Compound.

### SENIOR MANAGEMENT *(Continued)*

Mr. Li Feng, aged 47, is the deputy general manager of Chengdu Ko Yo Compound and is responsible for Chengdu Ko Yo Compound's sales and marketing activities. He graduated from Chongqing Steel Corporation Profession University. Prior to joining the Group in February 2000, Mr. Li was the manager of a branch office of an import and export company in Sichuan province, the PRC which concentrated on the production materials trading business.

Mr. Fung Wai Shing, aged 35, is the financial controller of the Group and is responsible for financial management of the Group. He graduated from University of London with bachelor degree in banking and finance. He is an associate member of each of the Hong Kong Institute of Certified Public Accountants and Association of Chartered Certified Accountants. Prior to joining the Group in February 2002, he was a manager of B&M Consultants Limited in Hong Kong.

## REPORT OF THE DIRECTORS

The Directors have the pleasure of presenting their report together with the audited accounts of the Company and its subsidiaries for the year ended 31 December 2004.

### GROUP REORGANIZATION

The Company was incorporated in the Cayman Islands on 11 February 2002 as an exempted company with limited liability under the Companies Law Cap. 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands.

The Group reorganized its structure on 10 June 2003 in preparation for the listing of the Company's shares on Growth Enterprise Market ("GEM") of the Stock Exchange of Hong Kong. The Company became the holding company of the companies now comprising the Group. Details of the reorganization are set out in the prospectus of the Company dated 30 June 2003. The shares of the Company were listed on GEM of the Stock Exchange on 10 July 2003.

### PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding. Its subsidiaries are principally engaged in the research and development, manufacture, marketing and distribution of chemical products, chemical fertilizers and BB Fertilizers.

### RESULTS AND APPROPRIATIONS

Details of the Group's profits for the year ended 31 December 2004 are set out in the consolidated profit and loss account.

The Directors recommend the payment of a final dividend of HK1.15 cents per share, totalling approximately RMB5,142,000 for the year ended 31 December 2004 (2003: RMB3,250,000).

### SHARE CAPITAL

Details of movements in share capital of the Company are set out in Note 24 to the accounts.

### RESERVES

Movements in the reserves of the Group and of the Company during the year are set out in Note 25 to the accounts.

### DISTRIBUTABLE RESERVES

Distributable reserves of the Company as at 31 December 2004 amounted to approximately RMB61,585,000 (2003: RMB60,519,000).



### **RIGHTS OF DIRECTORS AND EMPLOYEES TO ACQUIRE SHARES OR DEBENTURES**

During the year, certain options were granted to certain employees of the Company under the share option scheme adopted by the Company on 10 June 2003 and amended at an extraordinary general meeting on 28 July 2004 (the “Share Option Scheme”). A summary of the principle terms and conditions of the Share Option Scheme is set out under the section headed “Share Option Scheme” in Appendix IV of the prospectus of the Company dated 30 June 2003. The amendments of the Share Option Scheme are explained in the announcement and circular of the Company dated 12 July 2004.

### **PRE-EMPTIVE RIGHTS**

There is no provision for pre-emptive rights under the Company’s articles of association and there is no restriction against such rights under the Company Law (Law 3 of 1961, as consolidated and revised) of the Cayman Islands, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

### **FIVE YEAR FINANCIAL SUMMARY**

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out in page 69.

### **FIXED ASSETS**

Details of movements in fixed assets of the Group during the year are set out in Note 14 to the accounts.

## CONNECTED TRANSACTIONS

The continuing connected transactions are as follows:

On 1 January 2004, Dezhou Ko Yo Compound a non-wholly owned subsidiary of the Company, entered into a lease agreement with Dezhou Agricultural Production Information Company (“JV Partner”), to rent a piece of land with a site area of approximately 7,353 sq.m. together with 6 buildings with a gross floor area of approximately 3,469 sq.m. and a railway with a length of approximately 134 meters elected on the said piece of land and together with related facilities, all located at No.1 Shuichang Road, Commercial and Trade Development Zone, Decheng District, Dezhou City, Shandong Province, the PRC for a term of 20 years commencing from 1 January 2004 to 31 December 2023. The annual rent is RMB250,000 for the first year, which is unchanged for the year 2005. Such transaction was exempted from the reporting, announcement and independent shareholders’ approval requirement.

On 4 June 2004, Dezhou Ko Yo Compound and the JV Partner have entered into the BB Fertilizers Sales and Operation Agreement; and the Phosphate Fertilizers Purchase Agreement for a term of one year commencing from 4 June 2004. Pursuant to the BB Fertilizers Sales and Operation Agreement, Dezhou Ko Yo Compound agrees to appoint the JV Partner as the sole distributor of BB Fertilizers (at no fees) in Dezhou city, Shandong province, the PRC, and to supply an aggregate of approximately (no minimum sale quantities requirement but not more than) 5,000 tonnes of BB Fertilizers per annum to the JV Partner. Based on the Group’s historical sale price of BB Fertilizers, the estimated maximum aggregate annual purchase price payable by the JV Partner under the BB Fertilizers Sales and Operation Agreement will not exceed RMB6,000,000. Pursuant to the Phosphate Fertilizers Purchase Agreement, the JV Partner agrees to supply to Dezhou Ko Yo Compound phosphate fertilizers of an aggregate quantity of approximately 2,000 tonnes per annum. Based on the historical prices for the purchase of phosphate fertilizers from independent third party suppliers, the estimated maximum aggregate annual purchase price payable by Dezhou Ko Yo Compound under the Phosphate Fertilizers Purchase Agreement will not exceed RMB3,000,000.

Based on the estimated maximum aggregate annual purchase price payable under the BB Fertilizers Sales and Operation Agreement and the Phosphate Fertilizers Purchase Agreement, the transactions were not subject to independent shareholders’ approval in accordance with the GEM Listing Rules, but were subject to the reporting and announcement requirements as set out in the GEM Listing Rules.

For the year ended 31 December 2004, the aggregate sale volume and price payable under the BB Fertilizers Sales and Operation Agreement were 4,873 tonnes and RMB7,619,014 respectively, which exceeded the cap of RMB6,000,000 by approximately 27%. The aggregate purchase volume and price payable of transactions under the Phosphate Fertilizers Purchase Agreement were 366 tonnes and RMB859,235 respectively, which did not exceed the cap of RMB3,000,000. The aggregate price payable under the BB Fertilizers Sales and Operation Agreement and the Phosphate Fertilizers Purchase Agreement amounted to RMB8,478,249, and therefore no independent shareholders’ approval was required but was still subject to the reporting and announcement requirements as set out in the GEM Listing Rules.

**CONNECTED TRANSACTIONS** *(Continued)*

During the year under review, the marketing teams of the Group continuously monitored the sale volume of the BB Fertilizers to JV Partner within maximum sales quantities of 5,000 tonnes, but failed to monitor the effect of the growth of selling prices of the BB Fertilizers, which resulted in exceeding the cap of the BB Fertilizers Sales and Operation Agreement. The growth in selling prices of the BB Fertilizers was in line with the overall domestic growth in market prices of chemical fertilizers.

During the year ended 31 December 2004, the Group implemented strict control on the selling price of the BB Fertilizers and purchase price of phosphate fertilizers under the BB Fertilizers Sales and Operation Agreement and the Phosphate Fertilizers Purchase Agreement with the JV Partner in order to maintain the transaction prices in fair and reasonable terms. Under the BB Fertilizers Sales and Operation Agreement, Dezhou Ko Yo Compound sold the BB Fertilizers to the JV Partner at average selling price approximately 1% higher than the selling price of the BB Fertilizers to independent third party distributors. Under the Phosphate Fertilizers Purchase Agreement, Dezhou Ko Yo Compound purchased the phosphate fertilizers from the JV Partner at average purchase prices approximately 1% lower than the purchase prices of phosphate fertilizers from independent third party suppliers. The JV Partner took the profit margin into account and proposed to terminate the BB Fertilizers Sales and Operation Agreement and the Phosphate Fertilizers Purchase Agreement with effect from 1 January 2005.

The Board also evaluated the benefits of the continuing connected transactions between Dezhou Ko Yo Compound and JV Partner. During the evaluation, no sale or purchase transaction was concluded with the JV Partner because the sale quantities of the BB Fertilizers almost reached the maximum quantities of the BB Fertilizers Sales and Operation Agreement and the JV Partner was not willing to sell phosphate fertilizers at a price lower than the market level. The Board considers that termination of the agreements of continuing connected transactions with the JV Partner will have insignificant impact on the Group's operation as there will be other independent third party distributors to take over the role of the JV Partner. The Board decides to terminate the BB Fertilizers Sales and Operation Agreement and the Phosphate Fertilizers Purchase Agreement effective from 1 January 2005 without any compensation from Dezhou Ko Yo Compound or the JV Partner, which was mutually agreed with each other.

Dezhou Ko Yo Compound is a non-wholly owned subsidiary of the Company, and in respect of which 80 per cent. of its equity interest is indirectly owned by the Company, and the remaining 20 per cent. of its equity interest is owned by the JV Partner. Accordingly, the JV Partner is a substantial shareholder of Dezhou Ko Yo Compound and hence a connected person of the Company under the GEM Listing Rules.

The above continuing connected transactions have been reviewed by the independent non-executive directors of the Company. The independent non-executive directors have confirmed that the continuing connected transactions have been entered into (a) in the ordinary and usual course of business of the Group; (b) on normal commercial terms or on terms not less favourable to the Group than terms available to or from independent third parties; (c) in accordance with the relevant agreement governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

## DIRECTORS AND DIRECTORS' SERVICE CONTRACTS

The Directors who held office during the year ended 31 December 2004 and up to the date of this report are:

### Executive directors

Mr. Li Weiruo

Mr. Yuan Bai

Mr. Tang Shiguo (retired on 29 April 2004)

Ms. Chi Chuan

Ms. Man Au Vivian

Mr. Li Shengdi (appointed on 29 April 2004)

### Independent non-executive directors

Mr. Hu Xiaoping

Mr. Woo Che-wor, Alex

Mr. Qian Laizhong (appointed on 16 August 2004)

In accordance with Article 87 of the articles of association of the Company, at each annual general meeting, one-third of directors for the time being shall retire from office by rotation and, will be eligible for re-election. Chairman of the Board will not be subject to retirement by rotation. As Ms. Chi Chuan and Ms. Man Au Vivian have been longest in office, Ms. Chi Chuan and Ms. Man Au Vivian will retire by rotation and, being eligible, will offer themselves for re-election at the forthcoming annual general meeting.

Each of the executive directors has entered into a service contract with the Company for initial fixed term of three years, and will continue thereafter for successive terms of one year until terminated by not less than three months' notice in writing served by either party on the other. Each of the executive directors is entitled to a basic salary and director's fee subject to an annual review by the Board. In addition, the executive directors are also entitled to a discretionary bonus, which may not exceed 3% of the audited consolidated net profit of the Group attributable to shareholders in respect of that financial year of the Company. The percentage rate of discretionary bonus is subject to annual review by the Board.

