

ANNUAL REPORT **2006**



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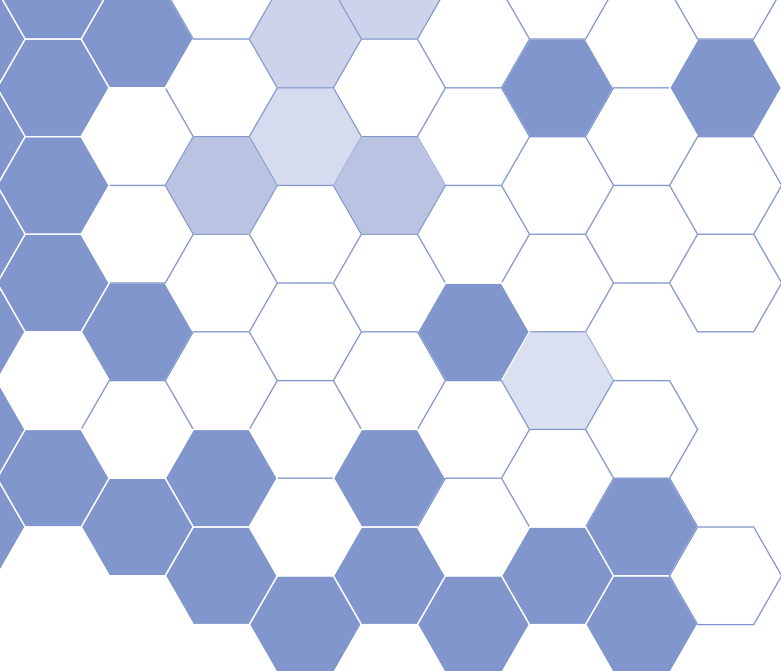


CHANGMAO BIOCHEMICAL ENGINEERING COMPANY LIMITED

常茂生物化學工程股份有限公司

(A Joint Stock Limited Company Incorporated In The People's Republic Of China)

(Stock Code: 8208)



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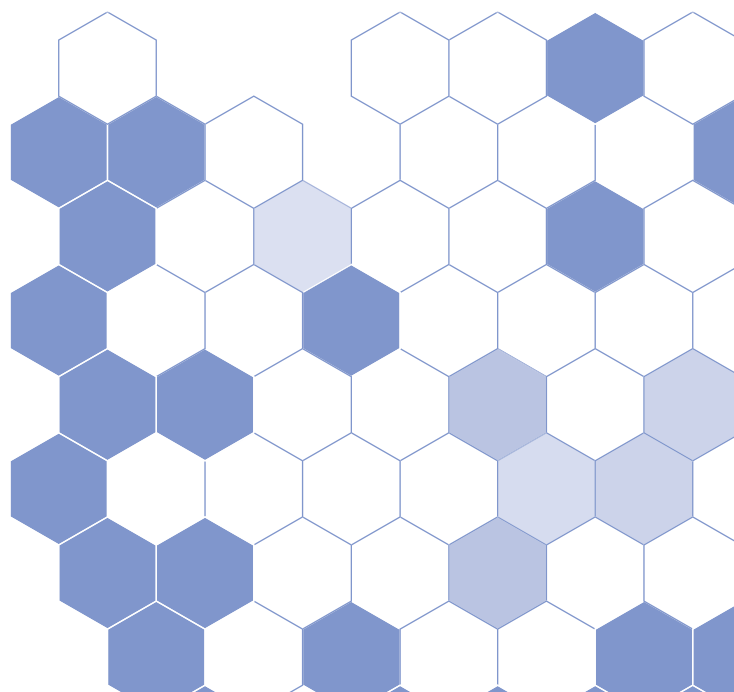
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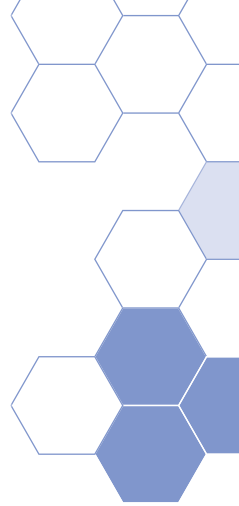
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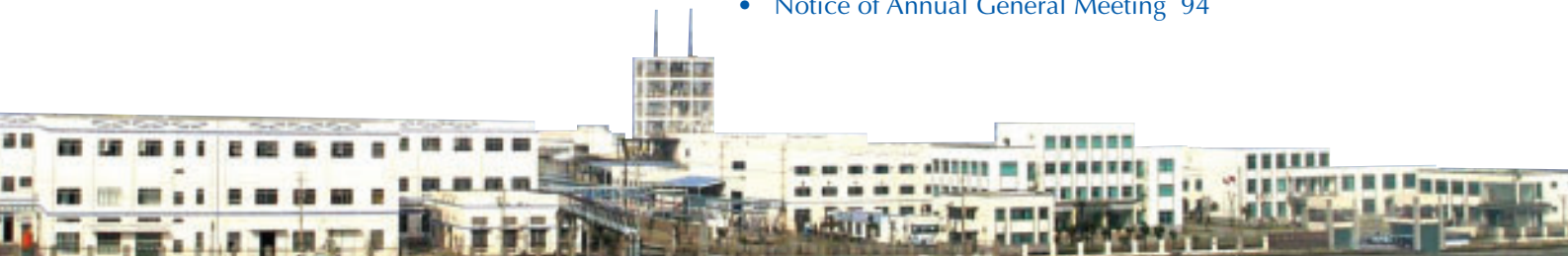
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This report, for which the directors of Changmao Biochemical Engineering Company Limited (the “Directors”) collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on GEM (“GEM Listing Rules”) for the purposes of giving information with regard to Changmao Biochemical Engineering Company Limited. The Directors, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief: (1) the information contained in this report is accurate and complete in all material respects and not misleading; (2) there are no other matters the omission of which would make any statement in this report misleading; and (3) 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.





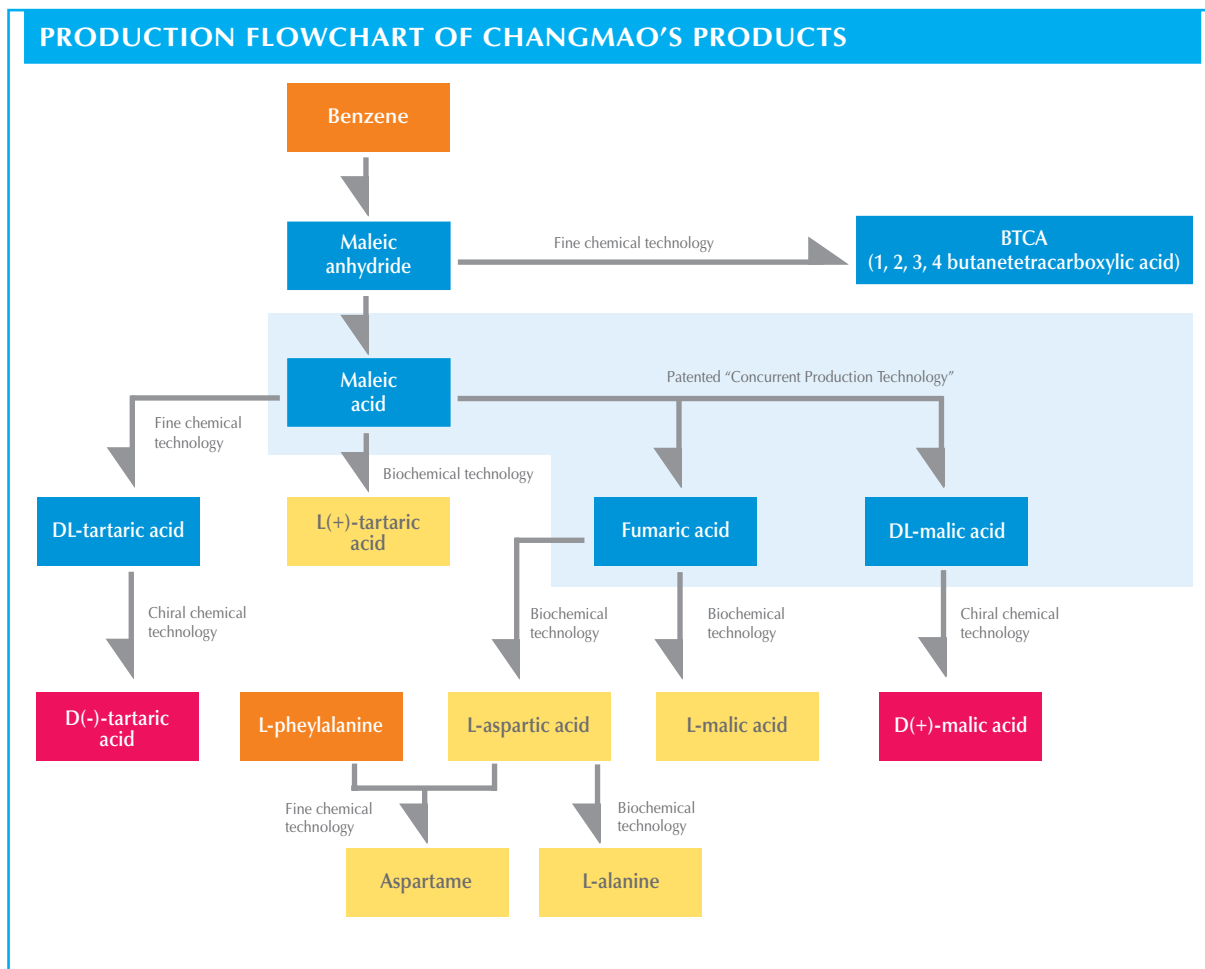
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CORPORATE PROFILE

Established in 1992, Changmao Biochemical Engineering Company Limited (the “Company” or “Changmao”) is a leading organic acid producer in the People’s Republic of China (the “PRC”). Changmao produces organic acids for sales to food additive, chemical and pharmaceutical industries. Changmao’s products conform to the highest international standards and are mainly exported to overseas such as Western Europe, the United States, Australia and Japan.

The core products of the Company and its subsidiary (collectively referred to as the “Group”) are organic acids and their derivatives with four carbons in their structures including fumaric acid, maleic acid, L-malic acid, D-malic acid, DL-malic acid, L(+)-tartaric acid, D(-)-tartaric acid, DL-tartaric acid, L-aspartic acid and aspartame. The Group’s major products are produced along vertical production chains. The major advantage of the production chains is that each of the products in the production chains is also a finished product for sales to customers.



CORPORATE PROFILE

The Group persists in pursuing advanced technologies as its production direction and focuses in investment in new technology research and development which combines the production process with theoretical concepts. The Group received numerous awards in relation to production technologies including 技術發明一等獎 (First Prize in Technological Achievement) and 進步二等獎 (Second Prize in Scientific Improvement) in 中國石油化工行業 (The Oil Chemical Industry in China). The Group attained the ISO9001 Quality System Standards and Hazard Analysis Critical Control Point (HACCP) certificate. Its core product, L(+)-tartaric acid obtained the Food and Drug Administration (FDA) certificate in 2006 and was also recognised as a 江蘇名牌產品 (Jiangsu Province Top Brand).

The Group's major competitive edge is its delicate and advanced production system. Changmao successfully applied the theoretical concepts of enzyme technology and chirotechnology in its highly efficient and cost effective production process. The Group has a research and development base in Changzhou, the Jiangsu Biochemical Chirotechnology Research Centre (the "Chirotechnology Centre"), to research on new products and new production technologies. The Group believes its strong ability in research and development would enable the Group continues to grow.



CORPORATE INFORMATION

EXECUTIVE DIRECTORS

Mr. Rui Xin Sheng
Mr. Jiang Jun Jie

NON-EXECUTIVE DIRECTORS

Mr. Zeng Xian Biao
Mr. Yu Xiao Ping
Mr. Lu Chong Zhu
Ms. Leng Yi Xin

INDEPENDENT NON-EXECUTIVE DIRECTORS

Prof. Ouyang Ping Kai
Prof. Yang Sheng Li
Ms. Wei Xin

SUPERVISORS NOMINATED BY SHAREHOLDERS

Ms. Zhou Rui Juan
Mr. Lu He Xing

SUPERVISOR NOMINATED BY EMPLOYEES

Mr. Pan Chun

INDEPENDENT SUPERVISORS NOMINATED BY SHAREHOLDERS

Prof. Gu Jian Xin
Prof. Jiang Yao Zhong

COMPANY SECRETARY

Ms. Wan, Pui Ling Alice (CPA)

AUTHORISED REPRESENTATIVES

Mr. Rui Xin Sheng
Ms. Wan, Pui Ling Alice (CPA)

COMPLIANCE OFFICER

Mr. Rui Xin Sheng

QUALIFIED ACCOUNTANT

Ms. Wan, Pui Ling Alice (CPA)

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AUDIT COMMITTEE

Prof. Ouyang Ping Kai
Prof. Yang Sheng Li
Ms. Wei Xin

REMUNERATION COMMITTEE

Mr. Rui Xin Sheng
Prof. Ouyang Ping Kai
Prof. Yang Sheng Li
Ms. Wei Xin

LEGAL ADDRESS

Western Chemical Area
Jiangbian Developing Zone
Changzhou City
Jiangsu Province, 213033
The PRC

PRINCIPAL PLACE OF BUSINESS IN HONG KONG

Room 54, 5/F, New Henry House
10 Ice House Street
Central
Hong Kong

PRINCIPAL BANKERS

Bank of China
Changzhou Branch, the PRC

Industrial and Commercial Bank of China
Changzhou Branch, the PRC

HONG KONG SHARE REGISTRAR AND TRANSFER OFFICE

Computershare Hong Kong Investor
Services Limited
46th Floor
Hopewell Centre
183 Queen's Road East
Hong Kong

AUDITORS

PricewaterhouseCoopers
Certified Public Accountants

COMPANY'S WEBSITE ADDRESS

www.cmbec.com

GEM STOCK CODE

8208

CHAIRMAN'S STATEMENT

To the Shareholders,

On behalf of the board of directors of the Company (the "Board"), I am pleased to present the annual report of the Company for the year ended 31 December 2006. In 2006, the production and operation of the Group posted a steady growth. The Group met its objectives in the new construction projects. The progress of collaboration with international partners and of research and development was satisfactory. The acquisition projects were smooth. These factors have promoted the healthy development of the Group.

RESULTS OF THE YEAR

The Group's turnover was Rmb321,440,000 and the net profit was Rmb67,358,000 for the year ended 31 December 2006. Although the new projects in 2006 have not achieved the expected results and the finance cost, selling and administrative expenses were more than last year, the increase in sales of existing products helped the Group to maintain a net profit with similar level compared to last year. The new projects in 2006 had laid a solid foundation for the long term development of the Group. The Group is financially stable and has high potential in future development.

DIVIDEND

The Board proposed to declare a final dividend of Rmb0.022 per share (2005: Rmb 0.033 per share) for the year ended 31 December 2006. The proposed final dividend is subject to the approval of the shareholders of the Company at the forthcoming annual general meeting.



CHAIRMAN'S STATEMENT

BUSINESS REVIEW

In 2006, the Group's performance was satisfactory. The Group's operation scale has increased significantly and shown a great potential in future growth. During the year, the Group has increased its production scale and increased its market share. The performance of the core products like tartaric acid and malic acid, was good which helped to promote the steady growth of the Group. Through the strategic acquisitions, the Group gradually increases its business scope and created more business opportunities for the Group to achieve a healthy development.

(I) Market development

In 2006, the Group has actively explored new markets and new application areas of the products, enlarged its customer base to increase its sales revenue. Apart from the increase in orders from the existing customers, the excellent performance of its sales agents in the United States and Australia, etc. also brought satisfactory return and helped the Group to increase its market share.

The Group continued to strengthen its marketing work in the United States to enhance its market position in that market. In 2006, the Group's L(+)-tartaric acid obtained the Food and Drug Administration (FDA) certificate and the Hazard Analysis Critical Control Point (HACCP) certificate. It is also recognised as a 江蘇省名牌產品 (Jiangsu Province Top Brand). These certificates and awards established a high quality brand name for the Group and increased customer confidence.

In the second half of 2006, the market share of L(+) - tartaric acid in the United States and Asia further increases, which offsets the impact of the anti-dumping import tax imposed by the European Commission in early 2006. As a result, the turnover of tartaric acid has



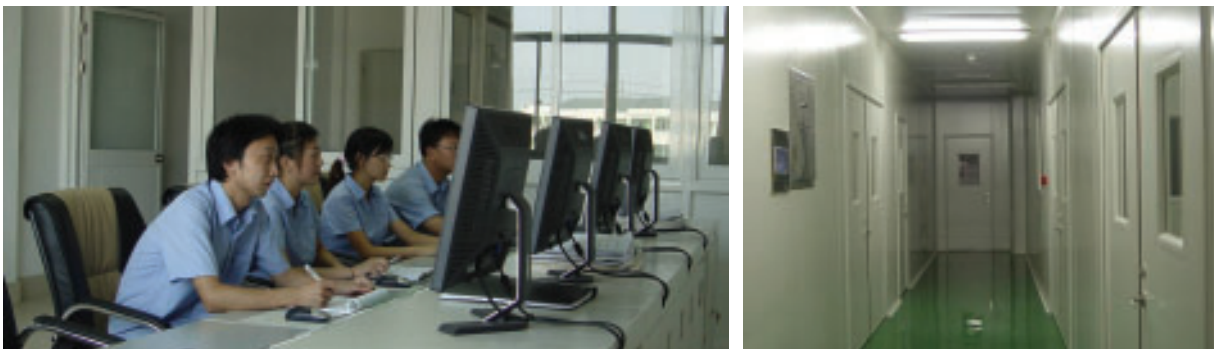
CHAIRMAN'S STATEMENT

increased by 1.5% as compared to last year. As the food additive industry is becoming increasingly prosperous, the tartaric acid market will grow steadily. In addition, the Group has made advertisements in internationally well known magazines for four consecutive years. This strategy increased the Group's brand awareness and customers' recognition on the Group's products.

(II) New construction projects

In 2006, the construction projects of the second phase production premises progressed as planned and gradually completed. This is the heaviest construction work in recent years and also an important milestone to the development of the Group. The original production lines were fully utilised. As such, based on the market conditions, the Group will increase the production capacity of its core products, tartaric acid and malic acid. The construction work for various production lines and the environmental protection facilities has been completed at the end of the year. There are great improvements in the design, construction, environment protection, product quality control and cost control of the new production lines. They will start production gradually in 2007 according to the Group's plan.

Since approximately 57% of the Group's products are exported to overseas (including sales through import-export agents in the PRC), the product quality has to attain international standard. The production lines in the second phase production premises were constructed according to the Good Manufacturing Practice (GMP) standards. The GMP production lines of aspartame and medicinal intermediaries are in use now. The aspartame GMP production line has been assessed by Moody International Certificate Ltd. for complying the cGMP110



CHAIRMAN'S STATEMENT

(GMP in manufacturing, packing or holding human food) and cGMP211 (GMP for finished pharmaceuticals) of the United States. The tartaric acid and malic acid GMP production lines will commence operation soon. The construction of the second phase production premises will be completed in 2007 and it will bring handsome return to the Company in the coming two years with a high growth rate.

(III) New products

There was a breakthrough in the progress of aspartame at the end of 2006. Its quality indicators complied with the requirements of the Japanese partner. Although this product has not yet created high economy benefits to the Group in the year, it has a great potential in the future. As there were further progress on the collaboration and the further exploration in the market, it is expected that this production line will make contribution to the Group's return in the coming two years. It will be a new growth element and is expected to bring satisfactory return to the Group.

