



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)

(Stock code: 8042)

2006

First Quarterly Report
For the three months
ended 31 March 2006



CHARACTERISTICS OF THE GROWTH ENTERPRISE MARKET (“GEM”) OF THE STOCK EXCHANGE OF HONG KONG LIMITED (THE “STOCK EXCHANGE”)

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This report, for which the directors of Ko Yo Ecological Agrotech (Group) Limited collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on GEM of the Stock Exchange for the purpose of giving information with regard to Ko Yo Ecological Agrotech (Group) Limited. The directors of Ko Yo Ecological Agrotech (Group) Limited, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief: (i) the information contained in this report is accurate and complete in all material respects and not misleading; (ii) there are no other matters the omission of which would make any statement in this report misleading; and (iii) all opinions expressed in this report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

HIGHLIGHTS

- For the three months ended 31 March 2006, unaudited turnover increased to approximately RMB177 million, which represents an approximate 24% growth as compared to that of the same period 2005.
- The sale quantities of BB Fertilizers of the Group increased to 52,338 tonnes, which represents a growth of 26% as compared with the first quarter of 2005.
- Profit attributable to shareholders of the Group was approximately RMB12.5 million for the three months ended 31 March 2006, which represents an approximately 4% growth as compared to that of the same period last year.
- Basic earnings per share of the Group was approximately RMB2.96 cents for the three months ended 31 March 2006.

UNAUDITED CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT

For the three months ended 31 March 2006

The board of directors (the “Board” or the “Directors”) of Ko Yo Ecological Agrotech (Group) Limited (the “Company”) is pleased to announce the unaudited consolidated results of the Company and its subsidiaries (collectively, the “Group”) for the three months ended 31 March 2006, together with the unaudited comparative figures for the corresponding periods in 2005 as follows:

		Three months ended 31 March 2006	Three months ended 31 March 2005
	<i>Notes</i>	RMB'000	RMB'000
Turnover	2	177,434	142,924
Cost of sales		(146,955)	(113,354)
Gross profit		30,479	29,570
Interest income		61	154
Distribution costs		(6,563)	(7,763)
Administrative expenses		(9,102)	(7,610)
Other income		549	1,442
Operating profit		15,424	15,793
Finance costs		(1,166)	(1,745)
Profit before taxation		14,258	14,048
Taxation	3	(1,765)	(2,026)
Profit after taxation		12,493	12,022
Minority interests		—	(11)
Profit attributable to shareholders		12,493	12,011
Basic earnings per share (RMB cents)	4	2.96	2.85
Diluted earnings per share	4	N/A	N/A

Notes:

1. Basis of preparation

The Hong Kong Institute of Certified Public Accountant (“HKICPA”) has undertaken to converge by 1 January 2005 all Hong Kong Financial Reporting Standards (“HKFRSs”) with International Financial Reporting Standards (“IFRSs”) issued by the International Accounting Standards Board. As a result, the HKICPA had aligned HKFRSs with the requirements of IFRSs in all materials respects as at 31 December 2004. The accounts have been prepared under the historical cost convention.

The adoption of HKFRS 2 has resulted in a change in accounting policy for employee share options. Prior to this, the provision of share options to employees did not result in a charge to the profit and loss account. Following the adoption of HKFRS 2, the fair value of share options at grant date is amortised over the relevant vesting periods to the profit and loss account. The Company has not applied this HKFRS retrospectively as share options of the Company granted after 7 November 2002 had vested at 1 January 2005.

The adoption of HKFRS 3 has resulted in a change in the accounting policy for negative goodwill. Prior to this, negative goodwill was recognized as income on a straight-line basis in the profit and loss account over the remaining weighted average useful life of assets acquired of 30 years. In accordance with the provision of HKFRS 3, the carrying amount of previously recognized negative goodwill as at 1 January 2005 shall be derecognized with a corresponding adjustment to the opening balance of retained earnings.

The adoption of other new HKFRS does not result in substantial changes to the Group’s accounting policies except certain presentation and disclosure of the accounts will be affected.

2. Turnover

Turnover represents the net amounts received and receivable for chemical products and chemical fertilizers sold, less returns and allowances and value-added taxes, if applicable, during the three-month period. The Group’s revenues are primarily generated in the People’s Republic of China (the “PRC”).