The independent non-executive directors of the Company are appointed with specific terms inside the letter of appointment for initial fixed terms of two years.

None of the directors who are proposed for re-election at the forthcoming annual general meeting has a service contract with the company which is not determinable within one year without payment of compensation, other than statutory compensation.



## SHARE OPTIONS

Share options are granted to directors, employees and consultants of the Company or its subsidiaries under the Share Option Scheme approved by written resolutions of shareholders of the Company on 10 June 2003 and amended at an extraordinary general meeting on 28 July 2004. The purpose of the Share Option Scheme is to recognize the contribution of employees and consultants to the Company and its subsidiaries, and to provide a performance related incentive to them. Currently under the Share Option Scheme the maximum number of shares which may fall to be issued pursuant to the exercise of all the share options granted and to be granted is 42,000,000 shares, representing 10% of the total number of issued shares upon listing on 10 July 2003. Unless approved by shareholders, the total number of shares issued and which may fall to be issued upon the exercise of the options granted to each participant may not exceed 4,200,000, such options being exercisable for 10 years from the date of grant of such option. Participants are required to pay an option price of HK\$10 for each acceptance of option offer. The subscription price shall be at least the highest of (i) the closing price of a share on the option offer date, (ii) the average closing price of a share for the five business days immediately preceding the option offer date and (iii) the nominal value of a share. The Share Option Scheme will remain valid for a period of ten years commencing from 10 June 2003.

On 10 August 2004, the Company granted share options to 247 employees to subscribe for an aggregate of 1,820,000 shares of the Company at subscription price of HK\$0.33. The details of option outstanding and movements are disclosed in the following table:

	Number of options				Exercise price HK\$	Grant date	Exercisable from	Exercisable until
	Held at 1 January 2004	Granted during the year	Exercised during the year	Held at 31 December 2004				
<b>Directors</b>								
Chi Chuan	4,200,000	—	—	4,200,000	0.62	23 September 2003	23 September 2004	22 September 2013
Man Au Vivian	3,800,000	—	—	3,800,000	0.62	23 September 2003	23 September 2004	22 September 2013
Li Shengdi	4,200,000	—	—	4,200,000	0.62	23 September 2003	23 September 2004	22 September 2013
Hu Xiaoping	400,000	—	—	400,000	0.62	23 September 2003	23 September 2004	22 September 2013
Woo Che-wor, Alex	400,000	—	—	400,000	0.62	23 September 2003	23 September 2004	22 September 2013
Employees	12,200,000	—	—	12,200,000	0.62	23 September 2003	23 September 2004	22 September 2013
Employees	—	1,820,000	1,820,000	—	0.33	10 August 2004	10 August 2004	9 August 2014
<b>Total</b>	<b>25,200,000</b>	<b>1,820,000</b>	<b>1,820,000</b>	<b>25,200,000</b>				

No option was cancelled or lapsed during the year ended 31 December 2004.

## VALUATION OF THE SHARE OPTIONS

The theoretical valuations of the share options calculated with the Black-Scholes option pricing model (the “Model”) as at the date of the grant of the options:

Grantee	Number of share options granted during the year	Theoretical value of share options HK\$
Employees	1,820,000	242,060

## VALUATION OF THE SHARE OPTIONS *(Continued)*

The Model is one commonly used model for theoretical option pricing. The assumptions in the calculation of the theoretical value of share options are as follows:

The expected volatility over the life of the share options is assumed equal to the historical volatility of the Company's shares for the year from 11 August 2003 to 10 August 2004, which is approximately 5.23%. Risk free rate is approximately 4.37%, which is the approximate yield of 10-year Hong Kong Exchange Fund Notes traded on 10 August 2004.

The theoretical value of share options calculating with the Model is subject to all assumptions and limitations of the Model.

## DIRECTORS' INTERESTS IN SHARES

As at 31 December 2004, the interests and short positions of the Directors and chief executives in the shares, underlying shares or debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")), which are required (a) to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they are taken or deemed to have under such provisions of the SFO); or (b) to be recorded in the register required to be kept under section 352 of the SFO; or (c) to be notified to the Company and the Stock Exchange pursuant to the minimum standards of dealings by directors referred to in Rule 5.46 of the GEM Listing Rules were as follows:

### (i) Long positions in the shares and the underlying shares of the Company

Name of Director	Type of shares	Capacity	Aggregate long position in shares and underlying shares	Approximate percentage of interests in the issued share capital
Li Weiruo	Personal	Beneficial owner	206,440,000	48.94
Yuan Bai	Personal	Beneficial owner	35,448,000	8.40
Chi Chuan	Personal	Beneficial owner	16,728,000 <i>(Note)</i>	3.97
Man Au Vivian	Personal	Beneficial owner	10,064,000 <i>(Note)</i>	2.39
Li Shengdi	Personal	Beneficial owner	4,200,000 <i>(Note)</i>	1.00
Hu Xiaoping	Personal	Beneficial owner	400,000 <i>(Note)</i>	0.10
Woo Che-wor, Alex	Personal	Beneficial owner	400,000 <i>(Note)</i>	0.10

*Note:* Long position in the underlying shares of the Company

## DIRECTORS' INTERESTS IN SHARES *(Continued)*

### (i) Long positions in the shares and the underlying shares of the Company *(Continued)*

Share options were granted to certain directors, employees and consultant of the Company or its Subsidiaries under the Share Option Scheme. Details of the options granted to Directors during the period are as follows:

Name of Director	Date of Grant	Number of share options				Outstanding as at 31 December 2004	Exercisable period	Exercise price HK\$
		Outstanding as at 1 January 2004	Granted during the year	Exercised during the year	Cancelled during the year			
Chi Chuan	23 September 2003	4,200,000	—	—	—	4,200,000	23 September 2004 - 22 September 2013	0.62
Man Au Vivian	23 September 2003	3,800,000	—	—	—	3,800,000	23 September 2004 - 22 September 2013	0.62
Li Shengdi	23 September 2003	4,200,000	—	—	—	4,200,000	23 September 2004 - 22 September 2013	0.62
Hu Xiaoping	23 September 2003	400,000	—	—	—	400,000	23 September 2004 - 22 September 2013	0.62
Woo Che-wor, Alex	23 September 2003	400,000	—	—	—	400,000	23 September 2004 - 22 September 2013	0.62

## REPORT OF THE DIRECTORS

### DIRECTORS' INTERESTS IN SHARES *(Continued)*

#### (ii) Interests in shares of an associated corporation of the Company

Name of Director	Name of company	Number and description of shares	Capacity	Type of interest	Approximate percentage of holding of such class
Li Weiruo	Ko Yo Development Co., Limited ("Ko Yo Hong Kong") <i>(Note)</i>	2,100,000 non-voting deferred shares	Beneficial owner	Personal	70
Yuan Bai	Ko Yo Hong Kong	420,000 non-voting deferred shares	Beneficial owner	Personal	14
Chi Chuan	Ko Yo Hong Kong	120,000 non-voting deferred shares	Beneficial owner	Personal	4
Man Au Vivian	Ko Yo Hong Kong	60,000 non-voting deferred shares	Beneficial owner	Personal	2

*Note:* a wholly-owned subsidiary of the Company

#### (iii) Short positions in the shares of an associated corporation of the Company

Name of Director	Capacity	Name of company	Number and description of shares	Aggregate percentage of holding of such class
Li Weiruo	Beneficial owner	Ko Yo Hong Kong	2,100,000 non-voting deferred shares	70
Yuan Bai	Beneficial owner	Ko Yo Hong Kong	420,000 non-voting deferred shares	14
Chi Chuan	Beneficial owner	Ko Yo Hong Kong	120,000 non-voting deferred shares	4
Man Au Vivian	Beneficial owner	Ko Yo Hong Kong	60,000 non-voting deferred shares	2

## SUBSTANTIAL SHAREHOLDERS

As at 31 December 2004, there was no substantial shareholder (not being a director or a chief executive of the Company) who had any interests or short positions in the shares or underlying shares of the Company which are required to be notified to the Company and the Stock Exchange under Divisions 2 and 3 of Part XV of the SFO and recorded in the register required to be kept under section 336 of the SFO, and who were directly or indirectly deemed to be interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of the Company.

## INTEREST OF OTHER PERSONS IN THE COMPANY

At 31 December 2004, the following person (not being a director or chief executive of the Company) had interests or short positions in the shares or underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO.

### (i) Long positions in the shares of the Company

Name	Type of shares	Capacity	Aggregate long position in shares	Approximate percentage of interests in the issued share capital
Tang Shiguo ( <i>Note</i> )	Personal	Beneficial owner	31,320,000	7.42

*Note:* Mr. Tang Shiguo ceased to be a director of the Company with effect from 29 April 2004.

### (ii) Long position in the underlying shares of the Company

No long positions of other persons in the underlying shares of equity derivatives of the Company were recorded in the register.

### (iii) Interests in shares of an associated corporation of the Company

Name	Name of company	Number and description of shares	Capacity	Type of interest	Approximate percentage of holding
Tang Shiguo ( <i>Note</i> )	Ko Yo Development	300,000 non-voting deferred shares	Beneficial owner	Personal	10

*Note:* Mr. Tang Shiguo ceased to be a director of the Company with effect from 29 April 2004.

## INTEREST OF OTHER PERSONS IN THE COMPANY *(Continued)*

### (iv) Short positions in the shares of an associated corporation of the Company

Name	Capacity	Name of company	Number and description of shares
Tang Shiguo <i>(Note)</i>	Beneficial owner	Ko Yo Hong Kong	300,000 non-voting deferred shares

*Note:* Mr. Tang Shiguo ceased to be a director of the Company with effect from 29 April 2004.

Save as disclosed above, as at 31 December 2004, there was no person or company (not being a Director of a chief executive of the Company) who had any interests or short positions in the shares or underlying shares of the Company which are required to be notified to the Company and the Stock Exchange under Divisions 2 and 3 of Part XV of the SFO and recorded in the register required to be kept under section 336 of the SFO, and who were directly or indirectly deemed to be interested in 5% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of the Company.

## DIRECTORS' INTEREST IN COMPETING BUSINESS

None of the Directors or the management shareholders of the Company and their respective associates (as defined under the GEM Listing Rules) had any interest in a business which competes or may compete, directly or indirectly with the business of the Company during the year under review.

## COMPLIANCE ADVISER'S INTEREST

Pursuant to an agreement dated 9 July 2003 between the Company and Guotai Junan Capital Limited ("Guotai Junan"), Guotai Junan has been appointed as the compliance adviser to the Company as required under the GEM Listing Rules at a fee for the remainder of the financial year of the Company ended 31 December 2003 and for a period of two years thereafter expiring on 31 December 2005.