In 2006, through the efforts of the Company and another Japanese collaborator, the progress on the development and production of various medicinal intermediary products was satisfactory. Each product has a stable customer base. In 2007, both parties will continue to bring in their respective skills and resources to deal with the challenges, to speed up the progress and to lay a good foundation for further collaboration in the future. As the demand on healthy food products increases, the market of medicinal intermediary products will be very optimistic. The project on medicinal intermediary will enhance the growth potential of the Group and create more economical benefits to the Group.



CHAIRMAN'S STATEMENT

(IV) Acquisitions

1. *Acquisition of an associate – 常州蘭陵製葯有限公司 (Changzhou Lanling Pharmaceutical Production Co., Ltd. or “Lanling Pharm”)*

The Group has acquired 42% equity interest in Lanling Pharm in the fourth quarter of 2006. After the acquisition, Lanling Pharm's management was reorganised and the operation is gradually improving and is currently stable. It is believed that Lanling Pharm will bring economical benefit to the Group in the future. The acquisition of Lanling Pharm is important to the Group's future development because it adds new aspects to the product mix of the Group. Most of the Group's products are chiral organic acids. Apart from their wide applications in food additives, they also have wide applications in chiral pharmaceuticals and chiral intermediaries. The Group is selling chiral intermediaries and these products have made contribution to the Group's returns. The acquisition of Lanling Pharm benefits the Group by extending the Group's production chain and provides a platform for the Group to extend its business into the bio-medicine industry which may increase the Group's earning ability.

2. *Acquisition of a subsidiary – 上海醫學生命科學研究中心有限公司 (Shanghai Medical Life Science Research Centre Limited or “Shanghai Life Science”)*

In addition to its own research centre, the chirotechnology centre, the Group will acquire 78% equity interest in Shanghai Life Science, with an aim to increase its ability on research and creativity and to form a foundation for entering into the bio-medicine industry. The acquisition is still in progress and expected to be completed in 2007. Shanghai Life Science is a research centre under Fudan University in Shanghai.





CHAIRMAN'S STATEMENT

It has more than ten doctors and is strong in research. It processes various patented products and has a high market potential.

3. *Setting up of a wholly owned subsidiary –上海常茂生物化學工程有限公司(Shanghai Changmao Biochemical Engineering Company Limited or “Shanghai Changmao”)*
Shanghai Changmao will be a window of the Group for its international development. It will adopt an advanced management style, attract capable research staff and products with high value to enhance the Group's product mix and sales network, and to promote further growth of the Group.

(V) Management

In addition to the ISO9001 Quality System Standards, the Group has attained the HACCP Standards in 2006. By complying with these standards, the Group monitors its production management and product quality to increase the competitiveness of its products. In addition, the Group has designed four GMP production lines and adopted GMP standards in managing production. The Group endeavours to have good quality control and process management so that the production process is up to the international standard.

In addition, the Group has committed to enhance its financial system, organisation structure and management system as a good foundation for the Group's future development, to provide quality services to the customers, to increase the Group's brand awareness and to create value for the shareholders.



CHAIRMAN'S STATEMENT

PROSPECT AND OUTLOOK

Looking into 2007, the economy of China will continue to grow rapidly. The Group will take the opportunities brought by the growth in economy and will also commit to deal with challenges brought by the market competitions.

The Group will continue the production of food additives as its core business and to increase its operating scale. The Group will make use of its cost advantage and continue to seek opportunities to explore new markets and new product application and to increase growth in business. The Group will also further explore opportunities in functional food products and medicinal intermediary productions, further strengthen the collaborations and create new growth area.

People are more health conscious nowadays and this drives the development of the biomedicine market. The Group has an advantage of having two research centres, the chirotechnology centre and Shanghai Life Science. The Group will integrate its resources on research, insist on technology innovation and extend its production chain by exploring the market of medicinal products and bio-nutrition products which is of high market potential and profitability. The Group will make use of its brand awareness and its international sales system to commercialise its new products, to promote the Group's development in business and profitability, to create best interest for the shareholders and also to make contributions to public health.

The Board and I are confident of the future of the Group. The Group's success is attributable to the support of the shareholders and the employees. Finally, on behalf of the Board, I would like to express my thanks to the fellow members of the Board, the employees of the Group, all customers and suppliers of the Group. Besides, I also extend my sincere gratitude to all the shareholders of the Company for their continuing support to the Group.

Rui Xin Sheng
Chairman

The PRC, 16 March 2007



MANAGEMENT DISCUSSION AND ANALYSIS

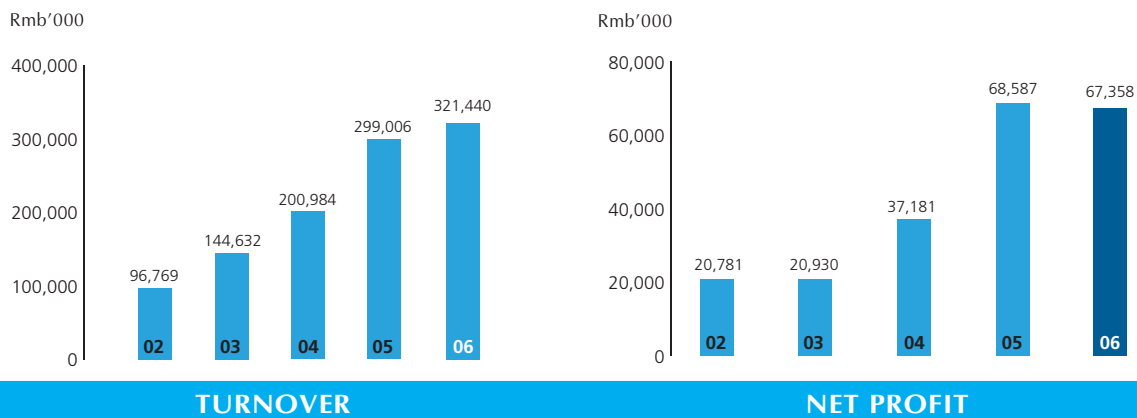
FINANCIAL REVIEW

Turnover

The Group recorded a turnover of approximately Rmb321,440,000 for the year ended 31 December 2006, representing an approximately 7.5% increase compared to that of the year ended 31 December 2005. The turnover in 2006 was mainly generated from the selling of existing products, of which the production facilities had already reached their maximum capacity. Sales of existing products in 2006 remain stable. Despite the impact of the anti-dumping import tax in Europe in the first half year, the sales of tartaric acid for the year increased by 1.5% due to the increase in market shares in the United States and Australia as a result of the Group's successful marketing strategy. The increase in turnover in 2006 mainly came from the increase in sales of maleic anhydride. The Group completed the construction of the second set of fumaric acid (including maleic anhydride) production line in mid 2005, which made a full year contribution to the sales in 2006. The maleic anhydride produced can be used as raw materials for the Group's downstream products such as malic acid and tartaric acid. The maleic anhydride produced by this production line was more than enough as raw materials for the downstream products. The surplus maleic anhydride was sold in the market. Sales of maleic anhydride reached Rmb56 million (2005: Rmb36 million) in 2006.

Gross profit margin

The gross profit margin for the year ended 31 December 2006 was approximately 32.4% as compared to that of 36.3% recorded for 2005. The decrease in overall gross profit margin was mainly due to the decrease in profit margin of the upstream products such as maleic anhydride. The Group expected that the sales of maleic anhydride to the market would gradually decrease as more maleic anhydride will be used as raw materials for downstream products such as L(+)-



MANAGEMENT DISCUSSION AND ANALYSIS

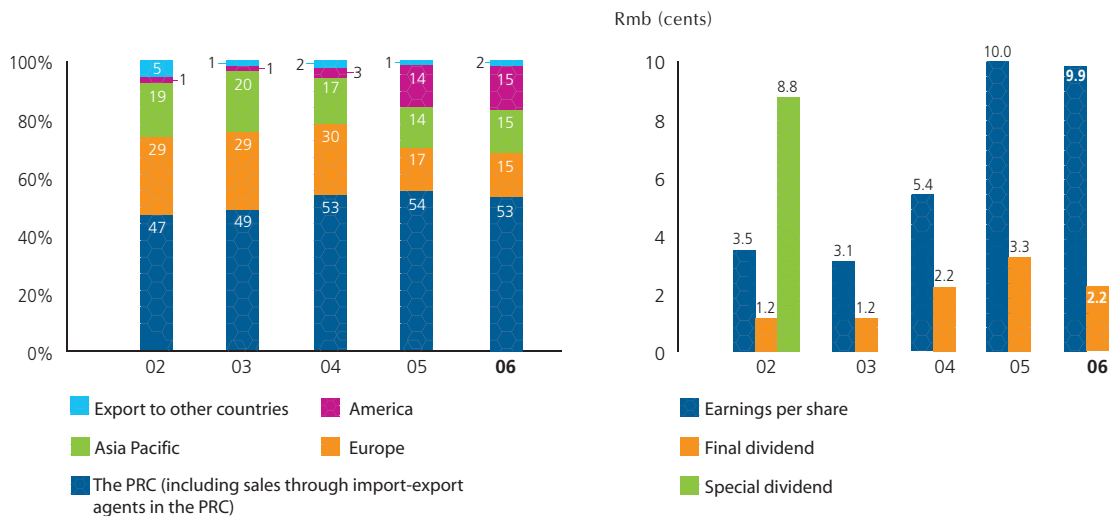
tartaric acid and malic acid upon the expansion of the production lines for these downstream products in 2007.

Expenses

Due to the continuous growth of business and production volume, the Group has recruited new staff, increased scale of the Group’s research and development, and devoted more effort into marketing and promotion this year. As a result, the selling and administrative expenses for the year ended 31 December 2006 increased as compared to last year.

Taxation

The Company, being located in the New Technology Industrial Development Experimental Zone in Changzhou and registered as a New and High Technology Enterprise is not subject to any local income tax. The Company obtained a 技術密集型知識密集型企業證書(The Certificate of Technology-intensive and Knowledge-intensive Enterprise), under which the Company was entitled to a reduced income tax rate of 15% for three financial years ending 31 December 2007. The subsidiary of the Group in Mainland China does not have assessable profit during the year. During the year, the Company has obtained approval from the tax bureau whereby it is granted a tax credit of approximately Rmb4,021,000 in respect of the purchase of certain equipments manufactured in Mainland China.





MANAGEMENT DISCUSSION AND ANALYSIS

SEGMENTAL INFORMATION

Most of the Group's products are exported to Western Europe, Australia, the United States and Japan. The turnover in 2006 increased by approximately 7.5% as compared to that of 2005. Export sales (including sales through import-export agents in the PRC) increased by approximately 1.4% as compared to that of last year while domestic sales increased by approximately 17.1% as compared to last year.

In terms of percentage, export sales (including sales through import-export agents in the PRC) accounted for approximately 57% (2005: 61%) of the Group's turnover while domestic sales in the PRC accounted for approximately 43% (2005: 39%) of turnover. The Group had increased its production capacity of fumaric acid (including maleic anhydride) to 20,000 tonnes per year in mid 2005. Maleic anhydride is produced for using as raw material for the Group's downstream products. There was excess maleic anhydride produced and was sold in the domestic market, which increased the proportion of the Group's domestic sales.

EXPOSURE TO FLUCTUATIONS IN EXCHANGE RATES AND RELATED HEDGES

The Group mainly operates in the PRC. Substantially all of its assets, liabilities and capital expenditure were located or incurred in Mainland China. Sales are made to customers in the PRC as well as overseas customers while purchases are mainly from suppliers in the PRC. The Group is therefore exposed to foreign exchange risk arising from various currency exposures, primarily with respect to United States Dollars and Euro. The Group has not used any significant forward contracts, currency borrowings or other means to hedge its foreign currency exposure. The depreciation or appreciation of foreign currencies against Renminbi will affect the Group's results of operations.

LIQUIDITY AND FINANCIAL RESOURCES

As at 31 December 2006, the Group had total outstanding unsecured bank borrowings of Rmb159 million (2005: Rmb38 million), all of which were repayable within one year (2005: Rmb29 million were repayable within one year and Rmb9 million were repayable in the second year). The average effective interest rate of all the outstanding bank loans is approximately 5.8% (2005: 5.6%) per annum.

MANAGEMENT DISCUSSION AND ANALYSIS

Except for the bank borrowings disclosed above, as at 31 December 2006 and 2005, the Group did not have any committed borrowing facilities.

As at 31 December 2006, the Group had capital commitments for property, plant and equipment amounting to approximately Rmb7 million. These capital commitments are mainly related to the expansion of production lines for the existing products or establishment of new production lines for the Group's proposed new products in 2007. The Group intends to finance the capital commitments by cash flows generated from the Group's operations and/or bank financings.

The Group did not have any charge on its assets during the year ended 31 December 2006. The gearing ratio (calculated based on total liabilities divided by total assets) was 37% (2005: 19%) as at 31 December 2006. As at 31 December 2006, the Group's bank balances and cash amounted to Rmb58,448,000 (2005: Rmb29,526,000). The Directors believe that the Group is in a healthy financial position.

CAPITAL STRUCTURE OF THE COMPANY

The H shares of the Company ("H Shares") were listed on the GEM on 28 June 2002. There has been no change in the capital structure of the Company since that date.

The Group generally finances its operations with equity fundings and bank borrowings. Excess cash held by the Group is generally placed at banks to earn interest income.

EMPLOYEES

Including the Directors, as at 31 December 2006, the Group employed a total of 395 employees (2005: 325 employees). Employees are remunerated in accordance with the nature of the job and also on individual merit. Total amount of staff costs for the year ended 31 December 2006 was approximately Rmb22,091,000 (2005: Rmb 20,081,000). The increase in staff cost was mainly due to the increase in number of employees and salary increment. An incentive bonus amounting to approximately Rmb4,703,000 (2005: Rmb4,916,000) was given to the staff for the year ended 31 December 2006. Under the staff incentive scheme for each of the three years ending 31 December 2007, so long as the audited profits (or, where applicable, combined or consolidated



MANAGEMENT DISCUSSION AND ANALYSIS

profits) attributable to the shareholders (after taxation and minority interest (if any) but before extraordinary and exceptional items and payment of the bonuses referred to below) amount to not less than Rmb40 million (the “Target Profit”):

- (a) a sum equivalent to 5% of the amount in excess of the Target Profit will be payable to Mr. Rui Xin Sheng as a bonus for the relevant year;
- (b) a sum equivalent to 5% of the amount in excess of the Target Profit will be payable to all the directors (other than Mr. Rui Xin Sheng and the independent non-executive directors) for the time being of the Company as a bonus for the relevant year; and
- (c) a sum equivalent to 5% of the amount in excess of the Target Profit will be payable as bonus to all the employees (including supervisors, but excluding the directors and the independent supervisors) of the Company and its subsidiaries (if any) from time to time, the basis of apportionment of which will be determined by the Board at its discretion.

SIGNIFICANT INVESTMENTS

There is no significant investments held by the Group as at 31 December 2006 and 2005.

CHANGES IN THE COMPOSITION OF THE GROUP DURING THE YEAR

The Company has set up a wholly-owned subsidiary, 上海常茂生物化學工程有限公司 (Shanghai Changmao Biochemical Engineering Co., Ltd.) in Shanghai with a registered capital of Rmb20 million in July 2006.

The Company has entered into an agreement in August 2006 for the acquisition of 42% interest in 常州蘭陵製葯有限公司 (Changzhou Lanling Pharmaceutical Production Co., Ltd. or “Lanling Pharm”), a limited liability company incorporated in the PRC principally engaged in the manufacture and sales of pharmaceutical products. The registered capital of Lanling Pharm is Rmb10 million. The amount of investment by the Company is Rmb4.2 million.

Save as disclosed above, there is no acquisitions and disposals of subsidiaries and affiliated companies by the Group during the year ended 31 December 2006.

CONTINGENT LIABILITIES

As at 31 December 2006 and 2005, the Group did not have any material contingent liabilities.

*PROFILE OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT***DIRECTORS****Executive Directors**

Mr. Rui Xin Sheng (芮新生), aged 50, is the Chairman of the Board, the general manager and the compliance officer of the Company. He is a researcher and a senior engineer of the Company. He was one of the founders of the Company. Mr. Rui graduated from 江蘇石油化工學院 (Jiangsu Institute of Petrochemical Technology) (“JSIPT”) with a bachelor degree in organic synthesis in 1982. He obtained an executive master of business administration in Nanjing University in 2005. He is the vice chairman of the Committee of Biochemical Engineering of the Chemical Industry and Engineering Society of China, the deputy managing director of 中國生物化工協會 (The Association of Biochemistry of China), the deputy managing director of Jiangsu Commission of Biotechnology and a part-time professor at Nanjing University of Technology. Owing to his significant achievement in the field of biochemistry, Mr. Rui received numerous awards including 常州市技術改造一等獎 (The First Class Award of Scientific Development and Technology Improvement in Changzhou) and 常州市科技進步二等獎 (The Second Prize of Changzhou City Scientific and Technological Achievement) in 1997. The concurrent production technology for the production of fumaric acid and malic acid (the “Concurrent Production Technology”) invented by Mr. Rui, Ms. Leng Yi Xin and Mr. Jiang Jun Jie obtained patent in 1998. Other awards obtained by Mr. Rui include 常州市第四屆傑出科技人員 (The Fourth Annual Excellent Scientists of Changzhou City) in 1999, DuPont Innovation Award and 江蘇省有突出貢獻的中青年專家 (Youth Expert with Excellent Contribution in Jiangsu Province) in 2000, 國家科技進步一等獎 (The First Class Award of State Technological Achievement) in 2001, 江蘇省創新創業人材獎 (Innovative Entrepreneur of Jiangsu Province), 中國石油化學工業行業科技進步二等獎 (The Second Class Award of Oil Chemical Industry Technological Achievement in the PRC) in 2003 and 江蘇省科學技術進步一等獎 (The First Class Award of Jiangsu Province Technological Achievement) in 2005. He is currently a director and a board committee member of 常州曙光化工廠 (Changzhou Shuguang Chemical Factory or “Shuguang Factory”).

Mr. Jiang Jun Jie (蔣俊杰), aged 40, is an executive Director and deputy general manager of the Company. He is a senior engineer of the Company and is responsible for the overall technology, product research and development of the Company. Mr. Jiang graduated from JSIPT in 1987 with a bachelor degree. He possesses over 20 years of working experience in the research and development of technology in the field of chemistry. Mr. Jiang is one of the inventors of the Concurrent Production Technology. Mr. Jiang published various theses. Mr. Jiang is a 中青年專家 (recognised youth expert) in Changzhou City in 2000 and obtained 江蘇省科學技術進步一等獎 (The First Class Award of Jiangsu Province Technological Achievement) in 2005. He is currently a director and a board committee member of Shuguang Factory. Mr. Jiang joined the Company in January 1993.

PROFILE OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

DIRECTORS (Continued)

Non-executive Directors

Mr. Zeng Xian Biao (曾憲彪), aged 64, is a non-executive Director. Mr. Zeng graduated from 南京石油工業學校 (Nanjing Petrochemistry School) in 1961. He has extensive experience engaging in research, development and production management in the field of chemistry. Mr. Zeng received various awards including 順酐2000t/a 技改省金牛獎 (The Golden Prize of Technological Improvement-Maleic Anhydride 2000t/a) from the State Economic Commission, 市化工系統十佳科技人員 (the best ten chemists in Changzhou), 3000t/a 順酐重點技改先進個人 (Maleic Anhydride 3000t/a Technology Improvement), 市九五跨世紀奉獻獎 (Changzhou Contribution Award for the Ninth Five-year Period and the Millennium) and 省第二次合理化建議科技成果獎 (The Second Annual State and City Award for Technological Development). He is currently a director and a board committee member of Shuguang Factory. Mr. Zeng joined the Company in December 1992.

