Global Bio-chem Technology Group Company Limited (the "Company") and its subsidiaries (collectively the "Group") are engaged in the manufacture and sale of upstream and downstream corn products. Upstream products include corn starch and other corn refined products. Corn starch is then refined into to wide range of high value-added downstream products including lysine, corn sweeteners and modified starch.

BUSINESS ENVIRONMENT

Despite SARS, the economic growth of the PRC remained stable, which sustained a favourable business environment. Sales in the PRC, our principal market, accounted for approximately 91% (2002: 92%) of the Group's turnover in the first half of 2003 (the "Period"). In the PRC, there is currently no comparable domestic competitor in lysine, a downstream biochemical product. Both modified starch and corn sweeteners faced downward price adjustments owing to domestic competition and low-priced substitutes respectively. For upstream products, increasing competition from domestic manufacturers imposed pressure on price.

To effect a strategic allocation of client base and in view of keen demand from overseas markets, the Group extended its market from the Asian Pacific region to Europe and Africa. During the Period, sales to these new markets recorded an increase, with lysine forming the majority of these exports. This served to alleviate domestic competition and to maintain higher product prices in the PRC.

FINANCIAL PERFORMANCE

The Group's unaudited consolidated turnover of approximately HK$1 billion, gross profit of approximately HK$375 million and net profit of approximately HK$229 million for the Period increased by 51%, 36% and 32% respectively, as compared to figures of 2002. The outstanding performance was mainly derived from the Group's success in the expansion of downstream products and the increase in upstream corn processing capacity last year.

For the downstream product segment, the sales amount, the gross profit and their respective growth rates were approximately HK$420 million, HK$223 million, 16% and 14% respectively. The average gross profit percentage of approximately 53% (2002: 54%) remained stable as compared to 2002. With the expansion in lysine production by 25,000 metric tonnes per annum completed in the second quarter last year, the sales amount of approximately HK$277 million and gross profit of approximately HK$147 million for lysine recorded substantial increases of 73% and 75% respectively during the Period. The market condition of other downstream products, modified starch and corn sweeteners, were less impressive in comparison. Competition from small local suppliers of food-grade modified starch and continuous depression in the price of cane sugar caused a drop in selling prices. As a result, sales of modified starch and corn sweeteners decreased 30% to approximately HK$143 million.

During the Period, the high fructose corn syrup ("HFCS") joint venture recorded an operating loss, of which the portion shared by the Group amounted to approximately HK$0.1 million. It was mainly due to continuous depression in the price of cane sugar in recent years, but the Directors of the Company are confident of a rebound in sugar price in the near future.

In late 2002, the second corn refinery in Changchun commenced commercial production, which then doubled the Group's annual corn processing capacity from 0.6 million metric tonnes to 1.2 million metric tonnes. Despite a drop in average selling price by 4%, the sales of upstream products were approximately HK$615 million, representing an increase of approximately 90% as compared to the previous year. At the same time, the drop in selling price was partially offset by the economies of scale arising from the expansion of capacity and the drop in raw material cost. Thus, the gross profit margin of upstream products remained stable at approximately 25% (2002: 25%) and the gross profit from upstream products of approximately HK$152 million represented an increase of approximately 87% over last year.

Because of the doubling of corn processing capacity, turnover and gross profit from upstream products increased and accounted for 59% (2002: 47%) and 41% (2002: 29%) of the Group's total respectively. Due to the change in sales mix, the overall gross profit margin dropped by approximately 4% to 36%.

Through stringent control over selling and distribution and administrative expenses, the percentage of operating expenses over turnover dropped slightly by approximately 1%. In addition, with the stability of finance costs, taxation and profit shared by minority shareholders over the turnover, the net profit from operating activities attributable to shareholders increased approximately HK$55 million or 32%.

LIQUIDITY AND FINANCIAL RESOURCES

As at 30 June 2003, cash and cash equivalents of the Group amounted to approximately HK$346 million (31 December 2002: HK$433 million). With the increase in bank borrowings of approximately HK$45 million, the net borrowing position rose by approximately HK$132 million. Despite the substantial profit generated from operations of approximately HK$229 million, the change in net borrowing position resulted mainly from (i) the huge capital expenditure incurred during the Period of approximately HK$146 million and (ii) additional working capital tied up after the Group doubled its annual corn refining capacity to 1.2 million metric tonnes in late 2002.

As a result of the inventory level being kept at above normal levels in anticipation of an increase in the price of corn, the inventory turnover days increased further from 94 days as at 31 December 2002 to 105 days as at 30 June 2003. Since most of the raw materials were acquired from farmers on a cash basis, trade creditors turnover days decreased further to 16 days (31 December 2002: 22 days). At the same time, the trade receivables turnover days improved slightly to 76 days (31 December 2002: 84 days). In accordance with the above change, the current ratio and the quick ratio as at 30 June 2003 were approximately 2.3 (31 December 2002: 2.1) and 1.6 (31 December 2002: 1.6) respectively.

As at 30 June 2003, the Group's bank borrowings amounted to approximately HK$520 million (31 December 2002: HK$476 million), of which 26% were denominated in Hong Kong dollars or US dollars while the remainder was in Renminbi ("RMB"). Except for a mortgage loan of approximately HK$14 million repayable in 8 years, the bank borrowings will be wholly repayable in 3 years, with annual interest rates ranging from 3% to 8%. As at 30 June 2003, 76% of bank borrowings was repayable in one year. As at 30 June 2003, certain borrowings were secured by the Group's fixed assets with a carrying value/aggregate net book value of approximately HK$146 million.