As confirmed by Guotai Junan, as at 31 December 2004, save for 20,400,000 shares of the Company, representing 4.8% of the issued share capital of the Company, which were held by certain associates of Guotai Junan, neither Guotai Junan, their directors, employees nor any of their respective associates (as defined under the GEM Listing Rules) had any interest in the share capital of the Company or any of its subsidiaries.

### **DIRECTORS' INTERESTS IN CONTRACTS**

No contract of significance in relation to the Group's business to which the Company or its subsidiaries was a party and in which any of the Company's Directors or members of its management had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

### **MANAGEMENT CONTRACTS**

No contract concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

### **AUDIT COMMITTEE**

The Company established an audit committee on 10 June 2003 with written terms of reference pursuant to the GEM Listing Rules. The primary duties of the audit committee are to review and supervise the financial reporting process and internal control system of the Company and provide advice and comments to the Directors. The audit committee has three members comprising the three independent non-executive directors, namely, Mr. Hu Xiaoping, Mr. Woo Che-wor, Alex and Mr. Qian Laizhong.

The audit committee has reviewed with management the accounting principles and practices adopted by the Company and the Group and discussed internal controls and financial reporting matters including a review of the audited accounts of the Company and the Group for the year ended 31 December 2004.

### **PURCHASE, SALE OR REDEMPTION OF SHARES**

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed shares during the year under review.

## CUSTOMERS AND SUPPLIERS

For the year ended 31 December 2004, the five largest customers accounted for approximately 24.2% of the Group's total turnover and the five largest suppliers of the Group accounted for approximately 38.4% of the Group's total purchases. The largest customer of the Group accounted for approximately 6.3% of the Group's total turnover and the largest supplier accounted for approximately 15.3% of the Group's total purchases.

None of the Directors, their associates, or any shareholders (which, to the knowledge of the Directors, owned more than 5% of the Company's share capital) had a beneficial interest in the Group's five largest customers and suppliers.

## BOARD PRACTICES AND PROCEDURES

The Company had complied throughout the year under review the minimum standards of good practice concerning the general management responsibilities of the Board as set out in Rules 5.34 to 5.45 of the GEM Listing Rules.

The Board practices and procedures set out in Rules 5.35 to 5.45 of the GEM Listing Rules were replaced by the Code on Corporate Governance Practices as set out in Appendix 15 of the GEM Listing Rules, which has been effective for accounting period commencing on or after 1 January 2005. Appropriate actions have been taken by the Company for complying with the Code on Corporate Governance Practices.

## AUDITORS

The accounts have been audited by PricewaterhouseCoopers who shall retire and, being eligible, will offer themselves for re-appointment at the forthcoming annual general meeting.

On behalf of the Board,

**Li Weiruo**

*Chairman*

23 March 2005





羅兵咸永道會計師事務所

**PricewaterhouseCoopers**  
22nd Floor Prince's Building  
Central Hong Kong

**AUDITORS' REPORT TO THE SHAREHOLDERS OF  
KO YO ECOLOGICAL AGROTECH (GROUP) LIMITED**  
(incorporated in the Cayman Islands with limited liability)

We have audited the accounts on pages 32 to 68 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

**RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS**

The Company's directors are responsible for the preparation of accounts which give a true and fair view. In preparing accounts which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently.

It is our responsibility to form an independent opinion, based on our audit, on those accounts and to report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

**BASIS OF OPINION**

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Institute of Certified Public Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the accounts, and of whether the accounting policies are appropriate to the circumstances of the Company and of the Group, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the accounts are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts. We believe that our audit provides a reasonable basis for our opinion.

**OPINION**

In our opinion the accounts give a true and fair view of the state of affairs of the Company and of the Group as at 31st December 2004 and of the Group's profit and cash flows for the year then ended and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

**PricewaterhouseCoopers**  
*Certified Public Accountants*

Hong Kong, 23rd March 2004

# CONSOLIDATED PROFIT AND LOSS ACCOUNT

For the year ended 31st December 2004

	Note	2004 RMB'000	2003 RMB'000
Turnover	3	422,728	281,810
Cost of sales		(336,679)	(221,242)
Gross profit		86,049	60,568
Interest income	3	773	148
Distribution costs		(22,062)	(15,142)
Administrative expenses		(28,394)	(21,766)
Other income	4	5,004	6,173
Operating profit	5	41,370	29,981
Finance costs	6	(7,476)	(5,877)
Profit before taxation		33,894	24,104
Taxation	7	(1,215)	(31)
Profit after taxation		32,679	24,073
Minority interests		33	—
Profit attributable to shareholders		32,712	24,073
Dividends	9	6,478	5,921
Basic earnings per share	10	RMB0.078	RMB0.066
Diluted earnings per share	10	N/A	N/A

# CONSOLIDATED BALANCE SHEET

As at 31st December 2004

	Note	2004 RMB'000	2003 RMB'000
<b>Non-current assets</b>			
Negative goodwill	13	(12,366)	(12,866)
Fixed assets	14	206,835	159,170
Long-term investment	16	1,000	1,000
		<u>195,469</u>	<u>147,304</u>
<b>Current assets</b>			
Inventories	17	51,037	24,679
Trade and other receivables	18	46,802	46,689
Pledged bank deposits	19(c), 20	53,940	13,032
Cash and bank deposits		13,926	34,517
		<u>165,705</u>	<u>118,917</u>
<b>Current liabilities</b>			
Trade and other payables	19	69,229	38,224
Current portion of long-term bank loans, secured	21	—	21,000
Short-term bank loans, secured	20	95,430	46,430
		<u>164,659</u>	<u>105,654</u>
Net current assets		<u>1,046</u>	<u>13,263</u>
Total assets less current liabilities		<u>196,515</u>	<u>160,567</u>
<b>Financed by:</b>			
Share capital	24	44,713	44,520
Reserves			
Proposed final dividends	9, 25	5,142	3,250
Others	25	101,239	74,561
Shareholders' funds		<u>151,094</u>	<u>122,331</u>
Minority interests		<u>567</u>	<u>600</u>
<b>Non-current liabilities</b>			
Long-term bank loans, secured	21	37,200	29,800
Provision for staff compensation	22	7,388	7,449
Deferred tax liabilities	23	266	387
		<u>44,854</u>	<u>37,636</u>
		<u>196,515</u>	<u>160,567</u>

**Li Weiruo**  
Director

**Yuan Bai**  
Director

# BALANCE SHEET

As at 31st December 2004

	Note	2004 RMB'000	2003 RMB'000
Non-current assets			
Investments in subsidiaries	15	<u>86,136</u>	<u>96,657</u>
Current assets			
Trade and other receivables	18	23,408	9,954
Cash and bank deposits		<u>53</u>	<u>53</u>
		<u>23,461</u>	<u>10,007</u>
Current liabilities			
Accruals and other payables	19	<u>3,299</u>	<u>1,625</u>
Net current assets		<u>20,162</u>	<u>8,382</u>
Total assets less current liabilities		<u>106,298</u>	<u>105,039</u>
Financed by:			
Share capital	24	44,713	44,520
Reserves			
Proposed final dividends	25	5,142	3,250
Others	25	<u>56,443</u>	<u>57,269</u>
		<u>106,298</u>	<u>105,039</u>

**Li Weiruo**  
*Director*

**Yuan Bai**  
*Director*

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31st December 2004

	Note	<b>2004</b> <b>RMB'000</b>	2003 RMB'000
Total equity as at 1st January		122,331	64,567
Net gains not recognised in the profit and loss account			
– Exchange differences arising on translation of the accounts of foreign group companies		—	54
Profit for the year		32,712	24,073
Dividends	25	(4,586)	(2,671)
Issue of shares	24	—	45,283
Exercise of share options	24	637	—
Share issue expenses		—	(8,975)
		<hr/>	<hr/>
Total equity as at 31st December		<b>151,094</b>	122,331

# CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31st December 2004

	Note	2004 RMB'000	2003 RMB'000
Net cash generated from/(used in) operating activities	26(a)	<b>56,620</b>	(3,614)
Income Tax paid		<b>(1,701)</b>	—
Interest paid		<b>(7,476)</b>	(5,877)
		<u>47,443</u>	<u>(9,491)</u>
Net cash inflow/(outflow) from operating activities			
Investing activities			
Purchases of fixed assets and payments for construction-in-progress		<b>(55,361)</b>	(10,492)
Proceeds from disposal of fixed assets		<b>342</b>	807
Dividends received from long-term investment		<b>130</b>	130
Interest received		<b>340</b>	148
		<u>(54,549)</u>	<u>(9,407)</u>
Net cash outflow from investing activities			
Net cash outflow before financing activities		<b>(7,106)</b>	(18,898)
		<u>(7,106)</u>	<u>(18,898)</u>
Financing activities	26(c)		
Increase in pledged bank deposits		<b>(40,908)</b>	(3,532)
Issue of ordinary shares		—	45,283
Exercise of share options		<b>637</b>	—
Contribution from a minority shareholder		—	600
New loans payable		<b>112,830</b>	64,891
Repayment of amounts borrowed		<b>(77,430)</b>	(43,891)
Dividends paid	25	<b>(4,586)</b>	(2,671)
Repayment of the convertible note		—	(5,300)
Payments for listing expenses	26(a)	<b>(4,028)</b>	(8,975)
		<u>(13,485)</u>	<u>46,405</u>
Net cash (outflow)/inflow from financing activities			
(Decrease)/increase in cash and cash equivalents		<b>(20,591)</b>	27,507
Cash and cash equivalents at 1st January		<b>34,517</b>	7,010
Cash and cash equivalents at 31st December		<b>13,926</b>	34,517
Analysis of balances of cash and cash equivalents			
Cash and bank deposits		<b>13,926</b>	34,517

## 1 GROUP REORGANISATION AND BASIS OF PRESENTATION

Ko Yo Ecological Agrotech (Group) Limited (the “Company”) was incorporated in the Cayman Islands on 11th February 2002 as an exempted company with limited liability under the Companies Law Cap. 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands. Its shares have been listed on the Growth Enterprise Market (the “GEM”) of The Stock Exchange of Hong Kong Limited (the “Stock Exchange”) since 10th July 2003.

On 10th June 2003, the Company became the holding company of the other companies now comprising the Group pursuant to a group reorganisation (the “Reorganisation”) which included exchange of shares of companies under common control, and the Company and its subsidiaries (the “Group”) resulting from the Reorganisation are regarded as a continuing group. Accordingly, the Reorganisation has been accounted for on the basis of merger accounting, under which the consolidated accounts have been prepared as if the Company had been the holding company of the other companies comprising the Group throughout the year ended 31st December 2003, or since the date of incorporation of the individual companies, where this is a shorter period.

