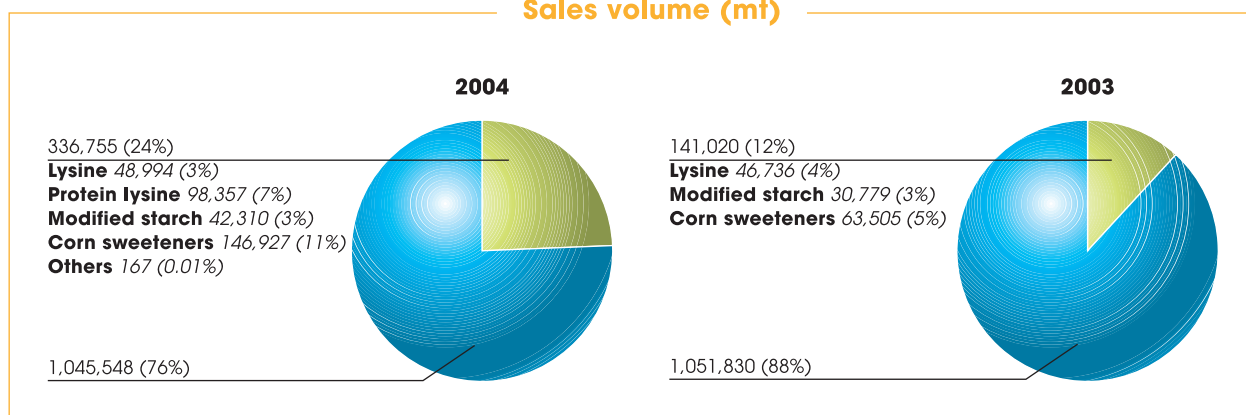


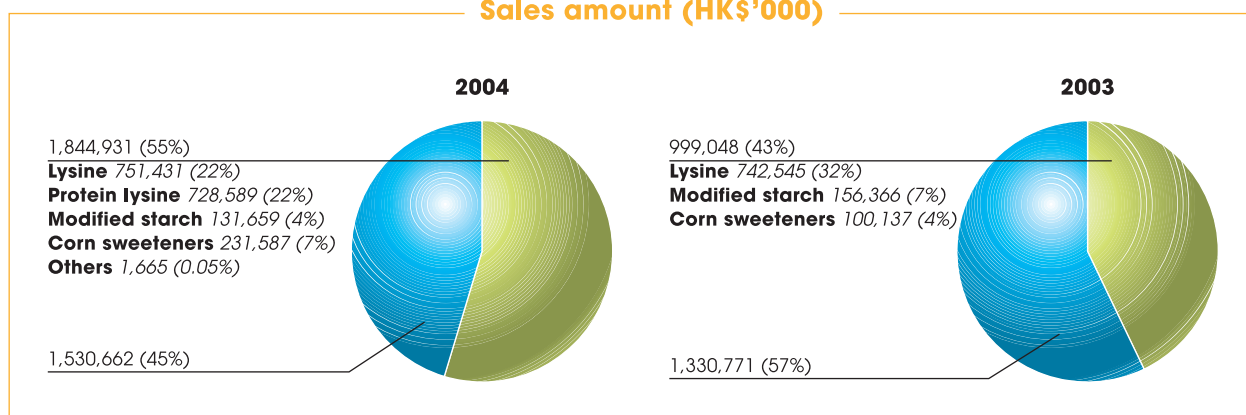
Management Discussion and Analysis

Sales and Gross Profit Analysis

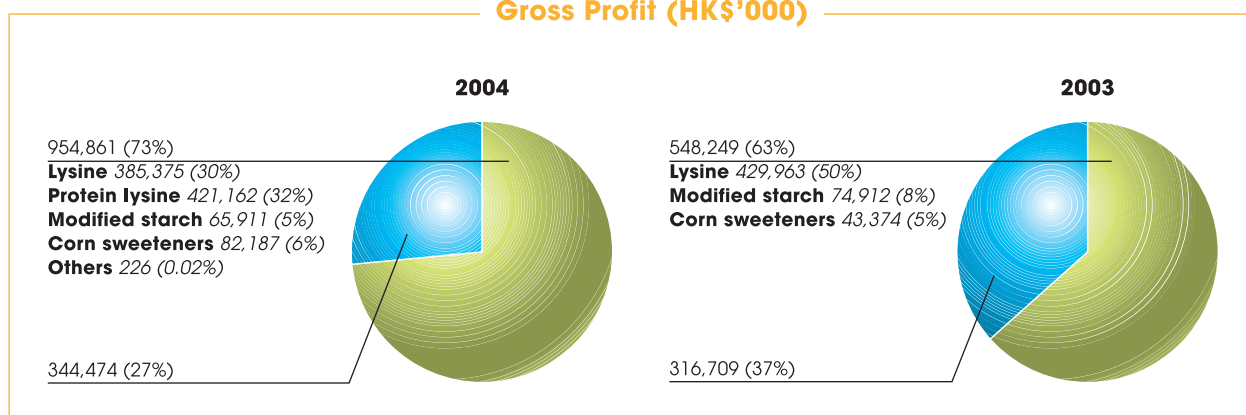
Sales volume (mt)



Sales amount (HK\$'000)



Gross Profit (HK\$'000)



■ Downstream products ■ Upstream products

mt: metric tonne(s)
%: percentage to the Group's total

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 products, categorised into upstream and downstream products. Upstream products, extracted from corn kernels, include corn starch, corn oil, gluten meal and fibres. Corn starch is then further refined, chemically and/or bio-chemically, into a wide range of high value-added downstream products including amino acids, corn sweeteners, modified starch and polyol products.

BUSINESS ENVIRONMENT

During the year under review (the “Year”), the momentum for economic growth in the PRC remained strong but there was overheating appeared in some industries such as automotive, steel, power industry etc. in order to control the situation, the PRC Government introduced austerity measures such as tightened bank lending and borrowing policies and land use. Some of the enterprises were subject to difficult financing environment and tight land supply. However, the impact on the Group’s operations was insignificant as 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 Year, the market price of corn kernels rose by approximately 5% as compared to 2003. In order to control the production cost, the Group maintained a high corn kernels storage level upon the harvest season, which minimised the effect of raw material on the price fluctuation. Part of the increased production cost had been successfully shifted to our customers by raising the prices of upstream products so the gross profit margin was kept stable. In addition, being fully vertically integrated, the rise in the price of corn starch did not cause significant effect on our downstream products production.

The product diversification strategy has successfully widen our product portfolio. During the year, the Group had launched a new series of product — the polyol products into commercial production. The Group became one of the pioneer in the PRC to use renewable resource to replace petroleum to produce such products. For lysine business, the Group maintained as one of the major global players while there is no comparable competitor in the PRC. Both modified starch and corn sweeteners faced downward price adjustment owing to domestic competition and low-priced substitutes, and the utilisation of the corresponding products were then adjusted.

While 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 capture global demand. During the Year, sales to regions other than the PRC accounted for approximately 14% (2003: 7%) of the Group’s turnover.

Management Discussion and Analysis

FINANCIAL PERFORMANCE

The Group's consolidated turnover of approximately HK\$3.4 billion (2003: HK\$2.3 billion), gross profit of approximately HK\$1,299 million (2003: HK\$865 million) and net profit of approximately HK\$815 million (2003: HK\$521 million) for the Year increased by approximately 45%, 50% and 57% respectively, as compared to year 2003. This outstanding performance was mainly derived from the Group's success in the expansion of downstream products.