Mr. Yu Xiao Ping (虞小平), aged 51, is a non-executive Director. Mr. Yu graduated from East China Normal University with a bachelor degree in English in 1977. He holds director positions in various pharmaceutical and investment companies in the PRC. Besides his experience in trading of pharmaceutical products, he has experience in promoting and facilitating the inspection and approval from the FDA for various PRC pharmaceutical products, of which he became the executive agent for these pharmaceutical products and has established a trading business in the United States. Mr. Yu joined the Company in December 1992.

Mr. Lu Chong Zhu (呂崇竹), aged 64, is a non-executive Director. He graduated with a bachelor degree in electronic system and communication from Southeast University. Mr. Lu is currently a director, a senior engineer of professor level and the general manager of Shanghai Technology Investment. Mr. Lu has over 22 years working experience in the electronic industrial department of the 14th Research Institute and has been an assistant supervisor of the research department. He has over 10 years working experience in the electronic industrial department of the 50th Research Institute, and was the director of the 50th Research Institute. Mr. Lu has received various awards of national and ministry level such as 國防科工委科技進步一等獎 (The First Class Award of Technological Improvement from the State Defense Department), 電子部科技成果一等獎 (The First Class Award of Electronic Technological Achievement) and several others awards of national and departmental level. In 1990 and 1992, he was recognised as 電子部優秀領導幹部 (The Excellent Leaders of the Electronics Department) and 電子部突出貢獻專家 (The Outstanding and Contributory Experts to the Electronic Department). Mr. Lu joined the Company in June 2001.

*PROFILE OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT***DIRECTORS** (Continued)**Non-executive Directors** (Continued)

Ms. Leng Yi Xin (冷一欣), aged 45, is a non-executive Director. She graduated from the Organic Chemistry Department of JSIPT with a bachelor degree in 1982 and subsequently obtained a master degree in chemical engineering from Nanjing University of Technology in 1996 and obtained a doctorate in 2006. She is also a professor of the chemical engineering department of Jiangsu Polytechnic University. Ms. Leng has participated in various research projects and published more than 20 theses. As mentioned above, Ms. Leng is one of the inventors of the Concurrent Production Technology. Ms. Leng participated in a project relating to the synthesis of chlorinated rubber by solvent method in the PRC and such project was awarded 江蘇省科學技術三等獎 (The Third Class Award of Jiangsu Technological Achievement) and 常州市科學進步三等獎 (The Third Class Award of Changzhou City Technological Achievement) in 1999 and 1998 respectively. She obtained 技術發明二等獎 (The Second Class Award of Technological Invention) from China Petroleum and Chemical Industry Association in 2004. She also obtained 江蘇省科學技術進步一等獎 (The First Class Award of Jiangsu Province Technological Achievement) in 2005. She is the wife of Mr. Rui. She joined the Company in June 2001.

Independent Non-executive Directors

Prof. Ouyang Ping Kai (歐陽平凱), aged 61, is an independent non-executive Director. He graduated from Tsinghua University with a bachelor degree in 1968 and subsequently obtained a master degree in Chemistry Research from the same university in 1981. From 1985 to 1987, he was a visiting scholar of the University of Waterloo, Ontario, Canada. Prof. Ouyang is an academician of the Chinese Academy of Engineering and the President of Nanjing University of Technology and instructed dozens of master students. He also holds memberships and positions in various science and academic institutions. Prof. Ouyang obtained various awards including 國家科技進步一等獎 (The First Prize of the State Technological Achievement) in 2001, 科技進步獎 (Technology Achievement Award) from the Ho Leung Ho Lee Foundation, Dupont Innovation Award and several other awards of national level. Prof. Ouyang published more than 180 theses and two publications. Prof. Ouyang was appointed as an independent non-executive Director in June 2001.

Prof. Yang Sheng Li (楊勝利), aged 66, is an independent non-executive Director. Prof. Yang is a professor of Shanghai Research Center of Biotechnology Chinese Academy of Science. In 1997, he became the academician of the Chinese Academy of Engineering. Prof. Yang has long been engaging in research relating to genetic function and structure and genetic engineering. He instructed dozens of master students and doctorate students and published more than 80 theses. Prof. Yang received 科技進步一等獎 (The First Class Award of Technological Achievement) from the Science Institute of the PRC in 1988, 第二屆德利達科技獎 (The Second Prize of Yilide Technology) from the Science Institute of the PRC in 1989, and 先進工作者一等獎 (The First Prize of Innovative Worker) from the Committee of the State Defense Department. Prof. Yang was appointed as an independent non-executive Director in June 2001.

Ms. Wei Xin (衛新), aged 39, is an independent non-executive Director. Ms. Wei is a Certified Public Accountant in the PRC. She graduated from Soochow University in accountancy in 1989. She has over fifteen years of experience in auditing and accounting. Ms. Wei is currently the partner of a Certified Public Accounting firm in the PRC. Ms. Wei was appointed as an independent non-executive Director in September 2004.

PROFILE OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

SUPERVISORS

Supervisors Nominated by Shareholders

Ms. Zhou Rui Juan (周瑞娟), aged 52, is the chairman of the Company's supervisory board and the director of the administration department of the Company. She graduated from Changzhou Light Industrial School specialising in corporate management in 1988. Ms. Zhou passed the State Examination for Assistant Accountant in 1997. She was a financial accountant and the vice chairman of the labour department of the Company. Ms. Zhou was recognised as an activist of the Labour Union and an advanced worker. Ms. Zhou currently is a supervisor of Shugang Factory. She joined the Company in January 1993.

Mr. Lu He Xing (陸和興), aged 62, is a supervisor of the Company (the "Supervisor"). Mr. Lu is recognised as an advanced manufacturer of the Bureau of Chemical Industry, a model worker of Changzhou and Jiangsu and one of the Ten Best Leaders from Changzhou City of Chemical Commission. Mr. Lu is currently the vice secretary of the Party Committee and the chairman of board of supervisors of Shuguang Factory. Mr. Lu joined the Company in December 1992.

Supervisor Nominated by Employees

Mr. Pan Chun (潘春), aged 37, is a Supervisor and a vice director of the production and technology department of the Company. He obtained a bachelor degree in applied chemistry from Nanjing University of Technology in 1993. Mr. Pan is responsible for the management of the Chirotechnology Centre, the research and development of new products, and the management of product quality. Mr. Pan received 常州市技術改進一等獎 (The First Class Award of Changzhou Technological Achievement) in 1997. Mr. Pan joined the Company in August 1993.

Independent Supervisors Nominated by Shareholders

Professor Gu Jian Xin (顧建新), aged 49, graduated from JSIPT with a bachelor degree in 1982 and subsequently obtained a doctorate degree from Nagoya University, Japan in 1989. Prof. Gu continued his post-doctorate research at Osaka University in Japan. He has been a professor and tutor of doctorate students in Shanghai Medical University. Prof. Gu currently presides several local and foreign research projects mainly for the control of the glycosyltransferase gene expression and the functions of new type neural growth factor. Prof. Gu published over a dozen of theses and was awarded 上海市科技進步三等獎 (The Third Prize of Shanghai Scientific Technology Progress) in 1995 and 上海市曙光學者 (Shanghai Shuguang Scholar) in 1996. He was recognised as 上海市優秀科學帶頭人 (Shanghai Excellent Scientific Leader) in 1999 and obtained a special allowance from the government of Shanghai for his research in β -1, 4-galactosyl-transferase in 1998. Prof. Gu was appointed as an independent Supervisor in June 2001.

PROFILE OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

SUPERVISORS (Continued)

Independent Supervisors Nominated by Shareholders (Continued)

Prof. Jiang Yao Zhong (蔣耀忠), aged 70, graduated from the Chemistry department of Peking University in 1957. He has been the vice president of the 中國科學院成都分院 (Chengdu branch of the Chinese Academy of Sciences) during 1990 to 1994. He was also the president of 中國科學院成都有機化學研究所 (Chengdu Institute of Organic Chemistry, the Chinese Academy of Sciences) during 1992 to 1997 and the scientific consultant of the Government of Sichuan from 1988 to 1998. He is a researcher and an instructor of doctorate students. He is a committee member of 中國化學會 (Chemistry Society of China), a deputy director of 有機化學委員會 (Committee of the Organic Chemistry), and a foreign member of the American Chemical Society. Prof. Jiang was recognised as the 四川省學術和技術帶頭人 (Leader of Academy and Technology in Sichuan) in 1998 and awarded with 中國化學會有機合成創造獎 (Prize of Creation in Organic Synthesis by the Chemistry Society of China) in 2000. Prof. Jiang was appointed as an independent Supervisor in June 2004.

SENIOR MANAGEMENT

Ms. Zhou Rui Juan (周瑞娟), whose personal particulars are set out under the paragraph headed "Supervisors" in this section.

Mr. Pan Chun (潘春), whose personal particulars are set out under the paragraph headed "Supervisors" in this section.

Ms. Wan, Pui Ling Alice (溫珮玲), aged 35, is the financial controller, qualified accountant and company secretary of the Company. She has over ten years of experience in auditing, accounting and financial management in Hong Kong and the PRC. Ms. Wan holds a bachelor degree and a master of science degree from the Chinese University of Hong Kong, and is an associate member of the Hong Kong Institute of Certified Public Accountants. Ms. Wan joined the Company in June 2001.

Mr. Wan Yi Dong (萬屹東), aged 33, is the deputy director of the chiral technology centre and the production manager of the chiral medicinal production line. Mr. Wan is a professional engineer. He graduated from Zhejiang University in 1996 with a bachelor degree in biochemistry. In 2004, he obtained a master degree in business administration from Nanjing University of Science and Technology. He joined the Company in August 1996. He was engaged in the technology advancement of bio-enzyme and immobilized enzyme technology and has been involved in various projects of the Company in respect of improvement in production technology and new technology on new products. Mr. Wan has published various professional articles in professional chemical magazines. He obtained various awards including the 常州市科技進步一等獎 (The First Class Award of Changzhou City Technological Achievement) in 2001 and 中國石油和化學工業協會科技進步二等獎 (The Second Class Award of Oil Chemical Industry Technological Achievement in the PRC) in 2003.



PROFILE OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

SENIOR MANAGEMENT (Continued)

Mr. Lu A Xing (陸阿興), aged 38, is a manager of the sales and marketing department of the Company. He obtained a diploma from Changzhou Chemical Worker's School in 1988 and continues his studies at Changzhou Party School. Mr. Lu has over 15 years' experience in sales and marketing. Mr. Lu joined the Company in January 1993.

Ms. Chang Yu Hong (常育紅), aged 33, is a manager of the business development department of the Company. She graduated from Beijing Institute of Clothing Technology with a bachelor degree in fine chemistry in 1997. Ms. Chang joined the Company in July 1997.

Save as disclosed above, each of the Directors or Supervisors does not have any relationship with any directors, senior management, management shareholders, substantial shareholders, or controlling shareholders of the Company (within the meaning of the GEM Listing Rules).

CORPORATE GOVERNANCE

The Company is committed to maintaining a high standard of corporate governance. Save as disclosed in the paragraph headed “Chairman and general manager (chief executive officer)” below, the Company has complied with the code provisions of the Code on Corporate Governance Practices as set out by the Stock Exchange in Appendix 15 to the GEM Listing Rules during the year ended 31 December 2006.

The Company’s corporate governance structure includes the board of directors and the supervisory committee. The Company has also established two committees under the Board, namely the remuneration committee and the audit committee. The corporate governance practices adopted by the Company are as follows:

THE BOARD

The major responsibilities of the Board include the formation of the Group’s overall strategies, setting business plans and the supervision of the performance of the management. The Directors acknowledge their responsibility for preparing the financial statements on a going concern basis, with supporting assumptions or qualifications as necessary. The Board is also responsible for preparing a balanced, clear and understandable assessment of annual, interim and quarterly reports, price-sensitive announcements and other disclosures required under the GEM Listing Rules and other statutory requirements.

The Board comprises two executive Directors, namely, Mr. Rui Xin Sheng and Mr. Jiang Jun Jie, four non-executive Directors, namely, Mr. Zeng Xian Biao, Mr. Yu Xiao Ping, Mr. Lu Chong Zhu and Ms. Leng Yi Xin and three independent non-executive Directors, namely, Prof. Ouyang Ping Kai, Prof. Yang Sheng Li and Ms. Wei Xin.



CORPORATE GOVERNANCE

The Board meets regularly, and had met four times for the year ended 31 December 2006. Attendance of individual members of the Board meeting for the year ended 31 December 2006 is as follows:

	Name of Director	Attended/ Eligible to attend
Chairman	Rui Xin Sheng	4/4
Executive Director	Jiang Jun Jie	4/4
Non-executive Directors	Zeng Xian Biao	4/4
	Yu Xiao Ping	0/4
	Lu Chong Zhu	4/4
	Leng Yi Xin	4/4
Independent Non-executive Directors	Ouyang Ping Kai	1/4
	Yang Sheng Li	1/4
	Wei Xin	4/4

Save that Ms. Leng Yi Xin is the wife of Mr. Rui Xin Sheng, each of the Directors is independent of other Directors.

Chairman and general manger (chief executive officer)

Code provision A.2.1 of Appendix 15 to the GEM Listing Rules stipulates that the roles of chairman and chief executive officer should be separate and should not be performed by the same individual. The division of responsibilities between the chairman and chief executive officer should be clearly established and set out in writing. Mr. Rui Xin Sheng, the chairman of the Board, also acts as the general manager (chief executive officer) of the Company. Since Mr. Rui Xin Sheng is well aware of the Group's business and operation, the Company considers that it is in the best interest of the Company for Mr. Rui Xin Sheng to act as the general manager of the Company.

CORPORATE GOVERNANCE

Code of Conduct Regarding Securities Transactions by Directors

The Company has adopted a code of conduct regarding securities transactions by directors on terms no less than the required standard of dealings as set out in rules 5.48 to 5.67 of the GEM Listing Rules. The Company had also made specific enquiry of all Directors and the Company was not aware of any non-compliance with the required standard of dealings and its code of conduct regarding securities transactions by Directors during the year ended 31 December 2006.

Appointment of Directors

Appointments of Directors, being individuals who are suitably qualified and expected to make positive contributions to the performance of the Board, are first considered by the existing Directors. Thereafter, all Directors are subject to election by shareholders at the shareholders' general meeting. A Director may serve consecutive terms if re-elected upon the expiration of the terms.

Each of Mr. Rui Xin Sheng and Mr. Jiang Jun Jie has entered into a service agreement with the Company. All the other Directors have not entered into any service agreement with the Company. The terms of each Director is not more than three years and will be expired on 17 June 2007.

Independent Non-executive Directors

The Company has received from each of the independent non-executive Directors an annual confirmation of his/her independence pursuant to GEM Listing Rule 5.09 and the Company still considers the independent non-executive Directors remained independent.

BOARD COMMITTEES

Remuneration Committee

The Remuneration Committee was established in March 2005 to ensure there are formal and transparent procedures for developing and overseeing the Company's policies on the remuneration of its directors and senior management. It is chaired by the Chairman, Mr. Rui Xin Sheng with three independent non-executive Directors, Prof. Ouyang Ping Kai, Prof. Yang Sheng Li and Ms. Wei Xin. The remuneration committee held one meeting in 2006 and the attendance rate was 100%.

The remunerations of Directors and senior management are based on the skill, knowledge and involvement in the Company's affair of each Director or senior management and is also determined with reference to the performance and profitability of the Company. The Company has formulated a staff incentive bonus scheme. Details of which is set out in the paragraph headed "Employees" under the section headed "Management Discussion and Analysis".



CORPORATE GOVERNANCE

Audit Committee

The Company has established an audit committee in June 2002 with written terms of reference in compliance with GEM Listing Rules. The audit committee comprises three independent non-executive Directors, namely, Prof. Ouyang Ping Kai, Prof. Yang Sheng Li and Ms. Wei Xin.

The primary duties of the audit committee are to review and to provide supervision over the financial reporting process and internal control system of the Group, to review the Group's financial information and to review the audit plan, audit findings and independence of the Auditors of the Company. The Audit Committee held four meetings for the year ended 31 December 2006 with attendance rate of 100%.

The audit committee has reviewed with management the accounting principles and practices adopted by the Group and discussed financial reporting matters including to review, inter alia, the Company's quarterly, interim and annual results released during the year ended 31 December 2006 and to recommend the Board the appointment of external auditors.

THE SUPERVISORY COMMITTEE

The supervisory committee is accountable to the general meeting. The primary responsibilities of the supervisory committee include the monitoring of whether the Directors and senior management have, in the performance of their duties, acted in contravention of any laws, administrative regulations, the Articles of Association or the resolutions passed at general meetings; and the reviewing of the Company's financial information. Supervisors can attend the Board meetings.

The supervisory committee comprises two supervisors nominated by shareholders, Ms. Zhou Rui Juan and Mr. Lu He Xing, a supervisor nominated by employees, Mr. Pan Chun and two independent supervisors nominated by shareholders, Prof. Gu Jian Xin and Prof. Jiang Yao Zhong. Each of Ms. Zhou Rui Juan, Mr. Lu He Xing and Mr. Pan Chun has entered into a service agreement with the Company. Prof. Gu Jian Xin and Prof. Jiang Yao Zhong have not entered into any service agreement with the Company. The terms of each supervisor is not more than three years and will be expired on 17 June 2007.

The supervisory committee held two meetings for the year ended 31 December 2006 with attendance rate of 100%.

CORPORATE GOVERNANCE

DIRECTORS' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The Directors acknowledge their responsibility for preparing the financial statements for the year ended 31 December 2006, which give a true and fair view of the state of affairs of the Company and of the Group at that date and of the Group's profit and cash flows for the year then ended and are properly prepared on the going concern basis in accordance with the statutory requirements and applicable accounting standards.

The statement of the Auditors of the Company about their reporting responsibilities on the financial statements of the Company is set out in the Independent Auditor's Report on pages 44 and 45.

INTERNAL CONTROL AND RISK MANAGEMENT

The Board is responsible for ensuring that the Group has a sound and effective internal control system. The Group is committed to the identification, monitoring and management of risks associated with its business activities and has implemented a practical and effective control system which includes a defined management structure with limits of authority, a sound cash management system and periodic review of the Group's operation and performance by the Audit Committee and the Board. The internal control system is reviewed on an ongoing basis by the Board to ensure it is effective. The Board is satisfied that, based on information furnished to it and on its own observations, the present internal controls of the Group are satisfactory. The Board has conducted review of the effectiveness of the system of internal control and is of the view that the system of internal control adopted for the year ended 31 December 2006 is sound and effective. The Group does not have an internal audit function and the Board is of the view that there is currently no need for the Group to have this function.

AUDITORS' REMUNERATION

PricewaterhouseCoopers have been re-appointed as the Company's international external auditors by the shareholders at the 2005 annual general meeting. They are primarily responsible for providing audit services in connection with the Company's annual financial statements.

During the year, the total remuneration in respect of audit services provided by the external auditors amounted to HK\$780,000 (approximately equivalent to Rmb784,000).



REPORT OF THE DIRECTORS

The Directors have pleasure in submitting their report together with the audited consolidated financial statements for the year ended 31 December 2006.

PRINCIPAL ACTIVITIES AND GEOGRAPHICAL ANALYSIS OF OPERATIONS

The principal activities of the Company are the production and sale of organic acids. The activity of the subsidiary is set out in note 19 to the consolidated financial statements.