## 2 PRINCIPAL ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these accounts are set out below:

### (a) Basis of preparation

The accounts have been prepared in accordance with accounting principles generally accepted in Hong Kong and comply with accounting standards issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”). They have been prepared under the historical cost convention.

The HKICPA has issued a number of new and revised Hong Kong Financial Reporting Standards and Hong Kong Accounting Standards (“new HKFRSs”) which are effective for accounting periods beginning on or after 1st January 2005. The Group has not early adopted these new HKFRSs in the financial statements for the year ended 31st December 2004. The Group has already commenced an assessment of the impact of these new HKFRSs but is not yet in a position to state whether these new HKFRSs would have a significant impact on its results of operations and financial position.

### 2 PRINCIPAL ACCOUNTING POLICIES *(Continued)*

#### (b) Group accounting

##### (i) Consolidation

The consolidated accounts include the accounts of the Company and its subsidiaries made up to 31st December.

Subsidiaries are those entities in which the Company, directly or indirectly, controls more than one half of the voting power; has the power to govern the financial and operating policies; to appoint or remove the majority of the members of the board of directors; or to cast majority of votes at the meetings of the board of directors.

All significant inter-company transactions and balances within the Group are eliminated on consolidation.

Minority interests represent the interests of outside shareholders in the operating results and net assets of subsidiaries.

The gain or loss on the disposal of a subsidiary represents the difference between the proceeds of the sale and the Group's share of its net assets together with any unamortised goodwill or negative goodwill or goodwill/negative goodwill taken to reserves and which was not previously charged or recognised in the consolidated profit and loss account and any related accumulated foreign currency translation reserve.

In the Company's balance sheet, the investments in subsidiaries are stated at cost less provision for impairment losses. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable.

##### (ii) Translation of foreign currencies

Transactions in foreign currencies are translated at exchange rates ruling at the transaction dates. Monetary assets and liabilities expressed in foreign currencies at the balance sheet date are translated at rates of exchange ruling at the balance sheet date. Exchange differences arising in these cases are dealt with in the profit and loss account.

The balance sheets of subsidiaries, expressed in foreign currencies, are translated at the rates of exchange ruling at the balance sheet date whilst the profit and loss accounts are translated at an average rate. Exchange differences are dealt with as a movement in reserves.



**2 PRINCIPAL ACCOUNTING POLICIES** *(Continued)*

**(c) Negative goodwill**

Negative goodwill represents the excess of the fair value of the Group's share of the net assets acquired over the cost of acquisition.

The amount of negative goodwill not exceeding the fair values of the non-monetary assets acquired, is recognised as income on a straight-line basis in the profit and loss account over the remaining weighted average useful life of these assets of 30 years.

**(d) Fixed assets**

*(i) Construction-in-progress*

Construction-in-progress represents plant and properties under construction and is stated at cost, which includes development and construction expenditure incurred and other direct costs attributable to the construction, less accumulated impairment losses. Construction-in-progress is not depreciated until such time as the assets are completed and put into operational use.

*(ii) Other fixed assets*

Other fixed assets, comprising land use rights, buildings, plant and machinery, motor vehicles, office equipment and others, are stated at cost less accumulated depreciation and accumulated impairment losses.

*(iii) Depreciation*

Land use rights are depreciated over the period of the rights while other fixed assets are depreciated at rates sufficient to write off their cost less accumulated impairment losses over their estimated useful lives on a straight-line basis. The principal annual rates are as follows:

Buildings	2.6 %
Plant and machinery	6.4-7.5 %
Motor vehicles	9.0 %
Office equipment and others	12.9 %

Major costs incurred in restoring fixed assets to their normal working condition are charged to the profit and loss account. Improvements are capitalised and depreciated over their expected useful lives to the Group.

### 2 PRINCIPAL ACCOUNTING POLICIES *(Continued)*

#### (d) Fixed assets *(Continued)*

##### (iv) Impairment and gain or loss on sale

At each balance sheet date, both internal and external sources of information are considered to assess whether there is any indication that fixed assets are impaired. If any such indication exists, the recoverable amount of the asset is estimated and where relevant, an impairment loss is recognised to reduce the asset to its recoverable amount. Such impairment losses are recognised in the profit and loss account.

The gain or loss on disposal of a fixed asset is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the profit and loss account.

#### (e) Operating leases

Leases where substantially all the risks and rewards of ownership of assets remain with the leasing company are accounted for as operating leases. Payments made under operating leases net of any incentives received from the leasing company are charged to the profit and loss account on a straight-line basis over the lease periods.

#### (f) Long-term investments

Long-term investments are stated at cost less any provision for impairment losses. The carrying amounts of individual investments are reviewed at each balance sheet date to assess whether the fair values have declined below the carrying amounts. When a decline other than temporary has occurred, the carrying amounts of such investments will be reduced to their fair values. The impairment loss is recognised as an expense in the profit and loss account. This impairment loss is written back to the profit and loss account when the circumstances and events that led to the write-downs or write-offs cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future.

#### (g) Inventories

Inventories comprise stocks and work in progress and are stated at the lower of cost and net realisable value. Cost, calculated on the weighted average basis, comprises materials, direct labour and an appropriate proportion of all production overhead expenditure. Net realisable value is determined on the basis of anticipated sales proceeds less estimated selling expenses.

#### (h) Accounts receivable

Provision is made against accounts receivable to the extent they are considered to be doubtful. Accounts receivable in the balance sheet are stated net of such provision.

## 2 PRINCIPAL ACCOUNTING POLICIES (Continued)

### (i) Cash and cash equivalents

Cash and cash equivalents are carried in the balance sheet at cost. For the purposes of the cash flow statement, cash and cash equivalents comprise cash on hand, deposits held at call with banks, cash investments with a maturity of three months or less from date of investment and bank overdrafts.

### (j) Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where the Group expects a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

### (k) Employee benefits

#### (i) Employee leave entitlements

Employee entitlements to annual leave and long service leave are recognised when they accrue to employees. A provision is made for the estimated liability for annual leave and long-service leave as a result of services rendered by employees up to the balance sheet date.

#### (ii) Pension obligations

Pursuant to laws and regulations in the People's Republic of China ("Mainland China"), contributions to the basic old age insurance for the Group's Mainland China employees are made monthly to a government agency based on 25% of the standard salary set by the provincial government, of which 20% is borne by the Group and the remainder is borne by the employees. Except for the monthly contribution of 20% on standard salary to the government agency, the Group has no further obligation in connection with Mainland China employees' retirement benefits. The government agency is responsible for the pension liabilities relating to such employees on their retirement. The Group accounts for these contributions on an accrual basis.

The subsidiary in Hong Kong operates a defined contribution scheme which is available to qualified employees. The assets of the scheme are held separately from those of the subsidiary in independently administered funds. Monthly contributions made by the subsidiary are calculated based on certain percentages of the applicable payrolls costs or HKD1,000, whichever is lower.

Contributions to the above retirement schemes are charged to the profit and loss account as incurred.

### 2 PRINCIPAL ACCOUNTING POLICIES *(Continued)*

#### (l) **Deferred taxation**

Deferred taxation is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the accounts. Taxation rates enacted or substantively enacted by the balance sheet date are used to determine deferred taxation.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred taxation is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

#### (m) **Contingent liabilities**

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised but is disclosed in the notes to the accounts. When a change in the probability of an outflow occurs so that the outflow becomes probable, it will then be recognised as a provision.

#### (n) **Revenue recognition**

Revenue from the sale of goods is recognised on the transfer of risks and rewards of ownership, which generally coincides with the time when the goods are delivered to customers and title has passed.

Interest income is recognised on a time proportion basis, taking into account the principal amounts outstanding and the interest rates applicable.

Dividend income is recognised when the right to receive payment is established.

#### (o) **Borrowing costs**

Borrowing costs that are directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of that asset.

All other borrowing costs are charged to the profit and loss account in the year in which they are incurred.

**2 PRINCIPAL ACCOUNTING POLICIES** *(Continued)*

**(p) Financial subsidies and tax refund**

Financial subsidies and tax refund are recognized in the profit and loss account when there is reasonable assurance that the Group will comply with the condition attaching with them and that the subsidies and refund will be received.

**(q) Segment reporting**

The Group regards chemical products and chemical fertilisers as a single business segment. The Group also operates mainly within one geographical segment as its revenues are primarily generated in Mainland China and its assets are located in Mainland China. Accordingly, no segmental information is presented.

**3 TURNOVER AND REVENUE**

The Company is an investment holding company. The Group is principally engaged in the manufacture and sale of chemical products and chemical fertilisers in Mainland China. Turnover represents invoiced value of sale of chemical products and chemical fertilisers to customers in Mainland China, net of goods returned and value-added tax (“VAT”), where applicable.

The Group’s sales made in Mainland China are subject to VAT on sales (“output VAT”). Such output VAT is payable after offsetting VAT paid by the Group on purchases. The applicable rates of output VAT range from 0% to 17%.

Revenues recognised during the year are as follows:

	<b>2004</b>	2003
	<b>RMB'000</b>	RMB'000
Turnover		
– Sale of chemical products and chemical fertilisers	<b>422,728</b>	281,810
Interest income	<b>773</b>	148
	<hr/>	<hr/>
Total revenues	<b>423,501</b>	281,958
	<hr/> <hr/>	<hr/> <hr/>

## 4 OTHER INCOME

	2004 RMB'000	2003 RMB'000
Financial subsidies ( <i>Note a</i> )	600	2,438
VAT refund ( <i>Note b</i> )	2,232	—
Cash discounts on settlement of certain payables ( <i>Note c</i> )	—	2,771
Amortisation of negative goodwill ( <i>Note 13</i> )	500	500
Dividend income from unlisted investment	130	130
Sales of waste materials	1,129	—
Others	413	334
	<u>5,004</u>	<u>6,173</u>

### (a) Financial subsidies

Pursuant to document Xin Du Wei Fa (1998) No. 38 issued by the local government authority, Chengdu Ko Yo Chemical Industry Co., Ltd. (“Chengdu Ko Yo Chemical”), a subsidiary of the Company, is entitled to receive a financial subsidy equal to 68% of its payment of the tax liabilities assumed from its predecessor, Xin Du County Nitrogenous Fertilisers Company (“Xin Du Fertilisers Company”, a state-owned enterprise) upon its establishment in July 1999.

Pursuant to document (1999) No.33 issued by the local government authority, Chengdu Ko Yo Chemical is entitled to receive a financial subsidy equal to certain percentage of its net VAT paid to the local tax bureau. The applicable rates for the two years ended 30th June 2001 and the four years ending 30th June 2005 are 80% and 50%, respectively. Such policy will be terminated on 1st July 2005.

