Global Bio-chem Technology Group Company Limited (the "Company") and its subsidiaries (collectively, the "Group") are engaged in the manufacture and sale of corn based refined products, categorised into upstream and downstream products. Upstream products include corn starch, gluten meal and other corn refined products. Corn starch is then further refined into a variety of high value-added downstream products including amino acids, corn sweeteners and modified starch.

BUSINESS ENVIRONMENT

During the period under review (the "Period"), the momentum for economic growth in the PRC remained strong but subsequently there was overheating appeared in some industries such as automotive, steel, power etc. Consequently, the PRC Government introduced austerity measures against the situation including tightened bank lending and borrowing policies and land use. Some of the enterprises were facing difficult financing environment and tight land supply. Apparently, the impact on the Group's operations was insignificantly 80% of the Group's power consumption was supported by its own power plants. Furthermore, the Group has strong financial resources for capital injection into new projects.

In the Period, the market price of corn kernels rose by around 20% as compared to the same period last year. To have a better cost control on the Group's production, the Group maintained a high corn kernels storage level upon the harvest season in the late 2003, which in fact minimised the impact on the rises in raw material cost. With the growth in upstream product prices, the increased cost of production had been successfully shifted to our customers so the gross profit margin was kept stable. In addition, as a vertically integrated manufacturer, the rise in the price of corn starch imposed insignificant effect on our downstream product production.

Our product diversification strategy had successfully built a wide product portfolio. Currently, there is no comparable domestic competitor of lysine, one of the amino acids, in the PRC. On the other hand, modified starch faced downward price adjustment owing to domestic competition and low-priced substitutes, the utilisation of the corresponding products were then adjusted.

With the PRC remained the Group's principal market, the Group further extended its sales to other regions to achieve a strategic diversification of client base and in view of keen demand from overseas markets. During the Period, sales to regions other than the PRC accounted for approximately 19% (2003: 9%) of the Group's turnover.

FINANCIAL PERFORMANCE

The Group's consolidated turnover of approximately HK$1.5 billion, gross profit of approximately HK$633 million and net profit of approximately HK$421 million for the Period increased by approximately 41%, 69% and 84% respectively, as compared to the same period in 2003.

This outstanding performance was mainly derived not only from the Group's success in the expansion of downstream products but also the substantial increase in lysine price since the fourth quarter of the last year.

Downstream Products Segment

(Sales amount: HK$820 million (2003: HK$420 million))
(Gross profit: HK$476 million (2003: HK$223 million))

During the Period, the sales of amino acids amounted to approximately HK$726 million (2003: HK$276 million) which mainly resulted from (i) the commencement of operation of protein lysine (with expected annual capacity of 80,000 m.t.) in the early 2004 and (ii) the substantial increase in average selling price of lysine by approximately 38% as compared to same period 2003. With such excellent performance of amino acids series, the sales achieved by downstream products segment increased by approximately 95%.

During the Period, the paper-grade modified starch had commenced operation. However, the market condition of modified starch was undesirable due to competition from small local suppliers. Meanwhile the performance of corn sweeteners remained stable during the Period.

Upstream Products Segment

(Sales amount: HK$634 million (2003: HK$615 million))
(Gross profit: HK$157 million (2003: HK$152 million))

Although the selling price of upstream products increased due to the low production yield of corn kernels in the PRC 2003. However, the sales amount of upstream products increased slightly by approximately 3%, which is resulted from the reduction of starch available for external customers because of expanded internal consumption for downstream products.

It is expected that the sales of upstream products will be improved in the second half 2004 with the commencement of the Jinzhou corn processing plant (''Jinzhou Plant'') with annual capacity of 600,000 m.t. in the second half 2004.

Being a mature industry, the gross profit percentage achieved by upstream products segment remained stable during the Period.