An analysis of the Group's turnover for the year by geographic segments is set out in note 5 to the consolidated financial statements.

RESULTS AND APPROPRIATIONS

The results of the Group for the year are set out in the consolidated income statement on page 46.

The Directors recommend the payment of a final dividend of Rmb0.022 per share, totalling approximately Rmb15,041,000.

RESERVES

Movements in the reserves of the Group and the Company during the year are set out in note 26 to the consolidated financial statements.

PROPERTY, PLANT AND EQUIPMENT

Details of movements in property, plant and equipment of the Group and the Company are set out in note 16 to the consolidated financial statements.

SHARE CAPITAL

Details of the movements in share capital of the Company are set out in note 25 to the consolidated financial statements.

DISTRIBUTABLE RESERVES

As at 31 December 2006, the distributable reserves of the Company were approximately Rmb128,044,000 (2005: Rmb93,723,000) as reported in the statutory financial statements prepared in accordance with the PRC Generally Accepted Accounting Principles.

PRE-EMPTIVE RIGHTS

There is no provision for pre-emptive rights under the Articles of Association of the Company or the laws of the PRC, being the jurisdiction in which the Company was established, which provide the existing shareholders with pre-emptive rights to purchase new shares in any new issue of the Company according to their respective proportion of shareholding.

SUMMARY FINANCIAL INFORMATION

A summary of the published results and assets and liabilities of the Group for the last five years is set out on page 93 of the annual report.

REPORT OF THE DIRECTORS

PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES OF THE COMPANY

Neither the Company nor its subsidiary has purchased, sold or redeemed any of the Company's listed securities for the year ended 31 December 2006.

DIRECTORS AND SUPERVISORS

The Directors and Supervisors during the year were:

Executive Directors

Mr. Rui Xin Sheng
Mr. Jiang Jun Jie

Non-executive Directors

Mr. Zeng Xian Biao
Mr. Yu Xiao Ping
Mr. Lu Chong Zhu
Ms. Leng Yi Xin

Independent non-executive Directors

Prof. Ouyang Ping Kai
Prof. Yang Sheng Li
Ms. Wei Xin

Supervisors nominated by shareholders

Ms. Zhou Rui Juan
Mr. Lu He Xing

Supervisor nominated by employees

Mr. Pan Chun

Independent Supervisors nominated by shareholders

Prof. Gu Jian Xin
Prof. Jiang Yao Zhong

In accordance with Article 97, 116 and 117 of the Company's Articles of Association, Directors and Supervisors nominated by shareholders shall be elected at the shareholders' general meeting for a term of three years. Supervisor who is a representative of employees shall be elected by the employees of the Company for a term of three years. A Director or Supervisor may serve consecutive terms if re-elected upon the expiration of the terms.

REPORT OF THE DIRECTORS

DIRECTORS' AND SUPERVISORS' SERVICE CONTRACTS

Each of Mr. Rui Xin Sheng, Mr. Jiang Jun Jie, Ms. Zhou Rui Juan, Mr. Lu He Xing and Mr. Pan Chun has entered into a service agreement with the Company. All the other Directors and Supervisors have not entered into any service agreement with the Company. The terms of each of the Directors and Supervisors are not more than three years and will be expired on 17 June 2007.

Save as above, no Director or Supervisor has entered into any service contract with the Company which may not be terminated by the Company within one year without payment of compensation other than statutory compensation.

DIRECTORS' AND SUPERVISORS' INTEREST IN CONTRACTS

Apart from the Directors' and Supervisors' service contracts disclosed above, no contracts of significance in relation to the Group's business to which the Company was a party and in which a Director or a Supervisor had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

INTERESTS AND SHORT POSITIONS OF THE DIRECTORS, SUPERVISORS OR CHIEF EXECUTIVES IN THE SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS

As at 31 December 2006, the interests (including interests in shares and short positions) of the Directors, Supervisors or chief executives of the Company in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) which were notified to the Company and the Stock Exchange pursuant to: (a) Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which each of them is taken or deemed to have taken under such provisions of the SFO); or (b) which were required pursuant to section 352 of the SFO to be entered in the register referred to in that section; or (c) were required, pursuant to Rules 5.48 to 5.67 of the GEM Listing Rules relating to securities transactions by Directors, to be notified to the Company and the Stock Exchange, were as follows:

Long positions in shares:

Director	Capacity	Number of Domestic Shares	Percentage shareholding in the Domestic Shares	Number of Foreign Shares	Percentage shareholding in the Foreign Shares
Mr. Rui Xin Sheng	Interest of spouse, interest of controlled corporation, trustee (other than a bare trustee) and custodian (Note (a))	2,500,000	1.14%	135,000,000	48.04%

REPORT OF THE DIRECTORS

INTERESTS AND SHORT POSITIONS OF THE DIRECTORS, SUPERVISORS OR CHIEF EXECUTIVES IN THE SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS

(Continued)

Long positions in shares:

Director	Capacity	Number of Domestic Shares	Percentage shareholding in the Domestic Shares	Number of Foreign Shares	Percentage shareholding in the Foreign Shares
Ms. Leng Yi Xin	Interest of spouse and interest of controlled corporation (Note (b))	2,500,000	1.14%	135,000,000	48.04%
Mr. Jiang Jun Jie	(Note (c))	–	–	(Note (c))	(Note (c))
Mr. Zeng Xian Biao	(Note (d))	–	–	(Note (d))	(Note (d))
Mr. Yu Xiao Ping	Interest of spouse and interest of controlled corporation (Note (e))	–	–	66,000,000	23.49%
Prof. Ouyang Ping Kai	(Note (f))	–	–	(Note (f))	(Note (f))
Prof. Yang Sheng Li	(Note (g))	–	–	(Note (g))	(Note (g))
Supervisor					
Ms. Zhou Rui Juan	(Note (h))	–	–	(Note (h))	(Note (h))
Mr. Pan Chun	(Note (i))	–	–	(Note (i))	(Note (i))
Mr. Lu He Xing	(Note (j))	–	–	(Note (j))	(Note (j))
Prof. Gu Jian Xin	(Note (k))	–	–	(Note (k))	(Note (k))
Prof. Jiang Yao Zhong	(Note (l))	–	–	(Note (l))	(Note (l))

REPORT OF THE DIRECTORS

INTERESTS AND SHORT POSITIONS OF THE DIRECTORS, SUPERVISORS OR CHIEF EXECUTIVES IN THE SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS

(Continued)

Notes:

- (a) The 135,000,000 foreign shares of the Company (“Foreign Shares”) are held by Hong Kong Xinsheng Pioneer Investment Company Limited (“HK Xinsheng Ltd”) and the 2,500,000 domestic shares of the Company (“Domestic Shares”) are held by 常州新生生化科技開發有限公司 (“Changzhou Xinsheng”). The issued share capital in HK Xinsheng Ltd comprises 170,000 Class “A” shares of HK\$1 each and 100,000 Class “B” shares of HK\$1 each. Mr. Rui is the registered holder and beneficial owner of 96,500 Class “A” shares. He is also the registered holder of 53,000 Class “B” shares and holds such shares as trustee in respect of a discretionary trust for the group of persons who made contribution to the Company or who from time to time make contribution to the Company. Mr. Rui is the registered holder and beneficial owner of 70% of the registered capital of Changzhou Xinsheng. Ms. Leng, a Director and the spouse of Mr. Rui, is also interested in HK Xinsheng Ltd and Changzhou Xinsheng, details of which are set out in Note (b) below.
- (b) Ms. Leng is the registered holder and beneficial owner of 73,500 Class “A” shares of HK\$1 each in HK Xinsheng Ltd, which is the registered holder and beneficial owner of 135,000,000 Foreign Shares. The issued share capital in HK Xinsheng Ltd comprises 170,000 Class “A” shares of HK\$1 each and 100,000 Class “B” shares of HK\$1 each. Ms. Leng is the registered holder and beneficial owner of 30% of the registered capital of Changzhou Xinsheng, which is the registered holder and beneficial owner of 2,500,000 Domestic Shares. Mr. Rui, a Director and the spouse of Ms. Leng, is also interested in HK Xinsheng Ltd and Changzhou Xinsheng, details of which are set out in Note (a) above.
- (c) Mr. Jiang is the registered holder and beneficial owner of 600,000 shares of HK\$0.01 each in Hong Kong Bio-chemical Advanced Technology Investment Company Limited (“HK Biochem Ltd”), which is the registered holder and beneficial owner of 67,500,000 Foreign Shares. The total number of issued shares in HK Biochem Ltd is 6,750,000 shares of HK\$0.01 each. Mr. Jiang is also the registered holder and beneficial owner of 15,000 Class “B” shares of HK\$1 each in HK Xinsheng Ltd, which is the registered holder and beneficial owner of 135,000,000 Foreign Shares. The issued share capital in HK Xinsheng Ltd comprises 170,000 Class “A” shares of HK\$1 each and 100,000 Class “B” shares of HK\$1 each.
- (d) Mr. Zeng is the registered holder and beneficial owner of 380,000 shares of HK\$0.01 each in HK Biochem Ltd, which is the registered holder and beneficial owner of 67,500,000 Foreign Shares. The total number of issued shares in HK Biochem Ltd is 6,750,000 shares of HK\$0.01 each. Mr. Zeng is also the registered holder and beneficial owner of 2,000 Class “B” shares of HK\$1 each in HK Xinsheng Ltd, which is the registered holder and beneficial owner of 135,000,000 Foreign Shares. The issued share capital in HK Xinsheng Ltd comprises 170,000 Class “A” shares of HK\$1 each and 100,000 Class “B” shares of HK\$1 each.

*REPORT OF THE DIRECTORS***INTERESTS AND SHORT POSITIONS OF THE DIRECTORS, SUPERVISORS OR CHIEF EXECUTIVES IN THE SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS***(Continued)*

- (e) Mr. Yu and his wife (who is not a Director) taken together are interested in the entire issued capital of Jomo Limited which is the registered holder and beneficial owner of 66,000,000 Foreign Shares.
- (f) Prof. Ouyang is the registered holder and beneficial owner of 4,000 Class "B" shares of HK\$1 each in HK Xinsheng Ltd, which is the registered holder and beneficial owner of 135,000,000 Foreign Shares. The issued share capital in HK Xinsheng Ltd comprises 170,000 Class "A" shares of HK\$1 each and 100,000 Class "B" shares of HK\$1 each.
- (g) Prof. Yang is the registered holder and beneficial owner of 2,000 Class "B" shares of HK\$1 each in HK Xinsheng Ltd, which is the registered holder and beneficial owner of 135,000,000 Foreign Shares. The issued share capital in HK Xinsheng Ltd comprises 170,000 Class "A" shares of HK\$1 each and 100,000 Class "B" shares of HK\$1 each.
- (h) Ms. Zhou is the registered holder and beneficial owner of 220,000 shares of HK\$0.01 each in HK Biochem Ltd, which is the registered holder and beneficial owner of 67,500,000 Foreign Shares. The total number of issued shares in HK Biochem Ltd is 6,750,000 shares of HK\$0.01 each.
- (i) Mr. Pan is the registered holder and beneficial owner of 2,000 Class "B" shares of HK\$1 each in HK Xinsheng Ltd, which is the registered holder and beneficial owner of 135,000,000 Foreign Shares. The issued share capital in HK Xinsheng Ltd comprises 170,000 Class "A" shares of HK\$1 each and 100,000 Class "B" shares of HK\$1 each. He is also the registered holder and beneficial owner of 200,000 shares of HK\$0.01 each in HK Biochem Ltd, which is the registered holder and beneficial owner of 67,500,000 Foreign Shares. The total number of issued shares in HK Biochem Ltd is 6,750,000 shares of HK\$0.01 each.
- (j) Mr. Lu is the registered holder and beneficial owner of 220,000 shares of HK\$0.01 each in HK Biochem Ltd, which is the registered holder and beneficial owner of 67,500,000 Foreign Shares. The total number of issued shares in HK Biochem Ltd is 6,750,000 shares of HK\$0.01 each.
- (k) Prof. Gu is the registered holder and beneficial owner of 2,000 Class "B" shares of HK\$1 each in HK Xinsheng Ltd, which is the registered holder and beneficial owner of 135,000,000 Foreign Shares. The issued share capital in HK Xinsheng Ltd comprises 170,000 Class "A" shares of HK\$1 each and 100,000 Class "B" shares of HK\$1 each.
- (l) Prof. Jiang is the registered holder and beneficial owner of 2,000 Class "B" shares of HK\$1 each in HK Xinsheng Ltd, which is the registered holder and beneficial owner of 135,000,000 Foreign Shares. The issued share capital in HK Xinsheng Ltd comprises 170,000 Class "A" shares of HK\$1 each and 100,000 Class "B" shares of HK\$1 each.

REPORT OF THE DIRECTORS

INTERESTS AND SHORT POSITIONS OF THE DIRECTORS, SUPERVISORS OR CHIEF EXECUTIVES IN THE SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY AND ITS ASSOCIATED CORPORATIONS

(Continued)

Save as disclosed above, as at 31 December 2006, none of the Directors, Supervisors or chief executives of the Company have interests in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the SFO) (including interests in shares and short positions) which were required to notify the Company and the Stock Exchange pursuant to: (a) Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which each of them is taken or deemed to have taken under such provisions of the SFO); or (b) which were required pursuant to section 352 of the SFO to be entered in the register referred to in that section; or (c) were required, pursuant to Rules 5.48 to 5.67 of the GEM Listing Rules relating to securities transactions by Directors, to be notified to the Company and the Stock Exchange.

DIRECTORS' AND SUPERVISORS' RIGHT TO ACQUIRE SHARES OR DEBT SECURITIES

At no time during the year was the Company or its subsidiary a party to any arrangement (including share option scheme) to enable the Directors or Supervisors or any of their spouses or children under eighteen years of age to acquire benefits by means of the acquisition of shares in, or debt securities (including debentures) of, the Company or any other body corporate.

PERSONS WHO HAVE AN INTEREST OR SHORT POSITION WHICH IS DISCLOSEABLE UNDER DIVISIONS 2 AND 3 OF PART XV OF THE SFO AND SUBSTANTIAL SHAREHOLDERS

So far as known to the Directors, as at 31 December 2006, the following, not being a Director, Supervisor or chief executives of the Company, have interests or short positions in the shares or underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO and required to be entered in the register maintained by the Company pursuant to section 336 of the SFO:

Long positions in shares:

Name of Shareholder	Capacity	Percentage shareholding		Percentage shareholding		Percentage shareholding	
		Number of Domestic Shares	in the Domestic Shares	Number of Foreign Shares	in the Foreign Shares	Number of H Shares	in the H Shares
常州曙光化工厂 (Changzhou Shuguang Chemical Factory)	Beneficial owner	154,000,000	70.32%	-	-	-	-
Hong Kong Xinsheng Pioneer Investment Company Limited	Beneficial owner	-	-	135,000,000	48.04%	-	-

REPORT OF THE DIRECTORS

PERSONS WHO HAVE AN INTEREST OR SHORT POSITION WHICH IS DISCLOSEABLE UNDER DIVISIONS 2 AND 3 OF PART XV OF THE SFO AND SUBSTANTIAL SHAREHOLDERS (Continued)

Long positions in shares:

Name of Shareholder	Capacity	Number of Domestic Shares	Percentage shareholding in the Domestic Shares	Number of Foreign Shares	Percentage shareholding in the Foreign Shares	Number of H Shares	Percentage shareholding in the H Shares
Hong Kong Bio-chemical Advanced Technology Investment Company Limited	Beneficial owner	–	–	67,500,000	24.02%	–	–
Union Top Development Limited	Interest of controlled corporation	–	–	67,500,000 (Note (a))	24.02%	–	–
Ms. Rakchanok Sae-lao	Interest of controlled corporation	–	–	67,500,000 (Note (b))	24.02%	–	–
Jomo Limited	Beneficial owner	–	–	66,000,000	23.49%	–	–
Ms. Lam Mau	Interest of spouse and interest of controlled corporation	–	–	66,000,000 (Note (c))	23.49%	–	–
上海科技投資股份有限公司 (Shanghai Technology Investment Company Limited)	Beneficial owner	62,500,000	28.54%	–	–	–	–
上海科技投資公司 (Shanghai Technology Investment Company)	Interest of controlled corporation	62,500,000 (Note (d))	28.54%	–	–	–	–
Chervon Investment Limited	Beneficial owner	–	–	–	–	14,668,000	7.98%
Chervon Holdings Limited	Interest of controlled corporation	–	–	–	–	14,668,000 (Note (e))	7.98%
PS Holdings Limited	Interest of controlled corporation	–	–	–	–	14,668,000 (Note (f))	7.98%
Atlantis Investment Management Ltd.	Investment Manager	–	–	–	–	17,000,000	9.25%



REPORT OF THE DIRECTORS

PERSONS WHO HAVE AN INTEREST OR SHORT POSITION WHICH IS DISCLOSEABLE UNDER DIVISIONS 2 AND 3 OF PART XV OF THE SFO AND SUBSTANTIAL SHAREHOLDERS (Continued)

Notes:

- (a) Union Top Development Limited is the beneficial owner of 37.03% of the issued share capital of Hong Kong Bio-chemical Advanced Technology Investment Company Limited, which is the registered holder and beneficial owner of 67,500,000 Foreign Shares.
- (b) Ms. Rakchanok Sae-lao is the beneficial owner of 100% of the issued share capital of Union Top Development Limited, which is the is the beneficial owner of 37.03% of the issued share capital of Hong Kong Bio-chemical Advanced Technology Investment Company Limited. Hong Kong Bio-chemical Advanced Technology Investment Company Limited is the registered holder and beneficial owner of 67,500,000 Foreign Shares.
- (c) Ms. Lam Mau and her spouse, Mr. Yu Xiao Ping (who is a Director) taken together are interested in the entire issued capital of Jomo Limited which is the registered holder and beneficial owner of 66,000,000 Foreign Shares.
- (d) Shanghai Technology Investment Company is the registered holder and beneficial owner of 49% of the issued share capital of Shanghai Technology Investment Company Limited, which is the registered holder and beneficial owner of 62,500,000 Domestic Shares.
- (e) Chervon Holdings Limited is the beneficial owner of 85% of the issued share capital of Chervon Investment Limited, which is the beneficial owner of 14,668,000 H Shares.
- (f) PS Holdings Limited is the beneficial owner of 59.99% of the issued share capital of Chervon Holdings Limited, which is the beneficial owner of 85% of the issued share capital of Chervon Investment Limited. Chervon Investments Limited is the beneficial owner of 14,668,000 H Shares.

Save as disclosed above, as at 31 December 2006, the Directors are not aware of any person, not being a Director, Supervisor or chief executives of the Company, have interests or short positions in the shares or underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO and required to be entered in the register maintained by the Company pursuant to section 336 of the SFO.

MANAGEMENT CONTRACTS

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

COMPETING BUSINESS

None of the Directors, Supervisors or management shareholders of the Company and their respective associate (as defined in the GEM Listing Rules) has an interest in a business which competes with the business of the Group.

*REPORT OF THE DIRECTORS***EMOLUMENT POLICY**

Employees are remunerated in accordance with the nature of the job and also on individual merit.

The emoluments of the Directors and Supervisors are determined by the Remuneration Committee, with reference to their respective contribution of time, effort and expertise on the Company's matters.

The Company has adopted a staff incentive bonus scheme, please refer to the paragraph headed "Employees" under the section headed "Management Discussion and Analysis" for details.