### (b) VAT refund

Pursuant to document Cai Shui (2004) No.33 issued by the Ministry of Finance and the National Tax Bureau of Mainland China in 2004, companies established in Mainland China are entitled to a refund of VAT paid on sale of certain qualified agricultural chemical fertilisers. Chengdu Ko Yo Chemical is entitled to receive a refund for its net VAT paid on its sales of urea for the year ended 31st December 2004 and the tax refund rate was 50%.

**4 OTHER INCOME** *(Continued)*

**(c) Cash discounts on settlement of certain payables**

Upon its establishment, Chengdu Ko Yo Chemical assumed from Xin Du Fertilisers Company certain payables, which had no fixed repayment terms according to the agreements between the relevant creditors and Chengdu Ko Yo Chemical. Part of such payables were subsequently granted with maturity periods of over one year and were interest-free.

As a result of further negotiations with these creditors during the year ended 31st December 2003, some of the above payables were settled with cash discounts which were recognised as other income.

**5 OPERATING PROFIT**

Operating profit is stated after crediting and charging the following:

	<b>2004</b>	2003
	<b>RMB'000</b>	RMB'000
Crediting:		
Gain on disposal of fixed assets	<u>222</u>	<u>—</u>
Charging:		
Staff costs (including directors' emoluments) <i>(Note 11)</i>		
– Salaries, wages and other benefits	<u>26,969</u>	18,770
– Contributions to retirement schemes	<u>1,711</u>	1,617
	<u>28,680</u>	<u>20,387</u>
Cost of inventories	<b>336,679</b>	221,242
Provision for doubtful receivables	<b>994</b>	525
Provision for impairment loss on fixed assets	<b>—</b>	126
Loss on disposal of fixed assets	<b>80</b>	98
Operating leases for buildings	<b>1,070</b>	861
Depreciation	<b>9,770</b>	9,169
Auditors' remuneration	<u>1,071</u>	<u>830</u>

## 6 FINANCE COSTS

	<b>2004</b>	2003
	<b>RMB'000</b>	RMB'000
Interest on loans wholly repayable within five years		
– Bank loans	<b>7,088</b>	5,308
– Other loans	<b>388</b>	569
	<u><b>7,476</b></u>	<u>5,877</u>

## 7 TAXATION

No provision for profits tax in the Cayman Islands, British Virgin Islands or Hong Kong has been made, as the Group had no assessable profit arising in or derived from those jurisdictions during the years ended 31st December 2004 and 2003.

Chengdu Ko Yo Chemical, Chengdu Ko Yo Compound Fertiliser Co., Ltd. (“Chengdu Ko Yo Compound”), Dezhou Ko Yo Compound Fertiliser Co., Ltd. (“Dezhou Ko Yo Compound”) and Dazhou City Dazhu Ko Yo Chemical Industry Co., Ltd. (“Dazhu Ko Yo Chemical”) were established as foreign investment enterprises in Mainland China. They are subject to Enterprise Income Tax (“EIT”) at rates of 15%, 15%, 33% and 15%, respectively, and are entitled to full exemption from EIT in the first two profitable years and a 50% reduction for the next three years thereafter.

The preferential EIT rate applicable to Chengdu Ko Yo Chemical in 2004 is 7.5% (2003: 7.5%). Pursuant to relevant taxation regulations of Mainland China and as approved by the local taxation bureau, Chengdu Ko Yo Chemical was entitled to deduct from its EIT expenses for an amount of 40% of cost of certain machinery acquired from Mainland China enterprises, which are local machinery suppliers and unrelated to the Group. Accordingly, EIT provision made for Chengdu Ko Yo Chemical for the year ended 31st December 2004 was RMB1,101,000 (2003: Nil).

The preferential EIT rate applicable to Chengdu KoYo Compound for the year ended 31st December 2004 is 7.5% (2003: Nil).

Dezhou Ko Yo Compound did not have taxable profit for the year ended 31st December 2004 (2003: Nil).

Dazhu Ko Yo Chemical did not have taxable profit for the period from 8th December 2004 (date of incorporation) to 31st December 2004.



**7 TAXATION** *(Continued)*

The amount of taxation charged to consolidated profit and loss account represents:

	<b>2004</b>	2003
	<b>RMB'000</b>	RMB'000
Current tax for Mainland China	<b>1,336</b>	—
Deferred tax <i>(Note 23)</i>	<b>(121)</b>	31
	<u><b>1,215</b></u>	<u>31</u>

The taxation on the Group's profit before taxation differs from the theoretical amount that would arise using the taxation rate of the home country of the Company as follows:

	<b>2004</b>	2003
	<b>RMB'000</b>	RMB'000
Profit before taxation	<b>33,894</b>	24,104
Calculated at a taxation rate of 15% (2003: 15%)	<b>5,084</b>	3,616
Expenses not deductible for tax purposes	<b>1,239</b>	334
Effect of preferential tax treatment-deduction of 40% of cost of machinery acquired from Mainland China enterprises	<b>(1,886)</b>	(1,665)
Effects on tax holiday available to different companies of the Group	<b>(3,222)</b>	(2,254)
Taxation	<u><b>1,215</b></u>	<u>31</u>

**8 PROFIT ATTRIBUTABLE TO SHAREHOLDERS**

The profit attributable to shareholders is dealt with in the accounts of the Company of approximately RMB5,208,000 (2003: RMB7,268,000).

## 9 DIVIDENDS

	<b>2004</b>	2003
	<b>RMB'000</b>	RMB'000
Interim, paid, of HKD0.003 (2003: HKD0.006) per ordinary share	<b>1,336</b>	2,671
Final, proposed, of HKD0.0115 (2003: HKD0.0073) per ordinary share	<b>5,142</b>	3,250
	<u><b>6,478</b></u>	<u>5,921</u>

At a meeting held on 29th July 2004, the directors declared an interim dividend of HKD0.003 (equivalent to RMB0.0032) per ordinary share, totalling approximately RMB1,336,000, which was paid during the year ended 31st December 2004.

At a meeting held on 23rd March 2005, the directors proposed a final dividend of HKD0.0115 (equivalent to RMB0.0122) per ordinary share, totalling approximately RMB5,142,000. This proposed dividend is not reflected as a dividend payable in these accounts, but will be reflected as an appropriation of retained earnings for the year ending 31st December 2005.

## 10 EARNINGS PER SHARE

The calculation of basic earnings per share for the year ended 31st December 2004 is based on the consolidated profit attributable to shareholders of approximately RMB32,712,000 (2003: RMB24,073,000) and the weighted average number of approximately 420,648,000 (2003: 364,113,000) ordinary shares in issue during the year. In determining the number of shares in issue, 313,200,000 shares issued on the incorporation of the Company and on the Reorganisation of the Group were deemed to have been in issue since 1st January 2003.

Diluted earnings per share is not presented as there were no dilutive potential ordinary shares.

## 11 STAFF COSTS

	<b>2004</b>	2003
	<b>RMB'000</b>	RMB'000
Wages and salaries	<b>25,658</b>	17,482
Pension costs – defined contribution plans	<b>1,711</b>	1,617
Social security costs	<b>1,311</b>	1,288
	<u><b>28,680</b></u>	<u>20,387</u>

12 DIRECTORS' AND SENIOR MANAGEMENT'S EMOLUMENTS

(a) Directors' emoluments

The aggregate amounts of emoluments paid/payable to directors of the Company during the year are as follows:

	2004 RMB'000	2003 RMB'000
Fees	1,233	585
Other emoluments		
– Basic salaries, housing allowances, other allowances and benefits in kind	915	915
– Bonuses	848	530
– Contributions to pension schemes	40	31
	<u>3,036</u>	<u>2,061</u>

The directors' fees disclosed above include approximately RMB152,000 (2003: RMB71,000) paid to the independent non-executive directors.

The emoluments of the directors fell within the following band:

	Number of directors	
	2004	2003
Nil to RMB1,060,000 (equivalent to HKD1,000,000)	<u>9</u>	<u>7</u>

The executive directors received individual emoluments for the year ended 31st December 2004 of approximately RMB1,049,000 (2003: RMB600,000), RMB553,000 (2003: RMB436,000), RMB427,000 (2003: RMB318,000), RMB427,000 (2003: RMB318,000), RMB340,000 (2003: Nil) and RMB88,000 (2003: RMB318,000), respectively.

The independent non-executive directors received individual emoluments for the year ended 31st December 2004 of approximately RMB64,000 (2003: RMB36,000), RMB64,000 (2003: RMB35,000) and RMB24,000 (2003: Nil).

No directors waived any emoluments during the year.

## 12 DIRECTORS' AND SENIOR MANAGEMENT'S EMOLUMENTS *(Continued)*

### (b) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for both years include four directors (2003: four) whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining individual (2003: also only one individual) during the year are as follows:

	<b>2004</b>	2003
	<b>RMB'000</b>	RMB'000
Basic salaries, housing allowances, other allowances and benefits in kind	<b>413</b>	413
Bonuses	<b>21</b>	—
Contributions to pension schemes	<b>13</b>	11
	<u><b>447</b></u>	<u>424</u>

The emoluments fell within the following band:

	<b>Number of individuals</b>	
	<b>2004</b>	2003
Nil to RMB1,060,000 (equivalent to HKD1,000,000)	<u><b>1</b></u>	<u>1</u>

During the year, the Group did not pay any amount to the five highest paid individuals (including directors and the employee) nor any other directors of the Company as an inducement to join or upon joining the Group or as compensation for loss of office.

13 NEGATIVE GOODWILL

	Group	
	2004 RMB'000	2003 RMB'000
Cost		
At 1st January and 31st December	<u>14,634</u>	<u>14,634</u>
Accumulated amortisation		
At 1st January	1,768	1,268
Charge for the year	<u>500</u>	<u>500</u>
At 31st December	<u>2,268</u>	<u>1,768</u>
Net book amount		
At 31st December	<u>12,366</u>	<u>12,866</u>
At 1st January	<u>12,866</u>	<u>13,366</u>

Upon the establishment of Chengdu Ko Yo Chemical, the fair value of the assets and liabilities taken over from Xin Du Fertilisers Company, its predecessor, was reviewed by the directors using replacement cost approach, open market value approach and present value approach, whichever is applicable. The negative goodwill represented the excess of the Group's interest of the fair value of the identifiable assets and liabilities acquired over the cost of the acquisition.

Negative goodwill is amortised over the remaining weighted average useful lives of the identifiable acquired depreciable/amortisable assets of 30 years on a straight-line basis.