Overall Gross Profit %

In view of the expansion of downstream products segment and increase in lysine price during the Period, sales amount from downstream products segment accounted for approximately 56% (2003: 41%) of the Group's turnover. Accordingly, the overall gross profit percentage improved to approximately 44% (2003: 36%).

Operating expenses, loss of jointly-controlled entities, tax and profit shared by minority shareholder

Due to the increase in both overseas sales and transportation cost, the percentage of selling and distribution expenses over turnover increased to approximately 4.0% (2003: 2.8%). In spite of the increase in transportation cost, the percentage of operating expenses over turnover of approximately 6.9% (2003: 7.6%) had improved compared to the same period 2003. Such achievement mainly resulted from the continuous and stringent control over other operating expenses, enhancement in operating efficiency arising from expansion.

To cope with the rapid expansion of the Group's capacity, syndicated loan facilities of US$100 million were raised in September 2003, of which 80% had been utilised at the end of the Period. Therefore, excluding those capitalised as construction in progress of approximately HK$7 million, the finance costs increased to approximately HK$17 million (2003: HK$8 million) which represented approximately 1.1% (2002: 0.8%) to turnover.

During the Period, the high fructose corn syrup (''HFCS'') joint venture (''HFCS JV'') still operated at a loss due to high raw material cost and high transportation charges. Operating loss shared by the Group of approximately HK$3 million had been reflected in the accounts.

With the prevailing income tax laws and regulations, most of the subsidiaries established in the PRC still enjoy income tax relief. As the profit growth rate of subsidiaries, with lower income tax rate, was relatively faster, the overall effective tax rate of the Group reduced to approximately 6.6% (2003: 8.7%).

During the Period, the profit shared by minority shareholder accounted for approximately 12% (2003: 12%) of the profit after tax.

Increase in net profit attributable to shareholders

Combining with the effect of capacity expansion, increase in lysine price and stringent control over operating expenses and finance costs, the net profit attributable to shareholders substantially increased approximately by 84% to HK$421 million.

FINANCIAL RESOURCES AND LIQUIDITY

Net cash position

As at 30 June 2004, cash and cash equivalents of the Group amounted to approximately HK$681 million (31 December 2003: HK$736 million) while the net borrowing increased by approximately HK$168 million. Despite the remarkable profit generated from operation of approximately HK$421 million and proceeds from exercise of share options of approximately HK$121 million, the change in net borrowing position resulted mainly from (i) the huge capital expenditure for the investing activities incurred during the Period of approximately HK$568 million and (ii) additional working capital tied up as a result of the expansion of the Group.

Capital expenditure

In view of the strong operating results and the support from external financing resources, the Group accelerated its expansion plan. During the Period, capital expenditure on non-current assets amounted to HK$568 million, which were mainly used for (i) lysine series in Dehui, (ii) corn processing plant in Jinzhou, (iii) lysine series in Changchun, (iv) sorbitol project in Changchun and (v) polyol project in Changchun. The expenditure for these projects amounted to approximately HK$276 million, HK$148 million, HK$60 million, HK$59 million and HK$25 million respectively. Trial run of polyol had been in progress.

Turnover days, liquidity ratios and gearing ratios

In order to avoid the anticipated upward movement of price in the second half of 2004 and to cope with the demand from Jinzhou corn processing plant which commenced its operation in the second half 2004, the Group intended to keep a high level of corn kernels. As a result, inventory turnover days increased to approximately 119 days (31 December 2003: 91 days). Meanwhile, the trade creditors turnover days increased to approximately 34 days (31 December 2003: 23 days). With the continuous stringent control over trade receivables, trade receivables turnover days remained at approximately 72 days (31 December 2003: 72 days).

In view of the stable operating environment and condition, the current ratio and the quick ratio as at 30 June 2004 remained at similar level as compared to last year and were approximately 2.0 (31 December 2003: 2.1) and 1.5 (31 December 2003: 1.7) respectively.