MAJOR CUSTOMERS AND SUPPLIERS

The percentage of purchases and sales for the year attributable to the Group's major suppliers and customers are as follows:

Purchases

	2006	2005
– the largest supplier	11%	20%
– five largest suppliers combined	30%	46%

Sales

	2006	2005
– the largest customer	16%	16%
– five largest customers combined	38%	34%

Save as disclosed in the paragraph "Connected Transactions" below, at no time during the year have the Directors, Supervisors, their associates or any shareholders of the Company (which to the knowledge of the Directors owns more than 5% of the Company's share capital) had any interest in these major customers and suppliers.

REPORT OF THE DIRECTORS

CONNECTED TRANSACTIONS

During the year, the Company entered into the following connected transactions with its shareholder, Shuguang Factory:

	2006 Rmb'000	2005 Rmb'000
Purchases of raw materials from Shuguang Factory (note (a))	88	3,557
Electricity charged by Shuguang Factory (note (b))	2,528	2,249
Water supply charged by Shuguang Factory (note (c))	334	303
Rental expenses to Shuguang Factory (note (d))	186	186
Transportation expenses charged by Shuguang Factory (note (e))	466	467
Processing fee charged by Shuguang Factory (note (f))	1,235	798
Sales commission charged by Shuguang Factory (note (f))	408	394

Notes:

- (a) The Company purchased maleic anhydride and crude maleic anhydride from Shuguang Factory. In accordance with a master purchase agreement dated 20 December 2004, the prices were determined by the two parties subject to that the prices of maleic anhydride should not exceed the lower of (i) the lowest price paid by any independent third party to Shuguang Factory for the maleic anhydride in the immediate preceding month; and (ii) the then prevailing market prices of maleic anhydride as reported from time to time in 中國化工市場七日訊 (China Chemical Industry Market Weekly) and that the prices of crude maleic anhydride are set at prices which are no higher than 73% of the prices of maleic anhydride for the same period of time.
- (b) The Company leases certain land and building from Shuguang Factory. Electricity is supplied to the Company by Jiangsu Changzhou Electric Power Supply Bureau through the network connected to Shuguang Factory. The monthly charges for electricity consumed is paid by the Company to Shuguang Factory by reference to the (i) total units of electricity consumed by the Company as measured by separate tariff meters; and (ii) the average tariff charged by Shuguang Factory, which is equal to the total electricity fee payable to Jiangsu Changzhou Electric Power Supply Bureau by Shuguang Factory divided by total units of electricity consumed by Shuguang Factory in the corresponding period. Jiangsu Changzhou Electric Power Supply Bureau charges Shuguang Factory tariff based on total units of electricity consumed by Shuguang Factory as shown on tariff meters installed by Jiangsu Changzhou Electric Power Supply Bureau and three different rates of tariff which are applicable in accordance with different time periods in a day.
- (c) The Company leases certain land and building from Shuguang Factory. Water is supplied by 常州市自來水公司 (Changzhou Water Supply Company) through the network connected to Shuguang Factory based on the average water fee per tonne as paid by Shuguang Factory to the Changzhou Water Supply Company.

*REPORT OF THE DIRECTORS***CONNECTED TRANSACTIONS** (Continued)

- (d) Rental expenses to Shuguang Factory includes the rental for leasing of a land use right and a building. The Company leases the land use right from Shuguang Factory for a term of 50 years at a rate of (i) in respect of the period between 20 June 2001 to 31 March 2002, Rmb5,611 per annum; and (ii) in respect of the period from 1 April 2002 to 12 June 2050, Rmb25,611 per annum. The Company leases a building from Shuguang Factory for a term of 5 years from 1 April 2002 to 31 March 2007 at an annual rental of Rmb160,000.
- (e) Transportation expenses to Shuguang Factory were based at fixed rates with reference to market price quoted from third parties.
- (f) Shuguang Factory (i) acts as the selling agent for liquid maleic anhydride of the Company; and (ii) processes the liquid form maleic anhydride of the Company into solid form maleic anhydride and then acts as the selling agent for the solid form maleic anhydride of the Company. Processing fee and sales commission to Shuguang Factory were based at fixed rates in accordance with the terms of the processing and sales agreements.

The Company had made announcements on 31 December 2004 and 18 May 2006 in respect of (i) the purchase of maleic anhydride and crude maleic anhydride from Shuguang Factory and the payment of electricity charge to Shuguang Factory and (ii) the payment of processing fee and sales commission to Shuguang Factory respectively. In the opinion of the independent non-executive Directors, the Company should continue with the agreements for these connected transactions and these connected transactions were entered into by the Company:

- (i) in the ordinary and usual course of business of the Company;
- (ii) either on normal commercial terms or; if there were not sufficient comparable transactions to judge whether they are on normal commercial terms, on terms not less favourable than terms available to and from (as the case may be) for independent third parties;
- (iii) in accordance with the relevant agreements governing the transactions; and
- (iv) on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

In accordance with rule 20.38 of the GEM Listing Rules, the Board engaged the auditors of the Company to perform certain factual finding procedures on the above connected transactions on a sample basis in accordance with Hong Kong Standard on Related Services 4400 "Engagements to Perform Agreed-Upon Procedures Regarding Financial Information" issued by the Hong Kong Institute of Certified Public Accountants. The auditors have reported their factual findings for the selected samples based on the agreed procedures to the Board.

REPORT OF THE DIRECTORS

SHARE CAPITAL STRUCTURE

As at 31 December 2006, the category of the issued shares of the Company is as follows:

	No. of Shares
H Shares (Note (a))	183,700,000
Domestic Shares (Note (b))	219,000,000
Foreign Shares (Note (c))	281,000,000
	<hr/> 683,700,000 <hr/>

Notes:

- (a) Overseas listed foreign shares in the capital of the Company, with a Rmb-denominated par value of Rmb0.10 each, which was credited as fully paid up in a currency other than Rmb and are traded in Hong Kong dollars and listed on GEM.
- (b) Ordinary shares in the capital of the Company, with a Rmb-denominated par value of Rmb0.10 each, which was credited as fully paid up in Rmb and issued to the promoters of the Company.
- (c) Ordinary shares in the capital of the Company, with a Rmb-denominated par value of Rmb0.10 each, which was credited as fully paid up in a currency other than Rmb and issued to the promoters of the Company.

Although the 到境外上市公司章程必備條款 (the Mandatory Provisions of the Articles of Association of Companies Seeking a Listing Outside the PRC) promulgated on 27 August 1994 by the Securities Commission of the State Council of the PRC and the State Commission for Restructuring the Economic System of the PRC provide for the definitions of “domestic shares”, “foreign shares” and “overseas listed foreign shares” (which definitions have been adopted in the Articles of Association of the Company), the rights attached to Foreign Shares (which are subject to certain restrictions on transfer and may become H Shares upon obtaining the requisite approvals from, among other bodies, the China Securities Regulatory Commission and the Stock Exchange) have not yet been expressly dealt with under the existing PRC laws or regulations. However, the creation by the Company and the subsistence of the Foreign Shares do not contravene any PRC laws or regulations.

REPORT OF THE DIRECTORS

SHARE CAPITAL STRUCTURE (Continued)

At present, there are no applicable PRC laws and regulations governing the rights attached to the Foreign Shares. Jingtian & Gongcheng, the legal adviser to the Company as to PRC Law, have advised the Company that until new laws or regulations are introduced in this respect, holders of Foreign Shares shall have the same rights and obligations as those of the holders of Domestic Shares (in particular, in respect of the right to attend and vote in the general meetings and class meetings and to receive notice of such meetings in the same manner applicable to holders of Domestic Shares), except that holders of Foreign Shares shall enjoy the following rights:

- (a) to receive dividends declared by the Company in foreign currencies;
- (b) in the event of the winding up of the Company, to participate in the distribution of surplus assets (if any) of the Company in foreign currencies and transfer such assets out of PRC, subject however to the applicable foreign exchange control regulations;
- (c) disputes between holders of Domestic Shares and Foreign Shares may upon agreement between them may be resolved by way of arbitration and in case no such agreement is reached, any of the disputing parties could submit the dispute to the courts with competent jurisdiction for determination. These methods of dispute resolution apply equally to disputes between holders of Foreign Shares and overseas listed foreign shares; and
- (d) upon all necessary approvals from the relevant regulatory authorities in the PRC and the Stock Exchange being obtained, the Foreign Shares may be converted into overseas listed foreign shares and shall thereafter carry the same rights and obligations attaching to overseas listed foreign shares.

COMPLIANCE WITH THE BOARD PRACTICES AND PROCEDURES OF THE GEM LISTING RULES

The Company has complied with the board practices and procedures as set out in rules 5.34 to 5.45 of the GEM Listing Rules at any time during the year ended 31 December 2006.



REPORT OF THE DIRECTORS

RETIREMENT SCHEMES

Details of the retirement schemes are set out in notes 2.18(a) and 13 to the consolidated financial statements.

AUDITORS

The financial statements have been audited by PricewaterhouseCoopers who retire and, being eligible, offer themselves for re-appointment.

By order of the Board

Rui Xin Sheng
Chairman

The PRC, 16 March 2007

REPORT OF THE SUPERVISORY COMMITTEE

To the Shareholders,

During the year ended 31 December 2006, the supervisory committee of Changmao Biochemical Engineering Company Limited (the "Supervisory Committee"), exercised conscientiously its authority, safeguarded the interests of the shareholders and the Company, followed the principle of trustworthiness, honestly carried out the duties of supervisors and worked cautiously and diligently, in accordance with the Company Law of the PRC, requirements of the relevant laws and regulations of Hong Kong and the Articles of Association of the Company for their accountability to the shareholders.

During the year, the major work performed by the Supervisory Committee included the attendance of the Board meetings; reviewing the report of the Directors and the reserve appropriation proposal prepared to be submitted by the Board for the shareholders' approval at the forthcoming annual general meeting; strictly and effectively monitored that whether the policies and decisions made by the management of the Company had conformed with the state laws and regulations of the PRC and the Articles of Association of the Company or safeguarded the interest of the shareholders. The Supervisory Committee has also reviewed the performance of the Directors, general manager and senior management in the daily operation by various means, seriously examined the Company's financial affairs and its connected transactions.

After the examination, the Supervisory Committee concluded that:

1. the report of the Directors and the reserve appropriation proposal prepared to be submitted by the Board for the shareholders' approval at the forthcoming annual general meeting are in accordance with the relevant laws and regulations and the Articles of Association of the Company;
2. the Directors, general manager and other senior management of the Company have strictly followed the principles of trustworthiness, worked diligently and responsibly, and discharged their duties for the best interest of the Company. The Supervisory Committee has not discovered that any Directors, general manager and other senior management of the Company have abused their powers, damaged the interest of the Company or the benefits of the shareholders and employees nor contravened any laws and regulations or the Articles of Association of the Company;
3. the consolidated financial statements of the Group for the year ended 31 December 2006, which have been audited by PricewaterhouseCoopers, reflected truly and fairly the operating results and financial position of the Company and its subsidiary. The connected transactions were in compliance with the GEM Listing Rules and were fair and reasonable and had not infringed upon the interest of the Company and the shareholders.

The Supervisory Committee takes this opportunity to thank the shareholders, Directors and all the employees of the Company for their supports in the past year!

By order of the Supervisory Committee

Zhou Rui Juan
Chairman of the Supervisory Committee

The PRC, 16 March 2007

INDEPENDENT AUDITOR'S REPORT



羅兵咸永道會計師事務所

PricewaterhouseCoopers
22nd Floor Prince's Building
Central Hong Kong
Telephone (852) 2289 8888
Facsimile (852) 2810 9888

**INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF
CHANGMAO BIOCHEMICAL ENGINEERING COMPANY LIMITED**

(a joint stock company incorporated in the People's Republic of China with limited liability)

We have audited the consolidated financial statements of Changmao Biochemical Engineering Company Limited (the "Company") and its subsidiary (collectively referred to as the "Group") set out on pages 46 to 92, which comprise the consolidated and Company balance sheets as at 31 December 2006, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

DIRECTORS' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The directors of the Company are responsible for the preparation and the true and fair presentation of these consolidated financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

INDEPENDENT AUDITOR'S REPORT

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit 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 person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2006 and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

PricewaterhouseCoopers

Certified Public Accountants

Hong Kong, 16 March 2007

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2006

	Note	2006 Rmb'000	2005 Rmb'000
Turnover	5	321,440	299,006
Cost of sales		(217,228)	(190,350)
Gross profit		104,212	108,656
Other operating income	6	6,374	2,168
Selling expenses		(7,015)	(6,717)
Administrative expenses		(23,884)	(21,759)
Operating profit		79,687	82,348
Finance costs	8	(5,219)	(1,659)
Share of loss of an associate	20	(123)	–
Profit before taxation		74,345	80,689
Taxation	9	(6,987)	(12,102)
Profit for the year, attributable to equity holders of the Company		67,358	68,587
Dividends	11	15,041	22,562
Earnings per share for profit attributable to equity holders of the Company during the year – basic and diluted	12	Rmb0.099	Rmb0.100

CONSOLIDATED BALANCE SHEET

AS AT 31 DECEMBER 2006

	Note	2006 Rmb'000	2005 Rmb'000
ASSETS			
Non-current assets			
Acid patent	15	6,278	6,944
Property, plant and equipment	16	145,604	101,124
Land use rights	17	25,056	11,062
Construction in progress	18	136,539	75,652
Investment in an associate	20	4,465	–
		317,942	194,782
Current assets			
Inventories	21	83,662	48,075
Trade and bills receivables	22	33,064	55,457
Amount due from a shareholder	23	128	–
Other receivables and prepayments		9,163	10,258
Bank balances and cash	24	58,448	29,526
		184,465	143,316
Total assets		502,407	338,098
EQUITY			
Capital and reserves attributable to the Company's equity holders			
Share capital	25	68,370	68,370
Reserves	26	250,426	205,630
Total equity		318,796	274,000

CONSOLIDATED BALANCE SHEET

AS AT 31 DECEMBER 2006

	Note	2006 Rmb'000	2005 Rmb'000
LIABILITIES			
Non-current liability			
Long-term bank borrowings	27	–	9,000
Current liabilities			
Amount due to a shareholder	23	–	2,285
Trade payables	28	6,978	3,244
Other payables and accrued charges		14,292	16,987
Taxation payable		3,341	3,582
Bank borrowings	27	159,000	29,000
		183,611	55,098
Total liabilities		183,611	64,098
Total equity and liabilities		502,407	338,098
Net current assets		854	88,218
Total assets less current liabilities		318,796	283,000

Rui Xin Sheng
Director

Jiang Jun Jie
Director

BALANCE SHEET

AS AT 31 DECEMBER 2006

	Note	2006 Rmb'000	2005 Rmb'000
ASSETS			
Non-current assets			
Acid patent	15	6,278	6,944
Property, plant and equipment	16	139,625	101,124
Land use rights	17	10,821	11,062
Construction in progress	18	136,539	75,652
Investment in a subsidiary	19	20,000	–
Investment in an associate	20	4,200	–
		317,463	194,782
Current assets			
Inventories	21	83,662	48,075
Trade and bills receivables	22	33,064	55,457
Amount due from a shareholder	23	128	–
Amount due from a subsidiary	19	500	–
Other receivables and prepayments		9,085	10,258
Bank balances and cash	24	58,240	29,526
		184,679	143,316
Total assets		502,142	338,098
EQUITY			
Capital and reserves attributable to the Company's equity holders			
Share capital	25	68,370	68,370
Reserves	26	250,161	205,630
Total equity		318,531	274,000

BALANCE SHEET
AS AT 31 DECEMBER 2006

	Note	2006 Rmb'000	2005 Rmb'000
LIABILITIES			
Non-current liability			
Long-term bank borrowings	27	–	9,000
Current liabilities			
Amount due to a shareholder	23	–	2,285
Trade payables	28	6,978	3,244
Other payables and accrued charges		14,292	16,987
Taxation payable		3,341	3,582
Bank borrowings	27	159,000	29,000
		183,611	55,098
Total liabilities		183,611	64,098
Total equity and liabilities		502,142	338,098
Net current assets		1,068	88,218
Total assets less current liabilities		318,531	283,000

Rui Xin Sheng
Director

Jiang Jun Jie
Director

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2006

	Note	Attributable to equity holders of the Company			Total Rmb'000
		Share capital Rmb'000	Other reserves Rmb'000	Retained earnings Rmb'000	
Balance at 1 January 2005		68,370	95,871	56,213	220,454
Transfer from income statement	26	–	5,577	(5,577)	–
Profit for the year		–	–	68,587	68,587
Final dividend for the year ended 31 December 2004		–	–	(15,041)	(15,041)
Balance at 31 December 2005		68,370	101,448	104,182	274,000
Balance at 1 January 2006		68,370	101,448	104,182	274,000
Transfer from income statement	26	–	10,290	(10,290)	–
Profit for the year		–	–	67,358	67,358
Final dividend for the year ended 31 December 2005		–	–	(22,562)	(22,562)
Balance at 31 December 2006		68,370	111,738	138,688	318,796

The notes on pages 53 to 92 are an integral part of these consolidated financial statements.

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2006

	Note	2006 Rmb'000	2005 Rmb'000
Cash flows from operating activities			
Cash generated from operations	29(a)	76,582	58,665
Interest paid		(5,638)	(1,961)
PRC income tax paid		(7,228)	(9,915)
Net cash generated from operating activities		63,716	46,789
Cash flows from investing activities			
New short-term bank deposit		–	(1,000)
Acquisition of an associate		(4,200)	–
Purchase of property, plant and equipment		(7,591)	–
Prepaid operating lease payments for land use rights		(14,235)	–
Additions of construction in progress		(108,631)	(61,492)
Proceeds from sale of property, plant and equipment		2,126	2
Interest received		310	297
Net cash used in investing activities		(132,221)	(62,193)
Cash flows from financing activities			
New bank borrowings	29(b)	155,500	61,000
Repayments of bank borrowings	29(b)	(34,500)	(55,000)
Dividends paid	29(b)	(22,562)	(15,041)
Repayments of amount due to a shareholder		(1,011)	–
Net cash generated from/(used in) financing activities		97,427	(9,041)
Net increase/(decrease) in cash and cash equivalents		28,922	(24,445)
Cash and cash equivalents at 1 January		28,526	52,971
Cash and cash equivalents at 31 December		57,448	28,526

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1 GENERAL INFORMATION

Changmao Biochemical Engineering Company Limited (the “Company”) is a joint stock limited company incorporated in the People’s Republic of China (“PRC”). The Company listed its H shares on the Growth Enterprise Market (“GEM”) of The Stock Exchange of Hong Kong Limited (the “Stock Exchange”) on 28 June 2002. The principal activities of the Company and its subsidiary (together the “Group”) are the production and sale of organic acids.

The address of the Company’s registered office is Western Chemical Area, Jiangbian Developing Zone, Changzhou City, Jiangsu Province, 213033, The PRC.

These consolidated financial statements are presented in thousand units of Renminbi (Rmb’000), unless otherwise stated. These consolidated financial statements have been approved for issue by the Board of Directors on 16 March 2007.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

2.1 Basis of preparation

The consolidated financial statements of the Company have been prepared in accordance with Hong Kong Financial Reporting Standards (“HKFRS”). They have been prepared under the historical cost convention.