## NOTES TO THE ACCOUNTS

### 14 FIXED ASSETS

	Group						Total RMB'000
	Land use rights RMB'000	Buildings RMB'000	Plant and machinery RMB'000	Motor vehicles RMB'000	Office equipment and others RMB'000	Construction- in-progress RMB'000	
Cost:							
At 1st January 2004	41,423	49,648	82,509	4,135	6,441	2,843	186,999
Additions	6,115	8,484	7,815	474	605	34,142	57,635
Transfers	—	473	9,165	—	430	(10,068)	—
Disposals	—	—	(333)	—	(26)	—	(359)
At 31st December 2004	<u>47,538</u>	<u>58,605</u>	<u>99,156</u>	<u>4,609</u>	<u>7,450</u>	<u>26,917</u>	<u>244,275</u>
Accumulated depreciation:							
At 1st January 2004	3,755	5,546	15,158	422	2,948	—	27,829
Charge for the year	826	1,242	6,554	321	827	—	9,770
Disposals	—	—	(155)	—	(4)	—	(159)
At 31st December 2004	<u>4,581</u>	<u>6,788</u>	<u>21,557</u>	<u>743</u>	<u>3,771</u>	<u>—</u>	<u>37,440</u>
Net book value:							
At 31st December 2004	<u>42,957</u>	<u>51,817</u>	<u>77,599</u>	<u>3,866</u>	<u>3,679</u>	<u>26,917</u>	<u>206,835</u>
At 31st December 2003	<u>37,668</u>	<u>44,102</u>	<u>67,351</u>	<u>3,713</u>	<u>3,493</u>	<u>2,843</u>	<u>159,170</u>

All the Group's land use rights and buildings were located in Mainland China. As at 31st December 2004, certain land use rights and buildings with a total net book value of approximately RMB69,116,000 (2003: RMB70,962,000) and plant and machinery with a total net book value of approximately RMB23,675,000 (2003: RMB29,248,000) were pledged as collateral for the Group's short-term bank loans and long-term bank loans (Notes 20 and 21).

15 INVESTMENTS IN SUBSIDIARIES

	Company	
	2004 RMB'000	2003 RMB'000
Unlisted investments at cost	70,361	70,361
Amounts due from subsidiaries	21,536	30,130
Amounts due to subsidiaries	(5,761)	(3,834)
	<b>86,136</b>	<b>96,657</b>
	<b>86,136</b>	<b>96,657</b>

The amounts due from/to subsidiaries are unsecured, non-interest bearing and have no fixed repayment term.

The following is a list of the subsidiaries as at 31st December 2004:

Name	Place of incorporation/ establishment and kind of legal entity	Principal activities and place of operation	Particulars of issued, registered and fully paid up capital	Interest held
Ko Yo Ecological Agrotech (BVI) Limited ("Ko Yo BVI") *	British Virgin Islands ("BVI"), limited liability company	Investment holding in BVI	100 ordinary shares of USD1 each	100%
Ko Yo Development Company Limited ("Ko Yo Hong Kong")	Hong Kong, limited liability company	Investment holding in Hong Kong	3,000,000 non-voting deferred shares and 100 ordinary shares of HKD1 each	100%
Chengdu Ko Yo Chemical	Mainland China, wholly foreign owned enterprise	Manufacture and sale of chemical products including sodium carbonate, ammonia, and chemical fertilisers including urea and ammonium chloride in Mainland China	RMB13,000,000	100%
Chengdu Ko Yo Compound	Mainland China, wholly foreign owned enterprise	Manufacture, research, development and sale of bulk blended fertilisers in Mainland China	RMB15,000,000	100%

## NOTES TO THE ACCOUNTS

### 15 INVESTMENTS IN SUBSIDIARIES (Continued)

Name	Place of incorporation/ establishment and kind of legal entity	Principal activities and place of operation	Particulars of issued, registered and fully paid up capital	Interest held
Dezhou Ko Yo Compound	Mainland China, sino-foreign equity joint venture	Manufacture, research, development and sale of bulk blended fertilisers in Mainland China	RMB3,000,000	80%
Dazhu Ko Yo Chemical**	Mainland China, wholly foreign owned enterprise	Manufacture and sale of chemical products including ammonia, ammonium bicarbonate and urea in Mainland China.	Nil	100%

\* Shares held directly by the Company

\*\* The issued, registered capital of RMB8,000,000 was fully paid up on 10th March 2005

### 16 LONG-TERM INVESTMENT

	Group	
	2004 RMB'000	2003 RMB'000
Unlisted investment, at cost	<u>1,000</u>	<u>1,000</u>

Long-term investment represented the Group's 1.2% equity interest in Sichuan Jiuda Industrial Salt Co. Ltd. ("Sichuan Jiuda"). The largest investor of Sichuan Jiuda, which has approximately 86% interest in Sichuan Jiuda, is one of the Group's large suppliers selling industrial salt to the Group.



17 INVENTORIES

	Group	
	2004 RMB'000	2003 RMB'000
Finished goods	2,718	10,503
Raw materials	44,524	11,775
Work in progress	3,795	2,401
	<u>51,037</u>	<u>24,679</u>

At 31st December 2004, there were no inventories stated at net realisable value (2003: Nil).

18 TRADE AND OTHER RECEIVABLES

	Group		Company	
	2004 RMB'000	2003 RMB'000	2004 RMB'000	2003 RMB'000
Trade receivables ( <i>Note a</i> )	10,642	15,899	—	—
Prepayments, purchase deposits and other deposits	25,983	19,711	194	96
Notes receivable ( <i>Note b</i> )	505	3,052	—	—
Other receivables ( <i>Note c</i> )	9,672	8,027	—	—
Due from a subsidiary	—	—	23,214	9,858
	<u>46,802</u>	<u>46,689</u>	<u>23,408</u>	<u>9,954</u>

## NOTES TO THE ACCOUNTS

### 18 TRADE AND OTHER RECEIVABLES (Continued)

#### (a) Trade receivables

In general, the credit terms granted by the Group ranged from 0 to 3 months. The ageing analysis of trade receivables is as follows:

	Group	
	2004	2003
	RMB'000	RMB'000
Aged:		
Less than 3 months	8,844	6,481
More than 3 months but not exceeding 1 year	1,209	9,626
More than 1 year but not exceeding 2 years	2,127	658
More than 2 years but not exceeding 3 years	322	—
More than 3 years	366	366
	<u>12,868</u>	<u>17,131</u>
Less: provision for doubtful receivables	(2,226)	(1,232)
	<u>10,642</u>	<u>15,899</u>

#### (b) Notes receivable

The balance represents bank acceptance notes with periods within six months.

18 TRADE AND OTHER RECEIVABLES (Continued)

(c) Other receivables

Included in other receivables are amounts due from officers as follows:

Name	Maximum outstanding during the year RMB'000	Amount outstanding at 31st December 2004 RMB'000	Amount outstanding at 31st December 2003 RMB'000
Li Weiruo (director)	418	—	389
Tang Shiguo*	6	—	6
Chi Chuan (director)	100	—	—
Yuan Bai (director)	7	—	7
Man Au Vivian (director)	3	—	3
Li Shengdi (director)**	106	—	—
	<u>640</u>	<u>—</u>	<u>405</u>

\* Mr. Tang Shiguo ceased to be a director of the Company with effect from 29th April 2004.

\*\* Mr Li Shengdi was elected to be a director of the Company with effect from 29th April 2004.

The above balances represent advances to officers and are unsecured, repayable on demand, and bear an interest rate of 7% per annum.

19 TRADE AND OTHER PAYABLES

	Group		Company	
	2004 RMB'000	2003 RMB'000	2004 RMB'000	2003 RMB'000
Due to related companies (Note a)	124	2,492	—	—
Trade payables (Note b)	18,796	11,360	—	—
Notes payable (Note c)	8,770	8,636	—	—
Deposits from customers	17,225	5,216	—	—
Accruals and other payables	24,314	10,520	3,299	1,625
	<u>69,229</u>	<u>38,224</u>	<u>3,299</u>	<u>1,625</u>

## NOTES TO THE ACCOUNTS

### 19 TRADE AND OTHER PAYABLES (Continued)

#### (a) Due to related companies

Balances with related companies, which are controlled by relatives of Mr. Li Weiruo, a shareholder and director, arose from advances from related companies and are unsecured and interest-free. The directors of the Company are of the opinion that the above balances arose in the ordinary course of the Group's business.

#### (b) Trade payables

The ageing analysis of trade payables of the Group is as follows:

	Group	
	2004	2003
	RMB'000	RMB'000
Aged:		
Less than 1 year	18,559	10,849
More than 1 year but not exceeding 2 years	178	65
More than 2 years but not exceeding 3 years	59	—
More than 3 years	—	446
	<u>18,796</u>	<u>11,360</u>

#### (c) Notes payable

Notes payable represented bank acceptance notes issued by the Group and were interest-free and with maturity periods of less than one year. As at 31st December 2004, notes payable of approximately RMB8,770,000 (2003: RMB8,636,000) were pledged by bank deposits of RMB3,940,000 (2003: RMB6,636,000).

### 20 SHORT-TERM BANK LOANS, SECURED

The bank loans bear interest with rates ranging from 4.87% to 6.70% (2003: 5.31% to 6.63%) per annum and are secured by a bank deposit of RMB50,000,000 (2003: 6,396,000) and certain fixed assets of the Group (Note 14).

**21 LONG-TERM BANK LOANS, SECURED**

	Group	
	2004 RMB'000	2003 RMB'000
Amounts due:		
Less than 1 year	—	21,000
More than 1 year but not exceeding 2 years	28,400	4,000
More than 2 years but not exceeding 5 years	8,800	25,800
More than 5 years	—	—
	<u>37,200</u>	<u>50,800</u>
Amounts due within 1 year included in current liabilities	—	(21,000)
	<u>37,200</u>	<u>29,800</u>

The bank loans bear interest with rates ranging from 6.14% to 6.98% (2003: 6.21% to 6.372%) per annum and are secured by certain fixed assets of the Group (Note 14).

**22 PROVISION FOR STAFF COMPENSATION**

	Group	
	2004 RMB'000	2003 RMB'000
At 1st January	7,449	7,632
Payments	(61)	(183)
At 31st December	<u>7,388</u>	<u>7,449</u>

Upon the establishment of Chengdu Ko Yo Chemical, certain government loans made to Xin Du Fertilisers Company and certain payables related to staff benefits were conditionally assigned to the former employees of Xin Du Fertilisers Company as provision for staff compensation. Under the arrangement, Chengdu Ko Yo Chemical is required to pay an amount of compensation predetermined at the date of its establishment to these employees if they are laid off by Chengdu Ko Yo Chemical or if they resign before their retirement.

## NOTES TO THE ACCOUNTS

### 22 PROVISION FOR STAFF COMPENSATION *(Continued)*

Upon retirement, these employees will be covered by the defined contribution retirement schemes organised by the relevant local government authorities in Mainland China (Note 2(k)), and will not be entitled to the repayment of the provision for staff compensation assigned to them. The unpaid balances of the provision for staff compensation are included in non-current liabilities in the balance sheet and were recognised as income upon the retirement of the employees as Chengdu Ko Yo Chemical no longer had any obligations to make repayment to them.

### 23 DEFERRED TAX LIABILITIES

Deferred taxation is calculated in full on temporary differences under the liability method using the taxation rates applicable to the respective companies.