In view of the stable borrowings structure, gearing ratios in terms of (i) bank borrowings to total assets, (ii) bank borrowings to equity and (iii) net debts (i.e. net balance between bank borrowings and cash and cash equivalent) to equity remained at approximately 25% (2003: 27%), 42% (2003: 45%) and 19% (2003: 16%), respectively. High interest coverage (i.e. profit from operating activities over finance costs) of approximately 32 times (2003: 35 times) reflected that the leverage level remained healthy.

Structure of interest bearing borrowings

As at 30 June 2004, the Group's bank borrowings amounted to approximately HK$1.25 billion (31 December 2003: HK$1.13 billion), of which approximately 54% (31 December 2003: 40%) were denominated in Hong Kong dollars or US dollars while the remainder was denominated in RMB. The average interest rate paid during the Period was approximately 3.8% (2003: 5.2%).

Except for a mortgage loan of approximately HK$12 million repayable in 7 years, the bank borrowings will be wholly repayable in 3 years and approximately 30% (31 December 2003: 45%) of bank borrowings was repayable in one year. As at 30 June 2004, certain borrowings were secured by the Group's fixed assets with a carrying value/ aggregate net book value of approximately HK$260 million (31 December 2003: 280 million).

Foreign Exchange Exposure

Although most of the operations were carried out in the PRC in which transactions were denominated in RMB, the board of directors of the Company (the "Board" or "Directors") opined that there is no unfavourable exposure to foreign exchange fluctuation and that there will be sufficient cash resources denominated in Hong Kong

Dollars for the repayment of borrowings and future dividends. During the Period, the Group did not use any financial instrument for hedging purposes and the Group did not have any hedging instrument outstanding as at 30 June 2004.

PROSPECTS

The Group is ambitious to become one of the leading vertically integrated corn based biochemical product manufacturers in the Asian Pacific Region and then a major player around the world. To achieve this objective, the Group will strive to enlarge its market share and diversify its product mix, as well as to enhance its capability in developing high value-added downstream products through extensive research and development and to strategic business alliances with prominent international market leaders.

Amino Acids Series

The Group strives to become the largest lysine manufacturer in the world in two to three years' time.

In view of the strong growth in global demand for lysine in recent years while over 40% of demand in the PRC is currently being met by imports, the Group, as the greatest domestic lysine supplier, intends to expand our lysine phase production capacity.

Based on the performance achieved during the Period, (i.e. the first half year full scale operation of protein lysine), it is expected that the annual production volume of protein lysine will reach 80,000 m.t. As a result, the Group has an overall amino acid production capacity of 40,000 m.t. lysine and 80,000 m.t. protein lysine.

New Amino Acids Production Base

In order to capture the fast-growing global market and to enlarge its market share ahead of others players, the Group has accelerated its development of lysine production capacity and decided to establish a centralised amino acids production base in Dehui, Jilin Province, the PRC. The Group had commenced the construction work of a lysine plant in this new production base with a total annual production capacity 120,000 m.t. It is expected that trial run of the first phase of this new facility with annual capacity of 60,000 m.t. will fall in early 2005. Then, the total annual lysine production capacity of the Group will reach 240,000 m.t.

With an aim to capture additional share in the international lysine market as well as to achieve well-balanced market coverage and attaining a better gross profit of its products, the Group also increased its export of lysine to overseas markets like US, Europe and Africa. During the Period, lysine with approximately 9,000 m.t. (2003: 2,600 m.t.) was sold to regions other than the PRC, which accounted for over 40% of the Group's lysine production capacity.

Glutamic Acid

In 2003, the Group decided to construct a glutamic acid plant, with annual capacity of 100,000 m.t., adjacent to Jinzhou plant. However, in line with centralisation of amino acids production in Dehui, glutamic acid plant will move to Dehui and the construction will commence in the second half 2004.

On 18 November 2003, the Group entered into a provisional agreement in relation to the acquisition of land use rights for the glutamic acid project in Jinzhou. Due to the change of construction site and pursuant to the terms of the provisional agreement, the agreement had been terminated without any penalties nor claims against the Group.