The preparation of financial statements in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group’s accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in Note 4.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**2.1 Basis of preparation** (Continued)*(a) Standards, amendments and interpretations effective in 2006 but not relevant for the Group's operations*

The following standards, amendments and interpretations are mandatory for accounting periods beginning on or after 1 January 2006 but are not relevant to the Group's operations:

- HKAS 19 Amendment – Employee Benefits
- HKAS 21 Amendment – Net Investment in a Foreign Operation
- HKAS 39 Amendment – Cash Flow Hedge Accounting of Forecast Intragroup Transactions
- HKAS 39 Amendment – The Fair Value Option
- HKAS 39 and HKFRS 4 Amendment – Financial Guarantee Contracts
- HKFRS 6 – Exploration for and Evaluation of Mineral Resources
- HKFRS 1 Amendment – First-time Adoption of Hong Kong Financial Reporting Standards and HKFRS 6 Amendment – Exploration for and Evaluation of Mineral Resources
- HK(IFRIC)-Int 4 – Determining whether an Arrangement contains a Lease
- HK(IFRIC)-Int 5 – Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds
- HK(IFRIC)-Int 6 – Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment

(b) Standards and interpretations to existing standards that are not yet effective and have not been early adopted by the Group

The following standards and interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 March 2006 or later periods that the Group has not early adopted. The Directors anticipate that the adoption of these standards and interpretations to existing standards will have no material impact on the Group's financial statements.

- HKFRS 7 – Financial instruments: Disclosures, and the complementary Amendment to HKAS 1 – Presentation of Financial Statements: Capital Disclosures
- HKFRS 8 – Operating Segments
- HK(IFRIC)-Int 7 – Applying the Restatement Approach under HKAS 29 – Financial Reporting in Hyperinflationary Economies
- HK(IFRIC)-Int 8 – Scope of HKFRS 2
- HK(IFRIC)-Int 9 – Reassessment of embedded derivatives
- HK(IFRIC)-Int 10 – Interim Financial Reporting and Impairment
- HK(IFRIC)-Int 11 – HKFRS 2 – Group and Treasury Share Transactions

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**2.2 Consolidation**

The consolidated financial statements include the financial statements of the Company and all of its subsidiaries made up to 31 December.

(a) Subsidiaries

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill (Note 2.9). If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Company's balance sheet the investment in a subsidiary is stated at cost less provision for impairment losses (Note 2.10). The results of the subsidiary are accounted for by the Company on the basis of dividend received and receivable.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.2 Consolidation (Continued)

(b) Associates

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investment in an associate is accounted for using the equity method of accounting and is initially recognised at cost. The Group's investment in an associate includes goodwill (net of any accumulated impairment loss) identified on acquisition (Note 2.9). If the cost of acquisition is less than the fair values of the net identifiable assets of the associate acquired, the difference is recognised directly in the income statement.

The Group's share of its associate's post-acquisition profits or losses is recognised in the income statement, and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the Group and its associate are eliminated to the extent of the Group's interest in the associate. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of the associate have been changed where necessary to ensure consistency with the policies adopted by the Group.

Dilution gains and losses in the associate are recognised in the consolidated income statement.

In the Company's balance sheet the investment in an associate is stated at cost less provision for impairment losses (Note 2.10). The results of the associate are accounted for by the Company on the basis of dividend received and receivable.

2.3 Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**2.4 Foreign currency translation***(a) Functional and presentation currency*

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in Renminbi, which is the Company's functional and presentation currency.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as qualifying cash flow hedges or qualifying net investment hedges.

2.5 Acid patent

Acid patent is stated at cost less accumulated amortisation and accumulated impairment losses, if any. Acid patent is amortised using the straight-line method over its estimated useful life of 15 years. Where an indication of impairment exists, the carrying amount of the acid patent is assessed and written down immediately to its recoverable amount.

2.6 Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses, if any. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged in the income statement during the financial period in which they are incurred.

Depreciation of property, plant and equipment is calculated on the straight-line basis to write off their costs less accumulated impairment losses to their estimated residual values over their estimated useful lives as follows:

Buildings	20 years
Plant and machinery	10 years
Equipment and motor vehicles	5 years

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.6 Property, plant and equipment (Continued)

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2.10).

The gain or loss on disposal of property, plant and equipment is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the income statement.

2.7 Land use rights

Land use rights are stated at cost less accumulated amortisation and accumulated impairment losses, if any. Land use rights are amortised using the straight-line method over their estimated useful life of 50 years. Where an indication of impairment exists, the carrying amount of the land use rights is assessed and written down immediately to its recoverable amount.

2.8 Construction in progress

Construction in progress is stated at cost which comprises construction costs, purchase costs and other related expenses incurred in connection with the construction of buildings, plant and machinery for own use, less provision for impairment losses, if any.

No depreciation is provided for construction in progress until they are completed and put into production ready for their intended use, upon which they will be transferred to property, plant and equipment.

2.9 Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary/associate at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill on acquisitions of associates is included in investments in associates and is tested annually for impairment as part of the overall balance. Separately recognised goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**2.9 Goodwill** (Continued)

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose.

2.10 Impairment of investments in subsidiary, associate and non-financial assets

Assets that are subject to depreciation or amortisation and construction in progress which are not subject to depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

2.11 Government grants

A government grant is recognised at its fair value where there is reasonable assurance that the Group will comply with the conditions attaching with it and that the grant will be received.

Grants relating to costs are deferred and recognised in the income statement over the period necessary to match them with the related costs that they are intended to compensate, otherwise grants with no future related costs are recognised as income in the period in which they become receivable.

Government grants relating to property, plant and equipment are included in non-current liabilities as deferred income and are credited to the income statement on a straight-line basis over the expected lives of the related assets.

2.12 Inventories

Inventories 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 expenditures. It excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.13 Trade and other receivables

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the assets is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement. When a receivable is uncollectible, it is written off against the allowance account for receivables. Subsequent recoveries of amounts previously written off are credited in the income statement.

2.14 Cash and cash equivalents

Cash and cash equivalents include cash in hand and deposits held with banks at call. Bank deposits with original maturities of more than three months are excluded from cash and cash equivalents.

2.15 Trade payables

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

2.16 Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

2.17 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 financial statements. Deferred taxation is determined using tax rates enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred tax assets are realised or the deferred tax liabilities are settled.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**2.17 Deferred taxation** (Continued)

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 subsidiary and associate, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

2.18 Employees benefits*(a) Pension obligations*

The Group contributes to various employee retirement benefit plans organised by municipal and provincial governments in Mainland China for its PRC based employees. Under these plans, the municipal and provincial governments undertake to assume the retirement benefit obligations of all existing and future retired PRC based employees of the Group. Contributions to these plans are expensed as incurred.

The Group's contributions to the Mandatory Provident Fund Scheme established under the Hong Kong Mandatory Provident Fund Schemes Ordinance are expensed as incurred. Both the Group and its employees in Hong Kong are required to contribute 5% of each individual's relevant income with a maximum amount of HK\$1,000 per month as a mandatory contribution. Employees may also elect to contribute more than the minimum as a voluntary contribution. The assets of the scheme are held separately from those of the Group and managed by independent professional fund managers.

(b) Profit-sharing and bonus plans

The Group recognises a liability and an expense for bonuses and profit-sharing, based on a formula that takes into consideration the profit attributable to the Company's shareholders after certain adjustments. The Group recognises a provision where contractually obliged or where there is a past practice that has created a constructive obligation.

2.19 Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.20 Research and development costs

Research costs are expensed as incurred. Costs incurred on development projects relating to the design and testing of new or improved products are recognised as an intangible asset when the technical feasibility and intention of completing the product under development has been demonstrated and the resources are available to do so, costs are identifiable and there is an ability to sell or use the asset that will generate probable future economic benefits. Such development costs are recognised as an asset and amortised on the straight-line basis to reflect the pattern in which the related economic benefits are recognised. Development costs that do not meet the above criteria are expensed as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period.

2.21 Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of goods in the ordinary course of the Group's activities. Revenue is shown net of value-added tax, returns, rebates and discounts and after eliminating sales within the Group. Revenue from sales of goods are recognised when goods are delivered to customers and title has passed.

Interest income is recognised on a time-proportion basis using the effective interest method.

2.22 Operating leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

2.23 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 income statement during the financial period in which they are incurred.

2.24 Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved by the Company's shareholders.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

3 FINANCIAL RISK MANAGEMENT**3.1 Financial risk factors**

The Group's activities expose it to a variety of financial risks, including foreign exchange risk, credit risk, liquidity risk and cash flow and fair value interest rate risk. The use of financial derivatives to hedge certain risk exposures is governed by the Group's policies approved by the Board of Directors. The Group does not use any significant derivative financial instruments during the year.

(a) Foreign exchange risk

The Group mainly operates in the PRC. Substantially all of its assets, liabilities and capital expenditure were located or incurred in Mainland China. Sales are made to customers in the PRC as well as overseas customers while purchases are mainly from suppliers in the PRC. The Group is therefore exposed to foreign exchange risk arising from various currency exposures, primarily with respect to United States Dollars ("USD") and Euro ("EUR"). The Group has not used any significant forward contracts, currency borrowings or other means to hedge its foreign currency exposure. The depreciation or appreciation of foreign currencies against Renminbi will affect the Group's results of operations.

(b) Credit risk

The Group has no significant concentrations of credit risk. The Group has policies in place to ensure that sales of products are made to customers with an appropriate credit history and the Group performs periodic credit evaluation of its customers.

(c) Liquidity risk

The Group's primary cash requirements have been for construction of and upgrades on property, plant and equipment, payment on related debts and payment for research and development expenses. The Group finances its working capital requirements through a combination of funds generated from operations, short-term and long-term bank borrowings.

Due to the dynamic nature of the underlying businesses, the Group's policy is to regularly monitor current and expected liquidity requirements, to ensure that it maintains sufficient reserves of cash and adequate lines of funding to meet its liquidity requirements in the short and long term.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

3 FINANCIAL RISK MANAGEMENT (Continued)**3.1 Financial risk factors** (Continued)*(d) Cash flow and fair value interest rate risk*

The Group's income and operating cash flows are substantially independent of changes in market interest rates and the Group has no significant interest-bearing assets except for the cash and cash equivalents, details of which are disclosed in Note 24. The Group's exposure to changes in interest rates is mainly attributable to its long-term and short-term bank borrowings which carry interest at fixed rates and expose the Group to cash flow interest-rate risk; long-term borrowings at fixed rate expose the Group to fair value interest-rate risk, details of which are disclosed in Note 27. The Group has not used any interest rate swaps to hedge its exposure to interest rate risk.

3.2 Accounting for derivative financial instruments

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. During the year ended 31 December 2006, the Group did not enter into any derivative financial instruments.

3.3 Fair value estimation

The carrying amounts of the Group's current financial assets, including cash and cash equivalents, trade receivables and other receivables, and current financial liabilities, including trade payables, other payables and short-term bank borrowings, approximate their fair values due to their short maturities.

The nominal value less estimated credit adjustments for financial assets and liabilities with a maturity of less than one year are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

*NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS***4 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS**

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

(a) Useful lives of property, plant and equipment

Management determines the estimated useful lives and related depreciation charges for the Group's property, plant and equipment, other than construction in progress. Management will revise the depreciation charge where useful lives are different to previously estimated, or it will write-off or write-down technically obsolete or non-strategic assets that have been abandoned or sold.

(b) Acid patent

Management determines the estimated useful life and the related amortisation charges for the Group's acid patent. Management will revise the amortisation charge where its useful life is different to previously estimated, or it will write-off or write-down the carrying value of the acid patent to its recoverable amount where there is an impairment of the asset.

(c) Impairment of non-financial assets

Other non-financial assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset exceeds its recoverable amount in accordance with the accounting policy stated in Note 2.10. The recoverable amount of an asset or a cash-generating unit is determined based on value-in-use calculations. The value-in-use calculation requires the entity to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate present value, which has been prepared on the basis of management's assumptions and estimates. Detailed sensitivity analyses have been performed and management is confident that the carrying amount of the relevant assets will be recovered in full.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

5 TURNOVER AND SEGMENT INFORMATION

The Group is principally engaged in the production and sale of organic acids. Turnover recognised during the year is as follows:

	2006 Rmb'000	2005 Rmb'000
Turnover		
Sales of goods	321,440	299,006

An analysis of the Group's turnover for the year by geographical segment is as follows:

	2006 Rmb'000	2005 Rmb'000
Mainland China	171,322	162,592
Europe	46,894	50,487
Asia Pacific	46,445	41,399
America	49,494	41,027
Others	7,285	3,501
	321,440	299,006

The Asia Pacific region includes Australia, Hong Kong, India, Indonesia, Japan, Malaysia, New Zealand, Singapore, South Korea, Taiwan and Thailand.

The analysis of turnover by geographic segment is based on the country in which the customer is located. No analysis of contribution by geographic segment has been presented as the ratio of profit to turnover achieved for individual segment is not substantially out of line with the Group's overall ratio of profit to turnover.

No analysis of the segment information by business segment has been presented as the Group has been engaged in the production and sale of organic acids only. Substantially all of its assets, liabilities and capital expenditure for the year were located or utilised in Mainland China.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

6 OTHER OPERATING INCOME

	2006 Rmb'000	2005 Rmb'000
Sales of scrap materials	1,651	1,473
Government grants and subsidies	2,723	672
Gain on disposal of property, plant and equipment	1,608	–
Negative goodwill on acquisition of an associate	388	–
Others	4	23
	6,374	2,168

7 EXPENSES BY NATURE

	2006 Rmb'000	2005 Rmb'000
Cost of inventories sold	160,470	146,820
Write-downs of inventories to net realisable value	1,018	–
Amortisation of acid patent recognised in administrative expenses (Note 15)	666	667
Amortisation of land use rights recognised in administrative expenses (Note 17)	241	241
Auditors' remuneration	780	588
Depreciation (Note 16)	12,436	9,330
Loss on disposal of property, plant and equipment	–	24
Net exchange losses	1,127	1,423
Operating leases in respect of land and buildings	448	416
Impairment of trade receivables	54	14
Research and development costs	2,104	1,770
Staff costs (including emoluments of Directors and Supervisors) (Note 13)	22,091	20,081
Other expenses	46,692	37,452
	248,127	218,826

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

8 FINANCE COSTS

	2006 Rmb'000	2005 Rmb'000
Interest on bank borrowings – wholly repayable within five years	5,832	1,961
Less: Interest capitalised (note)	(303)	(5)
	5,529	1,956
Interest income on bank deposits	(310)	(297)
Net finance costs	5,219	1,659

Note: A capitalisation rate of 5.8% (2005: 5.8%) was used, representing the borrowing cost of the loans used to finance the construction project.

9 TAXATION

PRC Enterprise Income Tax ("EIT") is provided on the basis of the statutory profit for financial reporting purposes, adjusted for income and expense items which are not assessable or deductible for income tax purposes. The Company, being located in the New Technology Industrial Development Experimental Zone in Changzhou and registered as a New and High Technology Enterprise, is not subject to any local income tax. Upon renewal of the 技術密集型知識密集型企業證書 (The Certificate of Technology-intensive and Knowledge-intensive Enterprise) in November 2005, the Company is entitled to a preferential EIT rate of 15% up to the financial year ending 31 December 2007. The subsidiary of the Group in Mainland China does not have assessable profit during the year.

The amount of taxation charged to consolidated income statement represents:

	2006 Rmb'000	2005 Rmb'000
Provision for EIT	11,008	12,102
Tax credit (note)	(4,021)	–
	6,987	12,102

Note: During the year, the Company obtained approval from the tax bureau in Mainland China whereby it is granted a tax credit of approximately Rmb4,021,000 in respect of purchase of certain equipments manufactured in Mainland China.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

9 TAXATION (Continued)

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

	2006 Rmb'000	2005 Rmb'000
Profit before taxation	74,345	80,689
Adjustment: share of loss of an associate	123	–
	<hr/>	<hr/>
	74,468	80,689

Calculated at the taxation rate of 15% (2005: 15%)	11,170	12,103
Income not subject to tax	(317)	–
Expenses not deductible for tax purposes	155	–
Tax credit	(4,021)	–
Others	–	(1)
	<hr/>	<hr/>
Taxation	6,987	12,102

As at 31 December 2006 and 2005, there was no significant unprovided deferred taxation.

10 PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

The profit attributable to equity holders of the Company is dealt with in the financial statements of the Company to the extent of approximately Rmb67,093,000 (2005: Rmb68,587,000).

11 DIVIDENDS

	2006 Rmb'000	2005 Rmb'000
Final, proposed, of Rmb0.022 (2005: Rmb0.033) per share	15,041	22,562

At a Board meeting held on 16 March 2007, the Directors proposed a final dividend of Rmb0.022 per share, totalling approximately Rmb15,041,000 for the year ended 31 December 2006. This proposed dividend is not reflected as a dividend payable in these financial statements, but will be reflected as an appropriation of retained earnings for the year ending 31 December 2007.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

12 EARNINGS PER SHARE

The calculation of basic earnings per share for the year ended 31 December 2006 is based on the profit attributable to the equity holders of the Company of Rmb67,358,000 (2005: Rmb68,587,000) and the 683,700,000 (2005: 683,700,000) shares in issue during the year.

The Company has no dilutive potential shares in issue during the year.