The movement on the deferred tax liabilities/(assets) account is as follows:

	Group	
	2004 RMB'000	2003 RMB'000
At 1st January	387	356
Deferred taxation (credited)/charged to profit and loss account	(121)	31
At 31st December	<u>266</u>	<u>387</u>

The movement in deferred tax assets and liabilities (prior to offsetting of balances within the same taxation jurisdiction) during the year is as follows:

	Deferred tax liabilities		Deferred tax assets		Total	
	2004 RMB'000	2003 RMB'000	2004 RMB'000	2003 RMB'000	2004 RMB'000	2003 RMB'000
	Difference in tax depreciation		Impairment of assets			
At 1st January	624	624	(237)	(268)	387	356
(Credited)/charged to profit and loss account	—	—	(121)	31	(121)	31
At 31st December	<u>624</u>	<u>624</u>	<u>(358)</u>	<u>(237)</u>	<u>266</u>	<u>387</u>

Deferred assets and liabilities are offset and shown in the consolidated balance sheet as there is a legally enforceable right to set off current tax assets against current tax liabilities, and the deferred income taxes related to the same fiscal authority.

24 SHARE CAPITAL

		<b>Authorised</b>	
		<b>Number of shares</b>	<b>RMB'000</b>
At 31st January 2003	(a)	3,900,000	413
Increase in authorised ordinary share capital	(b)	996,100,000	105,587
At 31st December 2003		<u>1,000,000,000</u>	<u>106,000</u>
At 31st December 2004		<u>1,000,000,000</u>	<u>106,000</u>
		<b>Issued and fully paid</b>	
		<b>Number of shares</b>	<b>RMB'000</b>
As at 31 January 2003	(a)	7,800	—
Issue of shares	(c), (d)	419,992,200	44,520
At 31st December 2003		420,000,000	44,520
Exercise of share options	(e)	1,820,000	193
At 31st December 2004		<u>421,820,000</u>	<u>44,713</u>

- (a) On 14th May 2002, the authorised share capital of the Company was re-denominated into Hong Kong dollars at an amount of HKD390,000 (approximately RMB413,000) and was sub-divided into 3,900,000 shares of HKD0.10 each. The issued share capital of the Company was HKD780, divided into 7,800 nil-paid shares.
- (b) On 10th June 2003, the authorised share capital of the Company was increased from HKD390,000 to HKD100,000,000 (approximately RMB106,000,000), by the creation of an additional 996,100,000 shares of HKD0.10 each.
- (c) On 10th June 2003, the Company acquired the entire issued share capital of Ko Yo BVI by issuing 313,192,200 shares of HKD0.10 each, credited as fully paid, and crediting as fully paid the 7,800 nil paid shares previously issued as mentioned in Note (a) above, totalling 313,200,000 shares with an amount of HKD31,320,000 (approximately RMB33,199,000).
- (d) On 10th July 2003, 106,800,000 shares of HKD0.10 each were issued at HKD0.40 per share through a placing and public offer (the “New Issue”), resulting in net proceeds of approximately RMB30,081,000. Immediately after the New Issue, the issued and fully-paid share capital of the Company was HKD42,000,000 (approximately RMB44,520,000), divided into 420,000,000 shares of HKD0.10 each.

### 24 SHARE CAPITAL *(Continued)*

- (e) The Company has a share option scheme adopted on 10th June 2003 (the “Share Option Scheme”). The purpose of the Share Option Scheme is to recognise the contribution of the eligible participants, and to provide a performance related incentive to them. The eligible participants include the employees (including executive and non-executive directors) and consultants of the Group.

The number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the Share Option Scheme and any other schemes must not exceed 30% of the shares in issue from time to time. The total number of shares which may be issued upon exercise of all options to be granted under the Share Option Scheme and any other schemes must not exceed 42,000,000 shares, 10% of the shares of the Company at the date of commencement of dealings of the Company’s share on GEM.

Each participant is entitled to a maximum of 4,200,000 share options, which are valid for a period of 10 years from the date of grant. Participants need to pay option price at HKD10 per option for each acceptance of option offer and is required to hold the option for a minimum of one year before exercising part of the options. The subscription price will be determined by the Company’s board of directors, and will not be less than the highest of (a) the closing price of the shares quoted on the GEM of the Stock Exchange on the date of the offer; (b) the average closing price of the shares quoted on the GEM of the Stock Exchange for the five business days immediately preceding the date of the offer and (c) the nominal value of the shares.

On 23rd September 2003, the Company granted share options to two executive directors, two independent directors and six employees to subscribe for an aggregate of 25,200,000 shares of the Company with an exercise price of HKD0.62.

On 10th August 2004, the Company granted share options to 247 employees for an aggregate of 1,820,000 shares of the Company with an exercise price of HKD0.33.

Share options granted on 10th August 2004 was exercised on 23rd August 2004, resulted in 1,820,000 shares being issued at HKD0.33 per share (equivalent to RMB0.35), yielding the proceeds of approximately HKD601,000 (equivalent to RMB637,000).



24 SHARE CAPITAL (Continued)

Movements in the number of share options outstanding during the years are as follows:

	Number of options '000
At 1st January 2003	—
Granted	25,200
	<hr/>
At 31st December 2003	25,200
Granted	1,820
Exercised	(1,820)
	<hr/>
At 31st December 2004	<u>25,200</u>

Share options outstanding at the end of the year were granted on 23rd September 2003 with an exercise price of HKD0.62 (equivalent to RMB0.67), and have the following terms:

Directors	Number of options '000	Exercise period of share options
Chi Chuan	4,200	23rd September 2004 to 22nd September 2013
Li Shengdi	4,200	23rd September 2004 to 22nd September 2013
Man Au Vivian	3,800	23rd September 2004 to 22nd September 2013
Hu Xiaoping	400	23rd September 2004 to 22nd September 2013
Woo Che-wor, Alex	400	23rd September 2004 to 22nd September 2013
	<hr/>	
	13,000	
Other employees	12,200	23rd September 2004 to 22nd September 2013
	<hr/>	
At 31st December 2004	<u>25,200</u>	

No share options were cancelled during the year (2003: Nil).

## NOTES TO THE ACCOUNTS

### 25 RESERVES

Movements of the Group's reserves were as follows:

	Share premium RMB'000	Merger reserve RMB'000	Reserve fund RMB'000	Enterprise expansion fund RMB'000	Exchange difference RMB'000	Retained earnings RMB'000	Total RMB'000
At 1st January 2004	18,760	(22,041)	7,974	412	115	72,591	77,811
Profit for the year	—	—	—	—	—	32,712	32,712
Exercise of share options ( <i>Note 24</i> )	444	—	—	—	—	—	444
Appropriation	—	—	2,563	146	—	(2,709)	—
Dividends	—	—	—	—	—	(4,586)	(4,586)
	<u>19,204</u>	<u>(22,041)</u>	<u>10,537</u>	<u>558</u>	<u>115</u>	<u>98,008</u>	<u>106,381</u>
At 31st December 2004	<u>19,204</u>	<u>(22,041)</u>	<u>10,537</u>	<u>558</u>	<u>115</u>	<u>98,008</u>	<u>106,381</u>
Representing:							
2004 final dividends proposed						5,142	5,142
Others						92,866	101,239
						<u>98,008</u>	<u>106,381</u>

Movements of the Company's reserves were as follows:

	Share premium RMB'000	Retained earnings RMB'000	Total RMB'000
At 1st January 2004	55,922	4,597	60,519
Profit attributable to shareholders	—	5,208	5,208
Exercise of share options	444	—	444
Dividends	—	(4,586)	(4,586)
	<u>56,366</u>	<u>5,219</u>	<u>61,585</u>
At 31st December 2004	<u>56,366</u>	<u>5,219</u>	<u>61,585</u>
Representing:			
2004 final dividends proposed		5,142	5,142
Others		77	56,443
		<u>5,219</u>	<u>61,585</u>

**25 RESERVES** *(Continued)***(a) Statutory reserves**

The Company's subsidiaries established in Mainland China are governed by the laws and regulations of Mainland China and their articles of association. They are required to provide for certain statutory funds, namely, reserve fund, enterprise expansion fund and staff and workers' bonus and welfare fund which are appropriated from net profit after taxation but before dividend distribution based on the local statutory accounts prepared in accordance with accounting principles and relevant financial regulations applicable to enterprises established in Mainland China. They are required to allocate at least 10% of their net profit to the reserve fund until the balance of such fund has reached 50% of its registered capital. Appropriations of enterprise expansion fund and staff and workers' bonus and welfare fund are determined at the discretion of its directors. Appropriation to staff and workers' bonus and welfare fund is charged to expenses. The reserve fund can only be used, upon approval by the relevant authorities, to offset accumulated losses or increase capital. The enterprise expansion fund can only be used to increase capital upon approval by the relevant authorities. The staff and workers' bonus and welfare fund can only be used for special bonus or collective welfare of their employees, and assets acquired through this fund shall not be treated as assets of the Group. Accordingly, the balance of staff and workers' bonus and welfare fund is recorded as a liability of the Group.

**(b) Merger reserve**

Merger reserve of the Group represents the difference between the nominal value of the share capital issued by the Company and share capital and share premium of a subsidiary acquired through an exchange of shares.

26 CONSOLIDATED CASH FLOW STATEMENT

(a) Reconciliation of profit before taxation to net cash inflow/(outflow) from operating activities

	2004 RMB'000	2003 RMB'000
Profit before taxation	33,894	24,104
Depreciation	9,770	9,169
Amortisation of negative goodwill	(500)	(500)
(Gain)/loss on disposal of fixed assets	(142)	98
Impairment of fixed assets	—	126
Interest income	(773)	(148)
Interest expenses	7,476	5,877
Dividend income	(130)	(130)
Listing expenses	4,098	—
	<hr/>	<hr/>
Operating profit before working capital changes	53,693	38,596
Increase in inventories	(26,358)	(7,360)
Decrease in trade and other receivables	320	10,514
Increase/(decrease) in trade and other payables	31,394	(2,822)
Decrease in other long-term payables	(61)	(42,500)
Decrease in amount due to related companies	(2,368)	(42)
	<hr/>	<hr/>
Cash generated from/(used in) operating activities	<u>56,620</u>	<u>(3,614)</u>

(b) Non-cash transactions:

	2004 RMB'000	2003 RMB'000
Acquisition of assets by taken up related liabilities	<u>12,894</u>	<u>—</u>

On 30th December 2004, Dazhu Ko Yo Chemical, an indirectly wholly-owned subsidiary of the Company, entered into an Assets Acquisition Agreement with Sichuan Dazhu Hongsen Chemical Industry Co., Ltd. (“Dazhu Hongsen Chemical”) to acquire the Sale Assets of Dazhu Hongsen Chemical at the total consideration of RMB24,264,000 of which RMB12,894,000 will be settled by taken up Dazhu Hongsen Chemical’s related liabilities.

