

## **MANAGEMENT DISCUSSION AND ANALYSIS**

### **BUSINESS REVIEW**

The Company was the first organic agricultural business successfully listed on the Main Board of The Stock Exchange of Hong Kong Limited on 15th December, 2000. The Group is an integrated and modernised agricultural enterprise practising in China, applying advanced agricultural technologies and modern organic farming techniques, over 100 species of organic vegetables and fruits are produced in carefully chosen, non-polluted production bases in China. Distribution is carried out through the Group's complete sales network, supported by a comprehensive logistics management system, to both the local and overseas markets. The Group is also engaged in the rice planting and livestock business.

The Directors are pleased to announce the Group's first interim results since its listing on the Main Board. For the six months ended 31st December, 2000, the Group recorded a turnover of RMB284,566,000 representing an increase of 325% as compared to the same period in 1999; profit before taxation was RMB187,429,000 representing an increase of 352% as compared to the same period in 1999; net profit attributable to shareholders was RMB185,777,000 representing an increase of 767% as compared to the same period in 1999; the gross profit margin increased to 75.5% representing an increase of 2.4% point as compared to the same period in 1999; the pre-tax profit margin increased to 65.9% representing an increase of 4.0% point as compared to the same period in 1999; and the net profit margin increased to 65.3% representing an increase of 33.3% point as compared to the same period in 1999.

During the period under review, the Group has been active in establishing production bases in China. Starting from its original production bases in Fujian province, the bases have been extended to Hainan Province, Guangdong Province, Jiangsu Province, Shandong Province, Liaoning Province and Shaanxi Province. The Group increased number of its production bases from 5 as at 30th June, 2000 to 22 as at 31st December, 2000, and its aggregate farmland area of 15,893 Mu (1,060 hectares) as at 30th June, 2000 was increased significantly to 47,830 Mu (3,189 hectares) as at 31st December, 2000. The enlarged production scale had brought to the increase in production volumes and species. With the extension of the sales network to all production bases and nearby cities with high consumer spending, the Group was capable to reach a substantial turnover for the period. The period under review experienced the seasonal cold climate in China, especially in the northern areas, leading to a lower production volume for agricultural produce as compared to the warm seasons in general. As an illustration, the first half-year ended 31st December, 1999 recorded a pro forma combined profit before taxation of RMB41,427,000 (Please refer to the above section "Supplementary Unaudited Financial Information"), contributing to about 45% of the pro forma combined profit before taxation for the previous financial year ended 30th June, 2000.

The Group conducted its export sales by means of direct sales to overseas customers and sales locally to the PRC trading companies. The overseas markets are primarily Japan and Hong Kong. During the review period, the Group recorded sales to the overseas markets (the aggregate of direct sales and sales to trading companies) at approximately RMB101,170,000. Although there was significant growth in sales to the overseas markets at about 3 times as compared to the same period last year, the initial development of the six additional provinces other than the Fujian Province are still mainly serving the domestic markets. Therefore percentage of such sales to the overseas markets to the total sales was about 35 %, as compared to 42% for the same period last year.

The performance of livestock business is also encouraging. The Directors are well aware of the effect of the devastating windstorm in Northern China on the reduction of the supply of the domestic livestock, as well as the recent spread of the “foot and mouth disease” and “mad cow disease” in England and on the European continent. It is emphasised that our imported Boer goats from South Africa have fulfilled all necessary quarantine requirements. After the period end, the Group had established a new pastureland with area of 483 Mu (32 hectares) in Shangdong Province and imported further flock of Boer goats. Together with our experienced breeding techniques, the Board of Directors believe our expansion of the livestock is able to capture the prevailing shortage in market supply.

The Group holds total cash in hand of RMB611,602,000 (of which the balance denominated in Hong Kong dollars amounts to HK\$543,272,000, equivalent to RMB576,629,000) as at 30 June, 2000. During the period under review, the Group utilised partial amounts from the funds raised and internal financial resources to invest in and improve production facilities at the production bases. This included the construction of protection shelters and improving drainage. As a result, for the period ended 31 December 2000, fixed assets and construction expenses increased substantially to RMB55,224,000 and RMB62,028,000, respectively.

The accreditation of vegetable and fruits species from the Group’s current largest production base - Sian You in the Fujian Province, by the Organic Food Development Center of China, further enhances the marketing ability of the produce.

The Group’s research institute continues to recruit high quality academicians and doctorate degree holders to strengthen the research and development team. The Group also cooperates with major research and development entities in China, to accelerate its research efforts.

## **PROSPECTS**

The Board of Directors believes that the Group should carry out improvements at agricultural facilities in production bases while also selecting suitable production bases to enhance production coverage, minimizing the adverse effects from seasonal and regional climatic variations. The Board of Directors also believe that expertise in organic farming is important for the Group’s future development. The Group will continue its commitment to foster and solicit suitable specialist skills to enhance the competitive edge in both domestic and overseas organic agricultural markets.

To complement the two macro-conditions stated above, the Group will speed up its application for the comprehensive international organic food certification for its agricultural produce. It will also publicize the results of its various research and development projects and explore new research and development projects to advance organic farming techniques and development new species.

The Group will also continue its efforts to extend the sales network. In China, the Group will increase its establishment of dedicated retail sales outlets to enhance direct sales to customers, and strengthen the sales channels to complement the primary focus on wholesale markets and institutional customers in the past. In the export market, the Group will actively promote its organic vegetables and fruits to the large department stores, hotels and governmental wholesale markets in Hong Kong, aiming to enhance the recognition of the “Chaoda” brandname by the general public. In Japan, the Group plans to set up its own representative office there to manage the supply of China grown agricultural produce directly to the Japanese customers.

The Board of Directors believes that China’s imminent entry into WTO will bring in positive business opportunities for the Group. Being a domestic organic agricultural producer, the Group can offer a more competitive price than imported produce from overseas. For the export market, the international accreditation of the organic standard of the Group’s produce will accelerate the Group’s entry to the world organic food market. The Group is paving the way in every aspect to capture these business opportunities.

The Group has confidence in its future prospects. It aims to be one of the leading Chinese high-tech organic green agricultural enterprises in the worldwide organic food market and have “Chaoda” branded organic produce to be widely accepted by the general public.