The gearing ratios as at 30 June 2003 including bank borrowings over total assets (17%) and bank borrowings over shareholders equity (25%) remained stable as compared to 31 December 2002.

During the Period, the Group did not use any financial instruments for hedging purposes and did not have any hedging instrument outstanding as at 30 June 2003.

PRODUCT DIVERSIFICATION IN ACCELERATION

Protein Lysine and Compound Amino Acids

In view of the strong growth in demand for lysine in the PRC in recent years and over 45% of demand in the PRC currently being met by imports, the Group decided to expand its lysine production capacity in order to capture the rising demand in the market and to enlarge market share.

In July 2003, the Group entered into agreements with a PRC joint venture partner to establish a joint venture company in which the Group will effectively hold 73% equity interest. The scope of business of this joint venture company will include the production and sale of various types of protein lysine and compound amino acids. The production capacity of this joint venture company will be 40,000 metric tonnes of protein lysine and 20,000 metric tonnes of compound amino acids per annum, to be implemented in two phases, while the total investment will amount to US$45 million and will be contributed by the joint venture partners according to their respective equity interest holding percentage.

Modified Starch

To capture the emerging market of modified starch used in the paper-making industry, the first phase of the expansion project on modified starch with an annual capacity of 100,000 metric tonnes is near completion, with the first 60,000 metric-tonne capacity to be launched by the end of 2003 and the remaining 40,000 metric tonnes to be operational by the first quarter of 2004. The second phase, with another 100,000 metric tonnes of annual capacity, is scheduled to commence construction under appropriate market conditions.

HFCS

During the Period, the joint venture vehicle for the HFCS project entered into contracts with international and local beverage bottling plants to supply HFCS to densely populated cities in the PRC. The amount of HFCS to be supplied by the joint venture under the contracts will take up about half of the production capacity of the HFCS refinery.

Sorbitol

The Group signed a Memorandum of Understanding ("MOU") in January with Mitsui Group to set up a joint venture company ("JVC") for the manufacture and sale of sorbitol products in the PRC. According to the MOU, the Group will hold 51% equity interest of the proposed JVC and the total investment on the project is expected to be an amount not exceeding US$15 million, which will be injected by joint venture partners according to their respective equity holding percentage.

Due to the impact of SARS, the negotiation process slowed down in the past few months. Nevertheless, the joint venture agreement is in the finalisation stage and the first sorbitol plant in Changchun, with an annual production capacity of 60,000 metric tonnes, is expected to commence commercial production in 2004.

Third Corn Refinery in Jinzhou

To satisfy the growing demand for corn starch from downstream expansion in terms of volume and variety, the Group entered into an agreement in May 2003 to acquire 70% equity interest in Jinzhou Yuancheng Bio-chem

Technology Co., Ltd. ("Jinzhou Yuancheng"), situated in Jinzhou, Liaoning Province, the PRC, which is mainly engaged in upstream product processing, with an annual capacity of 600,000 metric tonnes. The construction of a corn refinery in Jinzhou was completed in March 2003 and the installation of machineries and equipments is expected to be completed in early 2004. Commercial production is expected to commence in the first quarter of 2004, thereby raising the Group's total corn processing capacity to approximately 1.8 million metric tonnes per annum.

The consideration for the acquisition amounted to approximately HK$75 million, of which approximately HK$49 million will be settled by way of cash and the remaining HK$26 million by way of the allotment and issue of approximately 13 million ordinary shares of the Company ("Share(s)"). Since the equity transfer procedure was still in progress as at 30 June 2003, Jinzhou Yuancheng was not regarded as a subsidiary of the Group for the Period.

Glutamic Acid

With the imminent acquisition of Jinzhou Yuancheng as the second principal production base of the Group, the Directors have decided to start the construction of a glutamic acid plant with an expected annual capacity of 100,000 metric tonnes in Jinzhou in order to maximise the return derived from the vertical integration of both upstream and downstream operations and to gain easy access to southern PRC, the largest market for glutamic acid. It is expected that commercial production will commence in the fourth quarter of 2004.

SHARE OPTIONS TO OTHER CORPORATIONS

During the Period, 23.8 million Shares were subscribed by a wholly owned subsidiary of Cargill, from which approximately HK$38 million were received by the Group pursuant to the exercise of the share option granted thereto. At as 30 June 2003, options granted to that wholly owned subsidiary of Cargill for subscription of 84.2 million Shares remained outstanding, with exercise periods up to April 2005. If these options are fully exercised, an aggregate amount of approximately HK$172 million would be raised, which can enhance the Group's financial position and provides additional resources to the Group for its future development.

NUMBER, REMUNERATION AND RECRUITMENT OF EMPLOYEES

As at 30 June 2003, the Group has approximately 1,400 full time employees in Hong Kong and the PRC. The Group recognises the importance of human resources to its success, therefore qualified and experienced personnel are recruited in the production division as well as the research and development division to enhance production capability and to develop new biochemical products. Remuneration is maintained at competitive levels with discretionary bonuses payable on a merit basis and in line with industry practice. Other staff benefits provided by the Group include mandatory provident fund, insurance schemes and performance related commission.

During the Period, no share options had been granted to any staff. As at 30 June 2003, a total of approximately 116 million share options are outstanding with exercise periods up to 20 August 2011 and exercise prices ranging from HK$0.816 to HK$1.316 per Share.