



## MANAGEMENT DISCUSSION AND ANALYSIS

### Instant Noodle Business

Turnover of the Group's core instant noodle segment increased by 7.82% to US\$296 million as compared to same period last year and amounted to 56% of the Group's turnover. The growth was mainly because of the success in product positioning and product differentiation, strengthening the active reform of distribution network, more communication with target consumer group and carrying out different promotion activities. During the period, the Group launched "Gan Bun Mian", "Chao Ling Long" cup noodle and the repackaged Mr.Kon series noodle. Those new products made the brand of Mr.Kon more younger and more fashionable. Thanks for the foundation of "Better Access, Broader Reach" strategy, the Group's low-end noodle also had a good performance.

During the period, the gross margin for instant noodle was 27.82%, a drop by 0.4pp as compared to corresponding period last year. The decline was mainly due to (1) the change of product mix so that the sales growth from low-end noodle was greater than high-end noodle; and (2) higher packaging costs from container noodle to meet the government's environmental regulations.

### Beverage Business

The Group's Green Tea and Ice Tea are the leading brand in the PRC ready-to-drink (RTD) tea market and beverage segment now is the second core business for the Group. Through the modification of product mix and marketing strategy, the Group strengthened the sales resource for "Mr.Kon" juice series to increase the sales for juice product. According to the successful launch for "Wei Chuan Daily C" 100% juice in Shanghai, the Group launched an unrefrigerated, diluted juice series "Fresh Daily C" and gained the great appreciation of consumers. Thanks for the Group's distribution network, "Fresh Daily C" became one of the popular brand in the fast going juice market. During the period, turnover for beverage segment surged by 86.25% to US\$187 million as compared to the same period last year and amounted to 35% of the Group's turnover. Again, beverage sales reached a new record. The Group also launched family size tea drinks and juice to serve restaurant and family. Given Wei Chuan's know-how, the Group launched a live lactobacillus drink "Jian Bai Fen" in June in great Shanghai area. "Jian Bai Fen" will further strengthen the Group's platform in the PRC refrigerated drinks market.

During the period, the gross margin for beverage business was 46.36%, a jump of 5.45pp as compared to the same period last year. This was mainly due to the high utilization rate for PET production line and increase in the proportion of high gross margin PET drinks.

### Bakery Business

Turnover for bakery business increased by 3.39% to US\$40.823 million as compared to the same period last year and amounted to 8% of Group's turnover. The growth was mainly due to the sales increase from "Muffin" in which performance was better than the Group's expectation. As rice cracker was affected by the competition of low prices, the turnover decreased. To improve the operation of bakery business, the Group adjusted product structure, package and favour and promotion method. The Group also linked with one of the famous Taiwan food company - Hunya Foods Co., Ltd. and some international food companies as our strategic partners. Those famous food companies will help to increase the number of the categories in the Group's bakery product. The Group believes that this arrangement will improve the sales of bakery business in the second half of this year. The growth in export market for the bakery product was stable.

During the period, the gross margin for bakery products was 30.52%, fell by 2.48pp as compared to the same period last year mainly because of the lower utilization rate for production line and lower margin for export product.



**Financing**

Expansion of production facilities significantly strengthened the competitiveness of the Group. In June, the Group raised US\$90 million by the issue of convertible bonds which were listed on Luxembourg Stock Exchange. The proceeds were mainly used for the expansion in production capacity of the Group's existing and new production facilities for beverage business.

The remaining principal amount of the Group's 1997 convertible bonds was due on 17th July 2002. The Group has remitted an amount of US\$128.541 million, representing the total amount required to redeem the bonds together with accrued interest on the maturity date to trustee. The trustee paid such funds to the bondholders on the maturity date in accordance with the conditions. Up to the maturity date, none of the bondholders converted the bonds to the Group's shares and there was no change in the number of the Group's existing shares.

As of 30th June 2002, the Group's total liabilities amounted to US\$830 million, representing an increase of US\$250 million from US\$580 million as at 31st December 2001. Total assets amounted to US\$1,384 million. The leverage ratio (total liabilities to total assets) increased by 9.25pp to 59.97% as compared to 31st December 2001. Since most of the Group's transactions were by cash on delivery, the Group has healthy positive cash flow. As of 30th June 2002, the Group had US\$354 million cash on hand, including the remittance of US\$128.541 million to the trustee of the bond. The Group increased long-term and short-term loans by US\$135.266 million to US\$523.926 million as compared to 31st December 2001.

**Financial Ratio**

	<b>As at 30th June 2002</b>	<b>As at 31st December 2001</b>
Finished goods turnover	12.16 Days	13.32 Days
Accounts receivable turnover	13.77 Days	14.45 Days
Current ratio	1.08 Times	0.88 Times
Leverage ratio	59.97%	50.72%
Gearing ratio	0.31 Times	0.40 Times

**Production Scale**

Within the period, the production lines for PET beverage have increased to 27. Out of the 16 new lines, 12 lines have been put in production as of 30th June 2002. The rest of the lines will commence production in July, August and September. During the period between the end of the second quarter and the early third quarter, the Group faced the pressure of excess demand in the PET beverage. With the aim of satisfying the market needs and after careful discussions, the board of directors has approved in July the purchase of other 15 new PET beverage lines and supporting facilities with estimated total investment about US\$68 million. The Group believes that the new lines will commence production after the second quarter in next year. In the first half of 2002, the Group has established two synthetic factories for instant noodle and beverage in ShihHeJi, Xinjiang and Kunming in Yunnan and one beverage factory in Harbin. Those new factories will operate during the period between the end of this year and the first quarter of next year. For bakery business, one new muffin production line has commenced production in the first half of the year. The Group believes that those expansion will benefit the sales of the Group in the second half of the year and in the future.



### **Sales Network**

The result of “Better Access, Broader Reach” of the Group was significantly well in launching new product into market as the access to our customers was improved. Better network control enhanced our goods scheduling. Besides, the Group has strengthened the service towards wholesalers, and established the system of rewards and penalties so that the motivation of the wholesalers was strengthened effectively. On the other hand, the continuous development of overseas market, coupled with the integration of the Group’s logistics system in major cities in the PRC, would help in reducing the cost and increasing the business turnover for the coming seasons of the year.

### **Prospect**

Along with the growth of the PRC’s economy, the increase in income of consumers and their new consumption pattern, the development of PRC’s instant food market will grow further. The Group will make effort to expand the established business market. The Group’s strategies are as follows :

1. Introduce strategic partners to strengthen logistics systems in the PRC;
2. Actively expand refrigerated drinks market share in the eastern part of the PRC to establish the refrigerated product network:
  - (1) Plan to produce “Wei Chuan Daily C” 100% refrigerated juice drinks in Tianjin and Guangzhou beverage factories;
  - (2) To enrich the category of the Group’s refrigerated product by establishing small size model farm in Anji, Zhejiang to enter the dairy industry and give technical support to surrounding dairy farmers;
3. Strengthen and establish the Group’s logistics system to enhance the quality and cost of distribution network;
4. Seek for strategic partners to handle the Group’s supporting business and concentrate on food business;
5. Continue to upgrade production technology and develop basic research;
6. Actively establish a Group-wide ISO standard;
7. Adopt systematic development of manpower resources to strengthen the development and localization of human resources; and
8. Carry out full installation of the SAP computer management and establish the computerization for the logistics system in the major cities in the PRC.