Turnover consisted the following products:

	(unaudited)		(unaudited)	
	For the three months ended 31 March 2006		For the three months ended 31 March 2005	
	RMB’000	%	RMB’000	%
BB Fertilizers	86,527	48.8	73,954	51.8
Sodium carbonate	20,778	11.7	26,788	18.7
Ammonium chloride	9,625	5.4	13,399	9.4
Urea	56,324	31.7	20,901	14.6
Ammonia	1,906	1.1	3,909	2.7
Ammonium bicarbonate	2,118	1.2	3,973	2.8
Others	156	0.1	—	—
	<u>177,434</u>	<u>100</u>	<u>142,924</u>	<u>100</u>

3. Taxation

No provision for profits tax in the Cayman Islands, the 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 three months ended 31 March 2006.

Chengdu Ko Yo Chemical Industry Co., Ltd. (“Chengdu Ko Yo Chemical”), Chengdu Ko Yo Compound Fertilisers Co., Ltd. (“Chengdu Ko Yo Compound”), Dezhou Ko Yo Compound Fertiliser Co., Ltd. (“Dezhou Ko Yo Compound”), Dazhou City Dazhu Ko Yo Chemical Industry Co., Ltd. (“Dazhu Ko Yo Chemical”) and Qingdao Ko Yo Chemical Co., Ltd. (“Qingdao Ko Yo Chemical”) were established as foreign investment enterprises in the PRC. They are subject to Enterprise Income Tax (“EIT”) at the rate of 15%, 15%, 33%, 15% 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 for Chengdu Ko Yo Chemical in 2006 is 15%. Pursuant to relevant taxation regulations of the PRC 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 the PRC enterprises, which are local machinery suppliers and unrelated to the Group. Accordingly, EIT provision made for Chengdu Ko Yo Chemical for the three months ended 31 March 2006 was RMB1,310,000.

The EIT provision made for and preferential EIT rate applicable to Chengdu Ko Yo Compound for the three months ended 31 March 2006 are approximately RMB455,000 and 7.5%.

Dezhou Ko Yo Compound, Dazhu Ko Yo Chemical and Qingdao Ko Yo Chemical did not have EIT payable for the three months ended 31 March 2006.

4. Earnings per share

The calculation of basic earnings per share for the three months ended 31 March 2006 is based on the consolidated profit attributable to shareholders of approximately RMB12,493,000 (2005: RMB12,011,000) and the weighted average number of approximately 421,820,000 (2005: 421,820,000) ordinary shares in issue during the periods. Diluted earnings per share is not presented as there were no dilutive potential ordinary shares.

5. Dividend

The Board does not recommend the payment of interim dividend for the three months ended 31 March 2006 (31 March 2005: Nil).

6. Reserve

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	Retaining earnings RMB'000	Total RMB'000
Balance as at						
1 January 2005 (audited)	19,204	(22,041)	10,537	558	98,123	106,381
HKFRS 3	—	—	—	—	12,366	12,366
Balance as at						
1 January 2005 (restated)	19,204	(22,041)	10,537	558	110,489	118,747
Net Profit for the three months ended 31 March 2005	—	—	—	—	12,011	12,011
Balance as at 31 March 2005	<u>19,204</u>	<u>(22,041)</u>	<u>10,537</u>	<u>558</u>	<u>122,500</u>	<u>130,758</u>
Balance as at						
1 January 2006 (audited)	19,204	(22,041)	11,307	943	136,435	145,848
HKFRS 3	—	—	—	—	12,366	12,366
Balance as at						
1 January 2006 (restated)	19,204	(22,041)	11,307	943	148,801	158,214
Net Profit for the three months ended 31 March 2006	—	—	—	—	12,493	12,493
Balance as at 31 March 2006	<u>19,204</u>	<u>(22,041)</u>	<u>11,307</u>	<u>943</u>	<u>161,294</u>	<u>170,707</u>

MANAGEMENT DISCUSSION AND ANALYSIS

Financial Review

For the three months ended 31 March 2006, the Group recorded a turnover of approximately RMB177 million, representing an increase of 24% as compared with approximately RMB143 million for the same period last year. The total sale quantities reached 129,927 tonnes (2005: 105,144 tonnes), which represented a growth of approximately 24%. The turnover derived from the sales of BB Fertilizers was RMB87 million, which achieved a growth of 17% as compared with the same period last year. During the period under review, the growth in turnover of BB Fertilizers of the Group was due to increase in sale quantities of BB Fertilizers. Profit attributable to shareholders was approximately RMB12.5 million (2005: RMB12.0 million), which represented a growth of 4% compared with the same period last year, and earnings per share was RMB2.96 cents (2005: RMB2.85 cents).