13 STAFF COSTS

Staff costs including Directors' and Supervisors' remunerations are as follows:

	2006 Rmb'000	2005 Rmb'000
Salaries, wages and related welfare	18,632	17,339
Social security costs	1,584	1,177
Contribution to defined contribution retirement schemes (note)	1,875	1,565
	22,091	20,081

Note: The Group is required to participate in defined contribution retirement schemes organised by the relevant local government authorities for its PRC based employees. Contributions to the retirement schemes are payable at a rate of 21% of the total salaries and allowances of the PRC based employees, subject to a ceiling, and the Group has no further retirement benefit obligations to all its existing and future retired PRC based employees.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

14 EMOLUMENTS OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

- (a) The remuneration of each of the Directors of the Company for the year ended 31 December 2006 is set out as follows:

Name of Director	Fees Rmb'000	Basic salaries, allowances and benefits in kind Rmb'000	Bonus Rmb'000	Retirement benefit contributions Rmb'000	Total Rmb'000
<i>Executive director</i>					
Mr. Rui Xin Sheng	320	494	1,568	13	2,395
Mr. Jiang Jun Jie	100	164	523	13	800
<i>Non-executive director</i>					
Mr. Zeng Xian Biao	50	–	261	–	311
Mr. Yu Xiao Ping	50	–	261	–	311
Mr. Lu Chong Zhu	50	–	261	–	311
Ms. Leng Yi Xin	50	–	261	–	311
<i>Independent non-executive director</i>					
Prof. Ouyang Ping Kai	50	–	–	–	50
Prof. Yang Sheng Li	50	–	–	–	50
Ms. Wei Xin	50	–	–	–	50

The remuneration of each of the Directors of the Company for the year ended 31 December 2005 is set out as follows:

Name of Director	Fees Rmb'000	Basic salaries, allowances and benefits in kind Rmb'000	Bonus Rmb'000	Retirement benefit contributions Rmb'000	Total Rmb'000
<i>Executive director</i>					
Mr. Rui Xin Sheng	320	469	1,639	11	2,439
Mr. Jiang Jun Jie	100	140	468	10	718
<i>Non-executive director</i>					
Mr. Zeng Xian Biao	50	–	234	–	284
Mr. Zhu Lai Fa (note)	36	–	234	–	270
Mr. Yu Xiao Ping	50	–	234	–	284
Mr. Lu Chong Zhu	50	–	234	–	284
Ms. Leng Yi Xin	50	–	234	–	284
<i>Independent non-executive director</i>					
Prof. Ouyang Ping Kai	50	–	–	–	50
Prof. Yang Sheng Li	50	–	–	–	50
Ms. Wei Xin	50	–	–	–	50

Note: Resigned on 16 September 2005

None of the Directors waived any emoluments during the years ended 31 December 2006 and 2005.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

14 EMOLUMENTS OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT (Continued)

- (b) The remuneration of each of the Supervisors of the Company for the year ended 31 December 2006 is set out as follows:

Name of Director	Fees Rmb'000	Basic salaries, allowances and benefits in kind Rmb'000	Bonus Rmb'000	Retirement benefit contributions Rmb'000	Total Rmb'000
Ms. Zhou Rui Juan	15	32	89	9	145
Mr. Lu He Xing	6	–	–	–	6
Mr. Pan Chun	6	41	79	9	135
Prof. Gu Jian Xin	15	–	–	–	15
Prof. Jiang Yao Zhong	15	–	–	–	15

The remuneration of each of the Supervisors of the Company for the year ended 31 December 2005 is set out as follows:

Name of Director	Fees Rmb'000	Basic salaries, allowances and benefits in kind Rmb'000	Bonus Rmb'000	Retirement benefit contributions Rmb'000	Total Rmb'000
Ms. Zhou Rui Juan	15	42	74	8	139
Mr. Lu He Xing	6	–	–	–	6
Mr. Pan Chun	6	40	73	8	127
Prof. Gu Jian Xin	15	–	–	–	15
Prof. Jiang Yao Zhong	15	–	–	–	15

None of the Supervisors waived any emoluments during the years ended 31 December 2006 and 2005.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

14 EMOLUMENTS OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT (Continued)

- (c) The five individuals whose emoluments were the highest in the Group during the year are as follows:

	2006	2005
Directors	4	2
Supervisors	–	1
Employees	1	2
	<hr/>	<hr/>
	5	5

Details of the emoluments paid and payable to the employee (2005: two employees) mentioned above, whose emoluments were less than HK\$1,000,000, are as follows:

	2006 Rmb'000	2005 Rmb'000
Basic salaries, allowances and benefits in kind	719	758
Discretionary bonus	119	242
Retirement benefit contributions	12	16
	<hr/>	<hr/>
	850	1,016

- (d) During the year, no emoluments have been paid to the Directors and Supervisors of the Company or the five highest paid individuals as an inducement to join or as compensation for loss of office.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

15 ACID PATENT

	Group and Company	
	2006 Rmb'000	2005 Rmb'000
Net book amount, at 1 January	6,944	7,611
Amortisation charge (Note 7)	(666)	(667)
Net book amount, at 31 December	6,278	6,944

	Group and Company	
	2006 Rmb'000	2005 Rmb'000
At cost	10,000	10,000
Accumulated amortisation	(3,722)	(3,056)
Net book amount	6,278	6,944

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

16 PROPERTY, PLANT AND EQUIPMENT

	Group			
	Buildings	Plant and machinery	Equipment and motor vehicles	Total
	Rmb'000	Rmb'000	Rmb'000	Rmb'000
At 1 January 2005				
Cost	40,433	68,773	5,862	115,068
Accumulated depreciation	(4,940)	(15,272)	(3,096)	(23,308)
Net book amount	35,493	53,501	2,766	91,760
Year ended 31 December 2005				
Opening net book amount	35,493	53,501	2,766	91,760
Transfer from construction in progress (Note 18)	94	15,732	2,894	18,720
Disposals	–	–	(26)	(26)
Depreciation (Note 7)	(1,821)	(6,473)	(1,036)	(9,330)
Closing net book amount	33,766	62,760	4,598	101,124
At 31 December 2005				
Cost	40,527	84,505	8,499	133,531
Accumulated depreciation	(6,761)	(21,745)	(3,901)	(32,407)
Net book amount	33,766	62,760	4,598	101,124
Year ended 31 December 2006				
Opening net book amount	33,766	62,760	4,598	101,124
Additions	7,591	–	–	7,591
Transfer from construction in progress (Note 18)	18,237	28,936	2,670	49,843
Disposals	(478)	(40)	–	(518)
Depreciation (Note 7)	(2,252)	(8,718)	(1,466)	(12,436)
Closing net book amount	56,864	82,938	5,802	145,604
At 31 December 2006				
Cost	65,492	113,399	11,168	190,059
Accumulated depreciation	(8,628)	(30,461)	(5,366)	(44,455)
Net book amount	56,864	82,938	5,802	145,604

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

16 PROPERTY, PLANT AND EQUIPMENT (Continued)

	Company			Total Rmb'000
	Buildings Rmb'000	Plant and machinery Rmb'000	Equipment and motor vehicles Rmb'000	
At 1 January 2005				
Cost	40,433	68,773	5,862	115,068
Accumulated depreciation	(4,940)	(15,272)	(3,096)	(23,308)
Net book amount	35,493	53,501	2,766	91,760
Year ended 31 December 2005				
Opening net book amount	35,493	53,501	2,766	91,760
Transfer from construction in progress (Note 18)	94	15,732	2,894	18,720
Disposals	–	–	(26)	(26)
Depreciation	(1,821)	(6,473)	(1,036)	(9,330)
Closing net book amount	33,766	62,760	4,598	101,124
At 31 December 2005				
Cost	40,527	84,505	8,499	133,531
Accumulated depreciation	(6,761)	(21,745)	(3,901)	(32,407)
Net book amount	33,766	62,760	4,598	101,124
Year ended 31 December 2006				
Opening net book amount	33,766	62,760	4,598	101,124
Additions	1,612	–	–	1,612
Transfer from construction in progress (Note 18)	18,237	28,936	2,670	49,843
Disposals	(478)	(40)	–	(518)
Depreciation	(2,252)	(8,718)	(1,466)	(12,436)
Closing net book amount	50,885	82,938	5,802	139,625
At 31 December 2006				
Cost	59,513	113,399	11,168	184,080
Accumulated depreciation	(8,628)	(30,461)	(5,366)	(44,455)
Net book amount	50,885	82,938	5,802	139,625

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

17 LAND USE RIGHTS

The Group's interests in land use rights represent prepaid operating lease payments for land use rights on three pieces of land situated in Mainland China under lease term of 50 years.

	Group		Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Net book amount, at 1 January	11,062	11,303	11,062	11,303
Additions	14,235	–	–	–
Amortisation charge (Note 7)	(241)	(241)	(241)	(241)
Net book amount, at 31 December	25,056	11,062	10,821	11,062

	Group		Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
At cost	26,275	12,040	12,040	12,040
Accumulated amortisation	(1,219)	(978)	(1,219)	(978)
Net book amount	25,056	11,062	10,821	11,062

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

18 CONSTRUCTION IN PROGRESS

	Group and Company	
	2006 Rmb'000	2005 Rmb'000
At 1 January	75,652	33,646
Additions	110,730	60,726
Transfer to property, plant and equipment (Note 16)	(49,843)	(18,720)
At 31 December	136,539	75,652

19 INVESTMENT IN AND AMOUNT DUE FROM A SUBSIDIARY – COMPANY

(a) Investment in a subsidiary

	2006 Rmb'000	2005 Rmb'000
Unlisted investment, at cost	20,000	–

Details of the subsidiary at 31 December 2006 are as follows:

Name	Place of establishment, operations and kind of legal entity	Particulars of registered capital	Interest directly held	Principal activities
上海常茂生物化學工程 有限公司 (Shangahi Changmao Biochemical Engineering Company Limited)	PRC, limited liability company	Rmb20,000,000	100%	Property holding

(b) Amount due from a subsidiary

The amount due from a subsidiary is unsecured, interest free and does not have fixed repayment terms.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

20 INVESTMENT IN AN ASSOCIATE**(a) The Group**

	2006 Rmb'000	2005 Rmb'000
At 1 January	–	–
Acquisition of an associate		
– cost of acquisition	4,200	–
– negative goodwill	388	–
Share of loss	(123)	–
At 31 December	4,465	–

The Group's interest in its associate at 31 December 2006 is as follows:

Name	Particulars of registered capital held	Country of establishment	Assets	Liabilities	Revenues	Net loss	Interest directly held
			Rmb'000	Rmb'000	Rmb'000	Rmb'000	%
常州蘭陵制葯有限公司 (Changzhou Lanling Pharmaceutical Production Co., Ltd.)	Rmb4,200,000, unlisted	PRC	42,065	37,600	5,568	123	42

(b) The Company

	2006 Rmb'000	2005 Rmb'000
Unlisted investment, at cost	4,200	–

- (c) There are no contingent liabilities relating to the Group's investment in the associate, and no contingent liabilities of the associate itself.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

21 INVENTORIES

	Group and Company	
	2006 Rmb'000	2005 Rmb'000
Raw materials	27,162	13,193
Work-in-progress	12,002	6,290
Finished goods	44,498	28,592
	83,662	48,075

22 TRADE AND BILLS RECEIVABLES

	Group and Company	
	2006 Rmb'000	2005 Rmb'000
Trade receivables (note (a))	27,880	45,724
Bills receivables (note (b))	5,184	9,733
	33,064	55,457

- (a) The credit terms of trade receivables range from 30 to 90 days and the ageing analysis of the trade receivables is as follows:

	Group and Company	
	2006 Rmb'000	2005 Rmb'000
0 to 3 months	27,631	44,625
4 to 6 months	47	796
Over 6 months	202	303
	27,880	45,724

- (b) The maturity dates of bills receivable are normally within 30 days.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

22 TRADE AND BILLS RECEIVABLES (Continued)

The carrying amounts of trade and bills receivables approximate their fair values and are denominated in the following currencies:

	Group and Company	
	2006	2005
	Rmb'000	Rmb'000
RMB	18,887	28,706
USD	13,688	25,083
EUR	489	1,668
	<hr/>	<hr/>
	33,064	55,457

There is no concentration of credit risk with respect to trade and bills receivables, as the Group has a large number of internationally dispersed customers.

23 AMOUNT DUE FROM/TO A SHAREHOLDER

Pursuant to the Promoters' Agreement and a reorganisation agreement dated 9 June 2002 entered into between the Company and its then shareholders, Changzhou Shuguang Chemical Factory ("Shuguang Factory") and Jomo Limited ("Jomo"), provided that the net assets of the Company as at the close of business on 17 June 2001, determined in accordance with the accounting principles and financial regulations applicable to PRC foreign investment enterprises, exceed the net asset value of the Company as at the close of business on 31 October 2000, the excess amount (the "Excess") shall be payable by the Company to its then shareholders. Accordingly, the Excess at 17 June 2001 amounting to approximately Rmb17,602,000 was accounted for as distributions to shareholders payable to Shuguang Factory and Jomo.

As of 31 December 2006, all of Excess payable to Shungang Factory and Jomo had been fully repaid. As of 31 December 2005 included in the amount due to a shareholder was an amount of Rmb1,011,000 representing balance of the distributions of the Excess payable to Shuguang Factory.

The amount due from/to a shareholder is unsecured, interest free and repayable on demand and the amount receivable at 31 December 2006 is trading balance only (also see Note 31 (iii)).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

24 BANK BALANCES AND CASH

	Group		Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Cash and cash equivalents	57,448	28,526	57,240	28,526
Short-term bank deposit with an initial term of more than three months	1,000	1,000	1,000	1,000
	58,448	29,526	58,240	29,526

	Group		Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Denominated in:				
– RMB	44,189	19,136	43,981	19,136
– USD	13,684	7,483	13,684	7,483
– EUR	451	2,238	451	2,238
– HK Dollars	124	669	124	669
	58,448	29,526	58,240	29,526

Cash at banks earns interest at floating rates based on daily bank deposit rates. Short-term bank deposit earns interest at an effective interest rate of 2.1% (2005: 2.1%).

The conversion of Renminbi denominated balances into foreign currencies and the remittance of these funds out of the Mainland China is subject to relevant rules and regulations of foreign exchange control promulgated by the PRC government.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

25 SHARE CAPITAL

Registered, issued and fully paid:

	Share capital	
	Number of shares at Rmb0.10 each	Nominal value Rmb'000
At 31 December 2006 and 2005	683,700,000	68,370

As at 31 December 2006 and 2005, the share capital of the Company composed of 219 million domestic shares, 281 million Promoter foreign shares and 183.7 million H shares. The H shares rank pari passu with the domestic shares and Promoter foreign shares in all aspects and rank equally for all dividends or distributions declared, paid or made except that all dividends in respect of H shares are to be paid by the Company in Hong Kong dollars and H shares may only be subscribed for by, and trade in Hong Kong dollars between legal or natural persons of Hong Kong, Macau, Taiwan or any country other than the PRC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

26 RESERVES

	Share premium Rmb'000	Statutory common reserve Rmb'000	Group Statutory public welfare fund Rmb'000	Retained earnings Rmb'000	Total Rmb'000
At 1 January 2005	87,159	5,808	2,904	56,213	152,084
Transfer from income statement	–	3,718	1,859	(5,577)	–
Profit for the year	–	–	–	68,587	68,587
Final dividend for the year ended 31 December 2004	–	–	–	(15,041)	(15,041)
At 31 December 2005	87,159	9,526	4,763	104,182	205,630

Representing:

2005 proposed final dividend	22,562
Others	81,620
	<u>104,182</u>

	Share premium Rmb'000	Statutory common reserve Rmb'000	Statutory public welfare fund Rmb'000	Retained earnings Rmb'000	Total Rmb'000
At 1 January 2006	87,159	9,526	4,763	104,182	205,630
Transfer from income statement	–	6,860	3,430	(10,290)	–
Profit for the year	–	–	–	67,358	67,358
Final dividend for the year ended 31 December 2005	–	–	–	(22,562)	(22,562)
At 31 December 2006	87,159	16,386	8,193	138,688	250,426

Representing:

2006 proposed final dividend	15,041
Others	123,647
	<u>138,688</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

26 RESERVES (Continued)

	Share premium Rmb'000	Statutory common reserve Rmb'000	Company Statutory public welfare fund Rmb'000	Retained earnings Rmb'000	Total Rmb'000
At 1 January 2005	87,159	5,808	2,904	56,213	152,084
Transfer from income statement	–	3,718	1,859	(5,577)	–
Profit for the year	–	–	–	68,587	68,587
Final dividend for the year ended 31 December 2004	–	–	–	(15,041)	(15,041)
At 31 December 2005	87,159	9,526	4,763	104,182	205,630

Representing:

2005 proposed final dividend	22,562
Others	81,620
	<u>104,182</u>

	Share premium Rmb'000	Statutory common reserve Rmb'000	Statutory public welfare fund Rmb'000	Retained earnings Rmb'000	Total Rmb'000
At 1 January 2006	87,159	9,526	4,763	104,182	205,630
Transfer from income statement	–	6,860	3,430	(10,290)	–
Profit for the year	–	–	–	67,093	67,093
Final dividend for the year ended 31 December 2005	–	–	–	(22,562)	(22,562)
At 31 December 2006	87,159	16,386	8,193	138,423	250,161

Representing:

2006 proposed final dividend	15,041
Others	123,382
	<u>138,423</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

26 RESERVES (Continued)**(a) Statutory common reserve**

According to the Company's Articles of Association, the Company is required to transfer 10% of its profit after tax, as determined in accordance with the PRC accounting rules and regulations, to statutory common reserve until the reserve balance reaches 50% of the registered capital. The transfer to this reserve must be made before distribution of a dividend to shareholders.

Statutory common reserve can be used to make good previous years' losses, if any, to expand the business operations of the Company and may be converted into share capital by the issuance of new shares to shareholders in proportion to their existing shareholdings or by increasing the par value of the shares currently held by them, provided that the balance after such issue is not less than 25% of the registered capital of the Company. For the year ended 31 December 2006, the Board of Directors proposed the transfer of approximately Rmb6,320,000 (2005: Rmb6,861,000) to the statutory common reserve, being 10% of the current year's net profit determined in accordance with the PRC accounting rules and regulations, subject to the shareholders' approval at the forthcoming annual general meeting. The proposed transfer will be reflected as an appropriation of retained earnings for the year ending 31 December 2007.

(b) Statutory public welfare fund

According to the Company's Articles of Association, the Company is required to transfer 5% of its profits after tax, as determined in accordance with the then PRC accounting rules and regulations, to the statutory public welfare fund. This fund can only be utilised for the collective benefits of the Company's employees. This fund is non-distributable other than on liquidation. The transfer to this fund must be made before distribution of a dividend to shareholders.

For the year ended 31 December 2005, the Board of Directors proposed and the shareholders approved the transfer of approximately Rmb3,430,000 to the statutory public welfare fund, being 5% of the current year's net profit determined in accordance with the then PRC accounting rules and regulations. The transfer was reflected as an appropriation of retained earnings for the year ended 31 December 2006.

According to Cai Qi (2006) No. 67, a circular on accounting treatment following the implementation of Company Law issued by the Ministry of Finance of the PRC, statutory public welfare fund is no longer mandatory in annual distribution plan of net profit starting from 1 January 2006. For the year ended 31 December 2006, the Board of Directors proposed to amend the Company's Articles of Association and not to transfer any of the Company's profits to the statutory public welfare fund, subject to the shareholders' approval at the forthcoming annual general meeting.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

27 BANK BORROWINGS

Bank borrowings are analysed as follows:

	Group and Company	
	2006 Rmb'000	2005 Rmb'000
Non-current		
Unsecured, long-term bank borrowings wholly repayable within five years	13,500	18,000
Less: Current portion of long-term bank borrowings	(13,500)	(9,000)
	-	9,000
Current		
Unsecured, short-term bank borrowings	145,500	20,000
Current portion of long-term bank borrowings as shown above	13,500	9,000
	159,000	29,000
Total borrowings	159,000	38,000

The maturity of borrowings is as follows:

	Group and Company	
	2006 Rmb'000	2005 Rmb'000
Within 1 year	159,000	29,000
Between 1 and 2 years	-	9,000
	159,000	38,000

All the Group's borrowings are denominated in Renminbi. The carrying amounts of these bank borrowings approximate their fair values.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

27 BANK BORROWINGS (Continued)

As at 31 December 2006, the effective interest rates of the bank borrowings were as follows:

	Group and Company	
	2006	2005
	Rmb'000	Rmb'000
Long-term bank borrowings, at fixed rate	5.8%	5.8%
Short-term bank borrowings, at fixed rate	5.8%	5.4%

28 TRADE PAYABLES

The ageing analysis of trade payables is as follows:

	Group and Company	
	2006	2005
	Rmb'000	Rmb'000
0 to 6 months	6,889	3,150
7 to 12 months	13	21
Over 12 months	76	73
	6,978	3,244

The carrying amounts of trade payables approximate their fair values and are all denominated in Renminbi.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

29 NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

(a) Reconciliation of profit before taxation to net cash generated from operations

	2006 Rmb'000	2005 Rmb'000
Profit before taxation	74,345	80,689
Interest income	(310)	(297)
Interest expense	5,529	1,956
Depreciation	12,436	9,330
Amortisation of acid patent	666	667
Amortisation of land use rights	241	241
(Gain)/loss on disposal of property, plant and equipment	(1,608)	24
Impairment of trade receivables	54	14
Write-downs of inventories to net realisable value	1,018	–
Negative goodwill on acquisition of an associate	(388)	–
Share of loss of an associate	123	–
	92,106	92,624
Changes in working capital:		
Increase in inventories	(36,605)	(13,044)
Decrease/(increase) in trade and bills receivables, other receivables and prepayments	23,434	(24,685)
(Decrease)/increase in trade payables, other payables and accrued charges	(951)	4,064
Decrease in amount due to a shareholder	(1,402)	(294)
Net cash generated from operations	76,582	58,665

(b) Analysis of changes in financing during the year

	Bank borrowings		Dividends payable	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Balance at 1 January	38,000	32,000	–	–
New bank borrowings	155,500	61,000	–	–
Repayments of bank borrowings	(34,500)	(55,000)	–	–
2005 final dividend	–	–	22,562	–
2004 final dividend	–	–	–	15,041
Dividends paid	–	–	(22,562)	(15,041)
Balance at 31 December	159,000	38,000	–	–

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

30 COMMITMENTS**(a) Capital commitments for property, plant and equipment are as follows:**

	Group and Company	
	2006	2005
	Rmb'000	Rmb'000
Authorised but not contracted for	–	25,000
Contracted but not provided for	7,186	11,739
	<hr/>	<hr/>
	7,186	36,739

(b) Commitments under operating leases

The Group leases various offices and warehouses under non-cancellable operating leases. At 31 December 2006, the Group and the Company had future aggregate minimum lease payments in respect of land and buildings under non-cancellable operating leases as follows:

	Group and Company	
	2006	2005
	Rmb'000	Rmb'000
Not later than one year	171	423
Later than one year and not later than five years	102	251
Later than five years	986	1,011
	<hr/>	<hr/>
	1,259	1,685

The leases for offices and warehouses generally ranged from 2 to 5 years.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 RELATED PARTY TRANSACTIONS

Parties are considered to be related if they have the ability, directly or indirectly, to control the parties or exercise significant influence over the Group in making financial and operating decisions, or vice versa, or where the Group and the parties are subject to common control or common significant influence.