Polyol Project

In 2003, a joint venture company with overseas partners was established in Changchun engaged principally in the commercialisation of polyol chemicals. A 10,000 m.t. pilot plant was constructed during the Period and trial run had already started.

Polyol chemicals include ethylene glycol, propylene glycol, glycerin, butanediols, etc and can be used in textile, plastic, construction materials, medical, chemical and cosmetic industries. The end products from polyol include polyester fiber, polymer resin and anti-freezer, chemicals applied in production of coatings, PVC stablisers, detergents, paint driers, etc. Traditionally, polyols are refined from petroleum.

In view of insufficient and expensive supply of petroleum in the foreseeable future, the use of agricultural products as raw material of polyol production becomes a feasible solution to cope with the issue. The Group was the pioneer to produce polyol chemicals by using corn starch as principal raw material commercially.

According to the preliminary schedule and subject to results from the pilot plant, annual capacity of 200,000 m.t. commercial production plants will be developed in two phases. The Group is confident that the success in polyol project will generate strong contribution to the Group in the coming future.

Sorbitol Project

Sorbitol is a type of sweeteners applied to food, pharmaceutical and chemical industries and can be used as raw material for polyol production.

During the Period, the Group entered into a joint venture agreement with Mitsui Group to carry out a sorbitol project in the PRC. The project is engaged in the manufacture of sorbitol products in Changchun and sale of these products in the PRC and other regions. Mitsui Group will act as distributor for overseas markets. The Group holds 51% equity interest of the project and the total investment amounting to US$15 million, which had been injected by joint venture partners according to their respective equity holding percentage. The construction work of the refinery, with initial annual production capacity of 60,000 m.t., had commenced and commercial operation is expected to commence in the first half of 2005.

HFCS Project

Under the master agreement with Cargill Inc. (``Cargill''), another HFCS refinery, adjacent to Jinzhou Plant is under consideration. The new refinery will not only relieve the heavy transportation cost as it will mainly serve the nearby customers, but also save production cost through vertical integration. Starch slurry will be supplied by Jinzhou Plant, instead of starch powder adopted by HFCS JV in Shanghai.

Jinzhou Plant

To satisfy the growing demand for corn starch from downstream expansion in terms of volume and variety, the Jinzhou Plant with annual corn processing capacity of 600,000 m.t. acquired in 2003 has commenced its commercial production in the second half of 2004. The Group's total corn processing capacity raised to 1.8 million m.t. per annum. The Jinzhou plant will contribute additional profit in the second half in 2004.

EXERCISE OF SHARE OPTIONS

During the Period, 36.8 million ordinary shares of the Company (''Shares'') were subscribed by a wholly owned subsidiary of Cargill, from which approximately HK$67 million were received by the Group pursuant to the exercise of the share option granted to thereto. At as 30 June 2004, options granted to that wholly owned subsidiary of Cargill for subscription of approximately 47 million Shares remained outstanding, with exercise periods up to April 2005. If these options are fully exercised, an aggregate amount of approximately HK$105 million would be raised, which enhance the Group's financial position and provide additional resources to the Group for its future development.

In addition, 41 million shares options were exercised at a subscription price of HK$1.316 by full time employees of the Company during the Period, from which approximately HK$54 million were received by the Group.

NUMBER AND REMUNERATION OF EMPLOYEES

As at 30 June 2004, the Group has approximately 2,100 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 to strengthen the production capability and development of new biochemical products. Remuneration is maintained at competitive levels with discretionary bonuses payable on a merit basis and in line with industrial practice. Other staff benefits provided by the Group include mandatory provident fund, insurance schemes and performance related commission.

During the Period, no share options were granted to any staff. As at 30 June 2004, a total of approximately 33 million shares options are outstanding with exercisable period up to August 2011 with exercise prices at HK$1.316 per share.