During the period under review, the gross profit margin was decreased to 17.2% from 20.7% in the same period last year, which was due to the Group's production systems of the plant in Xindou District underwent substantial maintenance and technology enhancement for twenty-two days resulting in the decrease in apportionment of sales of products with high gross profit margin. Distribution costs were decreased by 15.5% as compared to same period last year. The Group's administrative expenses were increased 19.6% to approximately RMB9.1 million as compared with RMB7.6 million last year, which was due to administrative expenses of Dazhu Ko Yo Chemical and Qingdao Ko Yo Chemical.

Business Review

For the three months period ended 31 March 2006, the Group's total sales quantities of urea, sodium carbonate, ammonia, ammonium chloride and ammonium bicarbonate amounted to 77,569 tonnes, helped by stable product sales channel and good customer relationship. During the period under review, the Group proactively developed overseas market. A total of 835 tonnes compound fertilizers were exported to South-east Asian regions, achieving double growth over the same period last year.

During the period under review, the Group's sales quantities of BB Fertilizers reached 52,338 tonnes, which represented a growth of 26% as compared to the same period last year. This positive result was mainly attributable to the increasing stable and mature sales channel. Concrete measures implemented during the period under review to improve the Group's business performance were as follows:

1. The Group's BB Fertilizers were accredited by the General Administration of Quality Supervision, Inspection Quarantine of the PRC as the "Quarantine Exempted" product in December 2005. This product recognition increased peasants' confidence in purchasing BB Fertilizers and encouraged returned purchases. Through imposing "Quality Assurance" policy throughout the PRC where substandard products of the Group will be indemnified, peasants' loyalty and confidence in the Group and BB fertilizers was boosted.

MANAGEMENT DISCUSSION AND ANALYSIS (Continued)

Business Review (Continued)

2. The Group launched a new product foliar fertilizer that is used in conjunction with BB fertilizers. This product combination could enhance the effectiveness of BB fertilizers and facilitate the healthy growth of agricultural crops. Hence, the income of peasants could be increased.
3. The Group actively carried out marketing promotional activities to further enhance the corporate image. The tailor-made and customer-oriented service “Xia Mi Feng Tian Dai Fu” (「小蜜蜂甜大夫」服務到家門口) provided consolidated the good reputation of the Group.

The Group’s production systems of ammonia, urea and sodium carbonate underwent substantial maintenance and technology enhancement which were longest in time, thus resulting from a relatively slight increase in the Group’s turnover and profit and the drop in gross profit margin during the period under review. Yet the comprehensive maintenance and technology enhancement will lay a solid foundation for the growth of the Group in the second, third and fourth quarters.

Prospect

The 9% GDP growth rate of China and the continued introduction of macroscopic beneficial policies have built up a favorable environment for the Group’s business growth.

Cancellation of agricultural tax was mentioned in document No. 1 regarding “Communist Party of China Central Committee’s Policies and Advices on Promotion of Socialist New Rural Village Construction” (《中共中央國務院關於推進社會主義新農村建設的若干意見》) announced by Xinhua News Agency on 21 February 2006, which is the third document about “San Nong” (「三農」), namely China’s agricultural industry, agricultural villages and peasants, in recent three years. According to the document, agricultural tax will completely be cancelled throughout the PRC in 2006. The new incentive will increase the cultivation motivation of peasants, improve their purchasing power of fertilizers and perk up the usage of fertilizers.