26 CONSOLIDATED CASH FLOW STATEMENT (Continued)

(c) Analysis of changes in financing during the year

	Pledged bank deposit		Share capital including premium		Minority interests		Loans		Convertible note payable	
	2004 RMB'000	2003 RMB'000	2004 RMB'000	2003 RMB'000	2004 RMB'000	2003 RMB'000	2004 RMB'000	2003 RMB'000	2004 RMB'000	2003 RMB'000
At 1st January	(13,032)	(9,500)	63,280	26,972	600	—	97,230	76,230	—	5,300
Increase in pledged bank deposit	(40,908)	(3,532)	—	—	—	—	—	—	—	—
Issue of shares	—	—	—	36,308	—	—	—	—	—	—
Exercise of share options	—	—	637	—	—	—	—	—	—	—
Contribution from a minority shareholder	—	—	—	—	—	600	—	—	—	—
New loans payable	—	—	—	—	—	—	112,830	64,891	—	—
Repayment of amounts borrowed	—	—	—	—	—	—	(77,430)	(43,891)	—	—
Repayment of convertible note	—	—	—	—	—	—	—	—	—	(5,300)
Minority Interests' share of profits	—	—	—	—	(33)	—	—	—	—	—
At 31st December	<u>(53,940)</u>	<u>(13,032)</u>	<u>63,917</u>	<u>63,280</u>	<u>567</u>	<u>600</u>	<u>132,630</u>	<u>97,230</u>	<u>—</u>	<u>—</u>

27 COMMITMENTS

(a) Capital commitments for property, plant and equipment

	Group	
	2004 RMB'000	2003 RMB'000
Contracted but not provided for	4,342	3,945
	<u>4,342</u>	<u>3,945</u>

The Company did not have any material capital commitments at 31st December 2004 (2003: Nil).

## NOTES TO THE ACCOUNTS

### 27 COMMITMENTS (Continued)

#### (b) Commitments under operating leases

At 31st December 2004, the Group had future aggregate minimum lease payments under non-cancellable operating leases for land and buildings as follows:

	Group	
	2004	2003
	RMB'000	RMB'000
Not later than one year	820	460
Later than one year and not later than five years	453	—
	<u>1,273</u>	<u>460</u>

The Company did not have any operating leases commitments at 31st December 2004 (2003: Nil).

### 28 APPROVAL OF ACCOUNTS

The accounts were approved by the board of directors on 23rd March 2004.

## FIVE YEAR FINANCIAL SUMMARY

The following table summarizes the audited results, assets and liabilities of the Group for the five years ended 31 December 2004.

	<b>2004</b>	2003	2002	2001	2000
	<b>RMB'000</b>	RMB'000	RMB'000	RMB'000	RMB'000
Turnover	<b><u>422,728</u></b>	<u>281,810</u>	<u>277,572</u>	<u>164,535</u>	<u>167,825</u>
Profit before taxation	<b>33,894</b>	24,104	31,199	16,544	13,675
Taxation	<b><u>(1,215)</u></b>	<u>(31)</u>	<u>427</u>	<u>—</u>	<u>(512)</u>
Profit after taxation	<b>32,679</b>	24,073	31,626	16,544	13,163
Minority interests	<b>33</b>	—	(286)	(1,047)	(879)
Profit attributable to shareholders	<b><u>32,712</u></b>	<u>24,073</u>	<u>31,340</u>	<u>15,497</u>	<u>12,284</u>
Total assets	<b>361,174</b>	266,221	239,276	185,363	168,920
Total liabilities	<b>(209,513)</b>	(143,290)	(174,709)	(143,400)	(151,478)
Minority interests	<b><u>(567)</u></b>	<u>(600)</u>	<u>—</u>	<u>(2,510)</u>	<u>(1,463)</u>
Shareholders' funds	<b><u>151,094</u></b>	<u>122,331</u>	<u>64,567</u>	<u>39,453</u>	<u>15,979</u>

## NOTICE OF ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that the annual general meeting of the members of Ko Yo Ecological Agrotech (Group) Limited (the “Company”) will be held at Suite No.02, 31st Floor, Sino Plaza, 255-257 Gloucester Road, Causeway Bay, Hong Kong on 26 April 2005 at 11:00 a.m. for the following purposes:

1. To receive and consider the audited consolidated financial statements of the Company and its subsidiaries and the report of the directors and the auditors for the year ended 31 December 2004;
2. To consider the re-election of the retiring directors of the Company;
3. To consider and authorize the board of directors (the “Board”) of the Company to fix the directors’ remunerations;
4. To consider and approve the final dividend of the Company for the year ended 31 December 2004;
5. To consider the re-appointment of PricewaterhouseCoopers as auditors of the Company and to authorize the Board to fix their remuneration; and

As special business, to consider and if thought fit, pass the following resolutions as ordinary resolutions:

6. “THAT:
  - (a) subject to sub-paragraph (c) below, the exercise by the directors of the Company (“Directors”) during the Relevant Period (as defined below) of all the powers of the Company to allot, issue and deal with the ordinary shares of par value HK\$0.10 each (the “Shares”) in the capital of the Company and to make an offer or agreement or grant an option which would or might require such Shares to be allotted and issued be generally and unconditionally approved;
  - (b) the Directors be authorized to make an offer or agreement or grant an option during the Relevant Period which would or might require Shares in the capital of the Company to be allotted and issued either during or after the end of the Relevant Period pursuant to sub-paragraph (a) above;
  - (c) the aggregate nominal value of the Shares in the capital of the Company allotted or agreed conditionally or unconditionally to be allotted (whether pursuant to an option or otherwise) by the Directors pursuant to the approvals in sub-paragraphs (a) and (b) above, otherwise than pursuant to a rights issue (as defined below) or pursuant to the exercise of options which may be granted under the Share Option Scheme adopted by the Company on 10 June 2003 or an issue of Shares of the Company in lieu of the whole or part of a dividend on Shares of the Company in accordance with the articles of association of the Company, shall not exceed the aggregate of:
    - (i) 20% of the aggregate nominal value of the share capital of the Company in issue; and
    - (ii) conditional on the passing of Resolution No. 8 below, the aggregate nominal amount of the share capital of the Company purchased under the authority referred to in Resolution No. 7;



## NOTICE OF ANNUAL GENERAL MEETING

(d) for the purpose of this resolution:

“Relevant Period” means the period from the passing of this resolution until whichever is the earlier of:

- (i) the conclusion of the next annual general meeting of the Company following the passing of this resolution; or
- (ii) the expiration of the period within which the next annual general meeting of the Company is required by the laws of the Cayman Islands or the articles of association of the Company to be held; or
- (iii) the passing of an ordinary resolution by the shareholders of the Company in general meeting revoking or varying the authority given to the Directors by this resolution; and

“rights issue” means the allotment or issue of Shares in the Company or other securities which would or might require Shares to be allotted and issued pursuant to an offer made to all the shareholders of the Company (excluding for such purpose any shareholder who is resident in a place where such offer is not permitted under the laws of that place) and, where appropriate, the holders of other equity securities of the Company entitled to such offer, pro rata (apart from fractional entitlements) to their existing holdings of Shares or such other equity securities.”

7. “THAT:

- (a) the Directors be granted a general mandate to exercise all the powers of the Company to purchase its own securities on the Stock Exchange of Hong Kong Limited (the “Stock Exchange”) or on any other stock exchange on which shares in the capital of the Company may be listed and which is recognized by the Securities and Futures Commission and the Stock Exchange for this purpose, such number of securities as will represent up to 10% of the aggregate nominal value of the share capital of the Company in issue, during the Relevant Period (defined below) in accordance with all applicable laws and the requirements of the Rules Governing the Listing of Securities on the Growth Enterprise Market of the Stock Exchange (“GEM Listing Rules”) (as amended from time to time) (or of such other stock exchange);

(b) for the purpose of this resolution:

“Relevant Period” means the period from the passing of this resolution until whichever is the earlier of:

- (i) the conclusion of the next annual general meeting of the Company following the passing of this resolution; or
- (ii) the expiration of the period within which the next annual general meeting of the Company is required by the laws of the Cayman Islands or the articles of association of the Company to be held; or
- (iii) the passing of an ordinary resolution by shareholders of the Company in general meeting revoking or varying the authority given to the Directors by this resolution.”

## NOTICE OF ANNUAL GENERAL MEETING

8. "THAT the unconditional general mandate referred to in Resolution No. 6 above be extended by the addition to the aggregate nominal amount of the share capital of the Company which may be allotted or agreed to be allotted by the Directors pursuant to such unconditional general mandate of an amount representing the aggregate nominal amount of the securities of the Company purchased by the Company pursuant to the mandate to purchase securities referred to in Resolution No.7 above, provided that such extended amount shall not exceed 10% of the aggregate nominal value of the share capital of the Company in issue."

On behalf of the board

**Fung Wai Shing**

*Company Secretary*

Hong Kong, 23 March 2005

*Notes:*

- (1) A member entitled to attend and vote at the meeting is entitled to appoint a proxy to attend and, in the event of, a poll, vote instead of him. A proxy need not be a member of the Company.
- (2) In order to be valid, the form of proxy must be deposited with the Company's share registrar in Hong Kong, Standard Registrars Limited, at G/F., Bank of East Asia Harbour View Centre, 56 Gloucester Road, Wanchai, Hong Kong, together with any power of attorney or other authority, under which it is signed, or a notorially certified copy of that power or authority, not less than 48 hours before the time for holding the meeting or any adjournment thereof.
- (3) Where there are joint holders of any shares in the Company, any one of such joint holders may vote, either in person or by proxy, in respect of such shares as if he were solely entitled thereto, but if more than one of such joint holders are present at the meeting, the senior who tenders a vote, whether in person or by proxy, shall be accepted to the exclusion of the votes of the other joint holders, and for this purpose seniority shall be determined by the order in which the names stand in the register in respect of the joint holding.
- (4) The register of members of the Company will be closed for the purpose of determining the entitlements of the proposed final dividend from 21 April 2005 to 26 April 2005, both days inclusive, during which period no transfer of shares will be effected. In order to qualify for the proposed final dividend, all transfers, accompanied by the relevant share certificates, must be lodged for registration with the Company's registrar, Standard Registrars Limited, at the above address no later than 4:00 p.m. on 20 April 2005.
- (5) Concerning Resolutions No. 6 and No. 7, the Board wishes to state that there is no immediate plan to issue any new shares or to repurchase any shares of the Company. The general mandates are being sought from shareholders in compliance with the Companies Law (Law 3 of 1961, as revised and consolidated) of the Cayman Islands and the GEM Listing Rules.
- (6) For the sake of good corporate governance practice, the Chairman intends to demand poll voting for all the resolutions set out in the notice of the annual general meeting.