(i) Name and relationship with related parties

Shuguang Factory is a related party as it is a shareholder of the Company.

(ii) Transactions with related parties

The Group entered into the following significant transactions in the ordinary course of business with Shugang Factory during the year:

	2006 Rmb'000	2005 Rmb'000
Purchases of raw materials from Shuguang Factory (note (a))	88	3,557
Electricity charged by Shuguang Factory (note (b))	2,528	2,249
Water supply charged by Shuguang Factory (note (b))	334	303
Rental expenses to Shuguang Factory (note (c))	186	186
Transportation expenses charged by Shuguang Factory (note (d))	466	467
Processing fee charged by Shuguang Factory (note (e))	1,235	798
Sales commission charged by Shuguang Factory (note (e))	408	394

- (a) In the opinion of the Directors, the purchases were determined with reference to the then prevailing market prices and the prices charged by Shuguang Factory to third parties.
- (b) The electricity and water supply are charged by Shuguang Factory on a cost reimbursement basis.
- (c) Rental expenses to Shuguang Factory were based at fixed amounts in accordance with the terms of the lease agreements.
- (d) Transportation expenses to Shuguang Factory were based at fixed rates with reference to market price quoted from third parties.
- (e) Processing fee and sales commission to Shuguang Factory were based at fixed rates in accordance with the terms of the processing and sales agreements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 RELATED PARTY TRANSACTIONS (Continued)**(iii) Balances with related parties**

	2006 Rmb'000	2005 Rmb'000
Distribution of Excess payable to Shuguang Factory	–	(1,011)
Prepayment for purchase of raw materials from Shuguang Factory	128	–
Purchase of raw materials and services payable to Shuguang Factory	–	(1,274)
Amount due from/(to) a shareholder (Note 23)	128	(2,285)

The balance with the shareholder is unsecured, interest free and repayable on demand.

During the year ended 31 December 2006, the maximum balance due from Shuguang Factory amounted to approximately Rmb880,000.

(iv) Key management compensation

	2006 Rmb'000	2005 Rmb'000
Salaries and other short-term employee benefits	3,168	3,136
Retirement benefit costs	26	21
	3,194	3,157

32 EVENTS AFTER THE BALANCE SHEET DATE

In January 2007, the Group entered into an agreement to acquire 78% interest in 上海醫學生命科學研究中心有限公司 (Shanghai Medical Life Science Research Centre Limited) which is specialising in research and development of medicine and nutrition products, for a cash consideration of Rmb3,794,000.

FIVE YEAR SUMMARY

	2002 Rmb'000	2003 Rmb'000	2004 Rmb'000	2005 Rmb'000	2006 Rmb'000
Consolidated results					
Turnover	96,769	144,632	200,984	299,006	321,440
Operating profit	24,155	23,161	42,209	82,348	79,687
Finance costs	(569)	(370)	(900)	(1,659)	(5,219)
Share of loss of an associate	–	–	–	–	(123)
Profit before taxation	23,586	22,791	41,309	80,689	74,345
Taxation	(2,805)	(1,861)	(4,128)	(12,102)	(6,987)
Profit for the year attributable to the equity holders of the Company	20,781	20,930	37,181	68,587	67,358
Dividends	15,564	8,204	15,041	22,562	15,041
Consolidated assets and liabilities					
Acid patent	8,944	8,278	7,611	6,944	6,278
Property, plant and equipment	58,740	86,417	91,760	101,124	145,604
Land use rights	11,785	11,544	11,303	11,062	25,056
Construction in progress	29,898	24,963	33,646	75,652	136,539
Investment in an associate	–	–	–	–	4,465
Net current assets	75,251	60,275	76,134	88,218	854
Total assets less current liabilities	184,618	191,477	220,454	283,000	318,796
Long-term portion of amount due to shareholders	5,867	–	–	–	–
Long-term bank borrowings	–	–	–	9,000	–
	178,751	191,477	220,454	274,000	318,796
Share capital	68,370	68,370	68,370	68,370	68,370
Reserves	110,381	123,107	152,084	205,630	250,426
Total equity	178,751	191,477	220,454	274,000	318,796
Earnings per share – basic and diluted	Rmb0.035	Rmb0.031	Rmb0.054	Rmb0.100	Rmb0.099



NOTICE OF ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that the 2006 annual general meeting (“AGM”) of Changmao Biochemical Engineering Company Limited (the “Company”) will be held at Lecture Room C, Joint Professional Centre, Unit 1, G/F, The Center, 99 Queen’s Road Central, Hong Kong on 10 May 2007, at 10:00 a.m. for the following purposes:

As ordinary resolution:

1. To consider and approve the Report of the Directors for the year ended 31 December 2006;
2. To consider and approve the Report of the Supervisory Committee for the year ended 31 December 2006;
3. To consider and approve the audited financial statements of the Company and independent auditor’s report for the year ended 31 December 2006;
4. To consider and approve the final dividend distribution proposal for the year ended 31 December 2006;
5. To consider and approve the appropriation to statutory common reserve for the year ended 31 December 2006;
6. To consider and approve the transfer of the balance of the statutory public welfare fund as at 31 December 2006 to statutory common reserve (Note 5);
7. To elect the directors of the third session of the board (“Board”) of Directors, namely Mr. Rui Xin Sheng as the executive Director, Mr. Jiang Jue Jie, Mr. Zeng Xian Biao, Mr. Yu Xiao Ping, Mr. Wang Jian Ping and Ms. Leng Yi Xin as the non-executive Directors, Prof. Ouyang Ping Kai, Prof. Yang Sheng Li and Ms. Wei Xin as the independent non-executive Directors, for a term of three years from 18 June 2007 to 17 June 2010, and to authorise the Board to fix their remuneration (Please see Annex I for the details of candidates for the Directors);
8. To elect the supervisors who are representatives of the shareholders of the Company for the third session of the supervisory committee of the Company, namely Ms. Zhou Rui Juan and Mr. Lu He Xing as the Supervisors, Prof. Gu Jian Xin and Prof. Jiang Yao Zhong as the independent Supervisors, for a term of three years from 18 June 2007 to 17 June 2010, and to authorise the Board to fix their remuneration (Please see Annex 1 for the details of candidates for the Supervisors);

NOTICE OF ANNUAL GENERAL MEETING

9. To consider the re-appointment of 江蘇公証會計師事務所有限公司 (Jiangsu Gongzheng Certified Public Accountants Co., Ltd.) as the People's Republic of China ("PRC") auditors of the Company for the year 2007 and PricewaterhouseCoopers as the international auditors of the Company for the year 2007 and to authorise the Board to fix their remuneration;
10. To transact any other business.

As special resolution:

1. To consider and approve the resolution for the proposed amendments made to certain articles of the Articles of Association of the Company pursuant to the provisions and requirements of the Ministry of Finance of the PRC (Please see Annex 2 for details of the proposed amendments).
2. To consider and pass the following resolution as a special resolution:
 - (a) **“THAT** subject to the limitations imposed by (c) and (d) below and in accordance with the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (“GEM Listing Rules”), the Company Law of the PRC, and other applicable laws and regulations (in each case as amended from time to time), a general unconditional mandate be and is hereby granted to the board of directors to exercise once or more during the “Relevant Period” (as defined below) all the powers of the Company to allot and issue new shares on such terms and conditions the board of directors may determine and that, in the exercise of their powers to allot and issue shares, the authority of the board of directors shall include (without limitation):
 - (i) the determination of the class and number of the shares to be allotted;
 - (ii) the determination of the issue price of the new shares;
 - (iii) the determination of the opening and closing dates of the issue of new shares;
 - (iv) the determination of the class and number of new shares (if any) to be issued to the existing shareholders;



NOTICE OF ANNUAL GENERAL MEETING

- (v) to make or grant offers, agreements and options which might require the exercise of such powers; and
 - (vi) in the case of an offer or issue of shares to the shareholders of the Company, excluding shareholders who are residents outside the PRC or the Hong Kong Special Administrative Region, on account of prohibitions or requirements under overseas laws or regulations or for some other reasons which the board of directors consider expedient;
- (b) upon the exercise of the powers granted under paragraph (a), the board of directors of the Company may during the “Relevant Period” make or grant offers, agreements and options which might require the shares relating to the exercise of the authority there under being allotted and issued after the expiry of the “Relevant Period”;
- (c) the aggregate amount of the Foreign Shares, Domestic Shares and/or overseas listed foreign shares (“H Shares”) to be allotted or conditionally or unconditionally agreed to be allotted (whether pursuant to the exercise of options or otherwise) by the board of directors of the Company pursuant to the authority granted under paragraph (a) above (excluding any shares which may be allotted upon the conversion of the common reserve (公積金) into capital in accordance with the Company Law of the PRC or the Articles of Association of the Company) shall not exceed twenty per cent (20%) of the amount of the Foreign Shares, Domestic Shares and/or H Shares of the Company separately in issue as at the date of passing of this Resolution;
- (d) the board of directors of the Company in exercising the powers granted under paragraph (a) above shall (i) comply with the Company Law of the PRC, other applicable laws and regulations of the PRC, and the GEM Listing Rules (in each case, as amended from time to time) and (ii) be subject to the approvals of the China Securities Regulatory Commission and relevant authorities of the PRC;

NOTICE OF ANNUAL GENERAL MEETING

- (e) for the purposes of this Resolution: “Relevant Period” means the period from the date of the passing of this Resolution until whichever is the earlier of:
 - (i) the conclusion of the next annual general meeting of the Company; or
 - (ii) the date on which the powers granted by this Resolution is revoked or varied by a special resolution of the Company in general meeting;
- (f) the board of directors shall, subject to the relevant approvals of the relevant authorities and the exercise of the power granted under paragraph (a) above in accordance with the Company Law and other applicable laws and regulations of the PRC, increase the Company’s registered capital corresponding to the relevant number of shares allotted upon the exercise of the powers granted under paragraph (a) of this Resolution, provided that the registered capital of the Company shall not exceed 120% of the amount of registered capital of the Company as at the date of passing of this Resolution;
- (g) the board of directors be and they are hereby authorised to amend, as they may deem appropriate and necessary, relevant articles of the Articles of Association of the Company to reflect the change in the share capital structure of the Company in the event of an exercise of the powers granted under paragraph (a) to allot and issue new shares. (see Note 6)

By order of the Board
Rui Xin Sheng
Chairman

The PRC, 23 March 2007



NOTICE OF ANNUAL GENERAL MEETING

Notes:

1. The H share register of shareholders of the Company will be closed from 5 April 2007 to 10 May 2007 (both days inclusive), during which time no transfer of H shares will be effected. The holders of Domestic Share(s), Foreign Share(s) or H share(s) whose name appears on the register of members of the Company at the close of business on 4 April 2007 will be entitled to attend and vote at the AGM. In order to qualify for attending and voting at the AGM, all transfers, accompanied by the relevant share certificates, must be lodged with the Company's H Registrar, Computershare Hong Kong Investor Services Limited, at Room 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, not later than 4:30 p.m. on 4 April 2007.
2. Any holder of Domestic Share(s), Foreign Share(s) or H share(s) entitled to attend and vote at the AGM convened by the above notice is entitled to appoint one or more proxies to attend and vote at the AGM on his behalf. A proxy needs not be a holder of Domestic Share(s), Foreign Share(s) or H share(s) of the Company.
3. A voting proxy form for the AGM is enclosed with the annual report. In order to be valid, the voting proxy form together with the power of attorney (if any) or other document of authority (if any), under which it is signed or a notarily certified copy of the power of attorney or other document of authority must be delivered, in the case of holders of Domestic Share(s) or Foreign Share(s), to the Company's principal place of business in Hong Kong at Room 54, 5/F, New Henry House, 10 Ice Street, Central, Hong Kong, in the case of holders of H share(s), to the Company's H share registrar, Computershare Hong Kong Investor Services Limited at Rooms 1806-1807, 18th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong not less than 24 hours before the time appointed for holding the AGM or any adjournment thereof.
4. Holders of Domestic Share(s), Foreign Share(s) or H share(s) who intend to attend the AGM should complete (without prejudice to their right of attendance) the enclosed reply slip for the AGM and return it, in the case of holders of Domestic Share(s) or Foreign Share(s), to the Company's principal place of business in Hong Kong at Room 54, 5/F, New Henry House, 10 Ice Street, Central, Hong Kong, in the case of holders of H share(s), to the Company's H share registrar, Computershare Hong Kong Investor Services Limited at Rooms 1806-1807, 18th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong on or before 19 April 2007. The reply slip may be delivered by hand, by post or by fax to the number (852) 2865 0990.
5. The purpose of having ordinary resolution number 6 is to transfer the statutory public welfare fund pursuant to the provisions and requirements of the Ministry of Finance of the PRC.
6. The purpose of having special resolution number 2 is to grant a general power to the board of directors to allot and issue new shares subject to applicable laws, regulations and rules.
7. The AGM is expected to take half a day. Shareholders or their proxies attending the meeting should bear their own lodging and traveling costs.

NOTICE OF ANNUAL GENERAL MEETING

Annex 1: Information of Candidates for Directors and Supervisors

Mr. Wang Jian Ping, aged 45, was graduated from Shanghai Jiao Tong University with a bachelor degree in refrigerating engineering in 1983 and subsequently obtained a master degree in thermal engineering from Shanghai Jiao Tong University in 1986. Mr. Wang is currently a deputy general manager of Shanghai Technology Investment Company Limited. Mr. Wang has been a director of the 704 Research Centre, the seventh institute of the China Shipping Company and visiting scholar of the energy department in University of Leeds. Mr. Wang does not have any relationship with any directors, senior management, management shareholders, substantial shareholders, or controlling shareholders of the Company (within the meaning of the GEM Listing Rules). He does not have any interests in the shares of the Company within the meaning of Part XV of the Securities and Futures Ordinance.

Please see the “Profile of Directors, Supervisors and Senior Management” of the 2006 annual report of the Company for biographies of other candidates for the Directors and candidates for the Supervisors.

Each of Mr. Rui Xin Sheng, Ms. Zhou Rui Juan and Mr. Pan Chun will entered into a service agreement with the Company for a term from 18 June 2007 to 17 June 2010. Save as disclosed above, there will be no service contract between the Directors/Supervisors and the Company.

The remunerations payable to the Directors and Supervisors are determined by the Remuneration Committee, with reference to their contribution of time, effort and expertise on the Company’s matters and are as follows:

- (a) Mr. Rui Xin Sheng is entitled to an annual salary (on the basis of 12 calendar months per year) of Rmb800,000 for 2007, subject to adjustment of not more than 10% per annum for each of the subsequent calendar years;
- (b) Each of Ms. Zhou Rui Juan, Mr. Pan Chun and Mr. Lu He Xing is entitled to (in addition to their remuneration in respect of their respective office with the Company which shall not, in any event, exceed Rmb200,000 per annum (without annual adjustment) for each Supervisor) an annual Supervisor’s fee (on the basis of 12 calendar month per year) of Rmb15,000, Rmb6,000 and Rmb6,000 respectively for the calendar year 2007, subject to adjustment of not more than 10% per annum for each of the subsequent calendar years;



NOTICE OF ANNUAL GENERAL MEETING

- (c) Each of the non-executive Directors will for the year 2007 (on the basis of 12 calendar months each year) be paid a Director's fee of Rmb50,000 per annum; each of the independent non-executive Directors will for the year 2007 (on the basis of 12 calendar months each year) be paid a Director's fee of Rmb60,000 per annum; and each of the independent Supervisors will for the year 2007 (on the basis of 12 calendar months each year) be paid a supervisor's fee of Rmb15,000 per annum, subject to an increment of not more than 10% per annum for each of the subsequent years.
- (d) Apart from and in addition to the above salary, each Directors (other than the independent non-executive Directors) and each Supervisor (other than the independent Supervisors) is entitled to an incentive bonus each year, which is determined by the Remuneration Committee with reference to the profitability of the Company and its subsidiary and the market conditions;

Please refer to the paragraph headed "Interest and Short Positions of the Directors, Supervisors or Chief Executives in the Shares, Underlying Shares and Debentures of the Company and its Associated Corporations" in the Report of the Directors contained in the 2006 annual report of the Company for the interests in the shares of Company of the candidates for the Directors and Supervisors within the meaning of Part XV of the Securities and Futures Ordinance.

The Directors believe there is no other matters relating to the election of the third session of the Directors and Supervisors apart from the above that need to be brought to the attention of the shareholders of the Company. There is no information apart from the above which is discloseable pursuant to any of the requirements set out in Rule 17.50(2) of the GEM Listing Rules (particularly in relation to sub-paragraphs (h) to (v) of the rule.)

*NOTICE OF ANNUAL GENERAL MEETING***Annex 2: Details of the proposed amendments to certain articles of the Articles of Association are as follows (Note):**

- (1) Article 151 be amended by deleting its entirety and inserting the following paragraph in its place:

Amended paragraph:

The profit after taxation of the Company are utilised in the following sequence:

- (1) making good the loss;
- (2) making contributions to statutory common reserve;
- (3) paying dividend of preference shares (if any);
- (4) making contributions to discretionary common reserve;
- (5) paying dividend of ordinary shares.

Items (3) to (5) shall be appropriated in certain specific proportions in a year, which shall be formulated by the board of directors subject to the operating conditions and development needs of the Company, and subject to the approval by the general meeting.

- (2) Article 153 be amended by deleting its entirety and inserting the following paragraph in its place:

Amended paragraph:

When allocating the profit after tax for the year, the Company shall contribute ten per cent of the profits to the statutory common reserve. No further contribution to the statutory common reserve is required when its accumulative amount reaches more than fifty per cent of the registered capital of the Company.



NOTICE OF ANNUAL GENERAL MEETING

When the statutory common reserve is insufficient to make good the loss of the Company in prior years, the profit for the year shall be used to make good the loss before making contributions to statutory common reserve in accordance with the above provision.

Contribution to discretionary common reserve can only be made after making contribution to statutory common reserve and subject to resolutions adopted at a general meeting.

The remaining profit after making good the loss and contributions to common reserve(s) will be distributed to shareholders pro rata to their shareholdings.

Any profit distributed to shareholders by general meetings or the board of directors before making good the loss and contribution to the statutory common reserve, which jeopardises the above provision, must be returned to the Company.

- (3) Article 156 be deleted its entirety thereof.

Note: The above is the English translation of the Chinese version of the proposed alternations of the Articles of Association. Should there be any inconsistency between the English version and the Chinese version, the Chinese version shall prevail.