“The Notice of the Enhancement of Chemical Fertilizer Production and Supply and Price Adjustment in 2006” was promulgated by the National Development and Reform Commission and the Ministry of Finance on 20 January 2006. Privileges of the Notice to the agricultural industry include:

1. Discount on electricity price for chemical fertilizer production
2. Temporary waive of value-added tax on urea product
3. Waive of railway construction fee for chemical fertilizer railway transportation

MANAGEMENT DISCUSSION AND ANALYSIS (Continued)

Prospect (Continued)

4. Temporary seasonal tariff on urea export (30% tariff from January to September and 15 % tariff from October to December)

The Agricultural Department of China continues the promotion of “Testing Soil to Prescribe and Apply Suitable Fertilizers” policy. This policy enhances peasants’ understanding towards compound fertilizers and BB Fertilizers, enabling BB Fertilizers to become a fast-growing fertilizer.

The production technology improvement for the “large granule urea” production line, investing RMB6 million, was completed and the production line has commenced operation in April 2006. The production line can achieve an annual production capacity of 80,000 tonnes “large granule urea”. With the advanced production line, the Group can produce the “large granule urea” itself instead of purchasing from suppliers which will increase the gross profit of BB Fertilizers to around RMB100 per tonne. As a result, the competitiveness of BB Fertilizers in the market will be further strengthened.

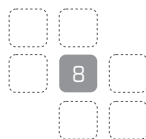
The project of new BB Fertilizers production line in Qingdao Laixi City, with an annual production capacity of 300,000 tonnes, is expected to commence operation in lower half of 2006. Currently, foundation works and facilities installation are running smoothly. The expected production capacity of BB Fertilizers will reach 700,000 tonnes this year. The enlarged production capacity will accelerate the business growth of the Group in the future.

Under the vigorous market competition and revenue dependency on the cost of raw materials, the Directors have intention to plan to increase the Group’s production capacity of urea by utilizing the abundant natural gas resource in Sichuan Province, in order to cope with the increasing internal demand for raw materials for the Group’s production of BB fertilizers.

DISCLOSURE OF INTERESTS

(a) Interests of the Directors in the Company

As at 31 March 2006, 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 of Hong Kong Limited (“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 Rules Governing the Listing of Securities on the Growth Enterprise Market of Stock Exchange (the “GEM Listing Rules”) were as follows:



DISCLOSURE OF INTERESTS *(Continued)***(a) Interests of the Directors in the Company** *(Continued)*

(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

Share options were granted to certain directors, employees and consultant of the Company or its subsidiaries under the share option scheme adopted by written resolutions of shareholders on 10 June 2003, which was amended by an ordinary resolution duly passed at an extraordinary general meeting by the Company's shareholders on 28 July 2004. 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 March 2006	Exercisable period	Exercise price HK\$
		Outstanding as at 1 January 2006	Granted during the period	Exercised during the period	Cancelled during the period			
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

DISCLOSURE OF INTERESTS (Continued)

(a) Interests of the Directors in the Company (Continued)

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

Name of Director	Date of Grant	Outstanding as at 1 January 2006	Number of share options			Outstanding as at 31 March 2006	Exercisable period	Exercise price HK\$
			Granted during the period	Exercised during the period	Cancelled during the period			
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

(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
Li Weiruo	Ko Yo Development Co., Limited ("Ko Yo Hong Kong") (Note)	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

DISCLOSURE OF INTERESTS *(Continued)*

(a) Interests of the Directors in the Company *(Continued)*

(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

(b) Interests of the substantial shareholders in the Company

As at 31 March 2006, 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.

(c) Interests of other persons in the Company

As at 31 March 2006, there was no person or company (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 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 period under review.

AUDIT COMMITTEE

The Company established an audit committee on 10 June 2003 with written terms of reference in compliance with Rules 5.28 to 5.33 of 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 the Group 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 unaudited quarterly accounts of the Company and the Group for the three months ended 31 March 2006.

The Company confirmed that annual confirmations of independence were received from each of independent non-executive directors of the Company pursuant to Rule 5.09 of the GEM Listing Rules and all independent non-executive directors are considered independent.

BOARD PRACTICES AND PROCEDURES

Save for the founder of the Group, Mr. Li Weiruo, currently holds both roles of the Chairman and the Chief Executive Officer, the Company had complied throughout the period under review the minimum standards of good practice concerning the general management responsibilities of the Board as in the Code on Corporate Governance Practices as set out in Appendix 15 of the GEM Listing Rules. Appropriate actions have been taken by the Company for complying with the Code on Corporate Governance Practices.

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 period under review.

By Order of the Board

Li Weiruo

Chairman

Chengdu, the PRC, 10 May 2006