Downstream Products Segment

(Sales amount: HK\$1,845 million (2003: HK\$999 million))

(Gross profit: HK\$955 million (2003: HK\$548 million))

During the Year, the market price of lysine fluctuated significantly. In the first quarter of the Year, the price of lysine increased to over HK\$25,000 per metric tonne. Since then there were some capacity expansion projects announced to produce lysine both in the PRC and other parts of the world which meant that there would be huge additional supply of lysine in 2005, and as a result the price fell to the lowest of approximately HK\$12,000 per metric tonne in the second half. Consequently, the average selling price of lysine was approximately HK\$15,300 per metric tonne and the performance of lysine operation during the Year remained at a similar level as compared to year 2003.

Commercial production of protein lysine in Changchun was commenced in early 2004 while a corn sweetener plant in Changchun was acquired in the second half of the Year. The turnover generated from these two new sources amounted to approximately HK\$729 million and HK\$147 million respectively, which were in fact the momentum for the increase in sales of downstream products segment in year 2004. Accordingly, the sales and gross profit achieved by downstream products segment increased by approximately 85% and 74% respectively as compared to year 2003.

Although the paper-grade modified starch had commenced operation during the Year, the market condition was undesirable due to competitions from small local suppliers. In addition, some of these production facilities had been used to produce an intermediate raw material for protein lysine. As a result, the performance of modified starch improved slightly during the year.

In the third quarter 2004, the polyol pilot plant in Changchun had commenced its trial run and few hundred metric tonnes polyol products were sold to customers mainly for their trial uses.

FINANCIAL PERFORMANCE (continued)

Upstream Products Segment

(Sales amount: HK\$1,531 million (2003: HK\$1,331 million))

(Gross profit: HK\$344 million (2003: HK\$317 million))

In mid 2004, the Jinzhou corn processing plant has commenced its operation and upstream products of approximately 180,000 metric tonnes were generated during the Year. However, in view of the reduction of corn starch available for external customers because of expanded internal consumption of approximately 1 million metric tonnes for downstream products, the sales volume of upstream products during the Year remained at a similar level as compared to 2003.

An improvement in turnover of upstream products was mainly contributed by the increase in their average selling prices, which was in line with the price increase in corn kernels due to the low production yield of corn kernels in the PRC in the late 2003.

Since the efficiency of Jinzhou corn processing plant had not yet reached its optimal level during the initial production period, the overall gross profit margin of upstream products was pulled down slightly by 1.3%.

Change in sales mix and gross profit mix between upstream and downstream segments

During the Year, sales amount and gross profit of high value-added downstream products accounted for approximately 55% (2003: 43%) and 73% (2003: 63%) of the Group's total turnover and gross profit respectively. The overall gross profit percentage thus improved by approximately 1.4% to approximately 38.5% (2003: 37.1%).

Operating expenses, loss of jointly-controlled entity, tax and profit shared by MI

Owing to the increase in overseas sales and transportation cost, the percentage of selling and distribution expenses over turnover increased by approximately 0.7% to 4.8%. In spite of the increase in transportation cost, the percentage of operating expenses over turnover of approximately 8.3% (2003: 8.7%) remained at a similar level as compared to year 2003. Such performance mainly resulted from the continuous and stringent control over other operating expenses, enhancement in operating efficiency arising from expansion. Arising from the acquisition of production plants during the past few years, goodwill, which is amortised over 20 years, amounting to approximately HK\$677,000 was amortised during the Year and captured under other operating expenses. The rest of other operating expenses included mainly research and developing expenses.

FINANCIAL PERFORMANCE (continued)

Operating expenses, loss of jointly-controlled entity, tax and profit shared by MI (continued)

To cope with the rapid expansion of the Group's capacity and to maintain a healthy gearing level, interest bearing borrowing was still one of the major financing resources. Among those external borrowings, syndicated loan facilities of US\$80 million had been utilised at the end of the Year. In view of a higher borrowing level during the Year, the finance costs, after excluding those capitalised as construction in progress of approximately HK\$17 million, increased to approximately HK\$28 million (2003: HK\$24 million) which represented approximately 1% (2003: 1%) to turnover.

Although the high fructose corn syrup ("HFCS") joint venture ("HFCS JV") still recorded an operating loss of which approximately HK\$1.5 million was shared by the Group for the Year, slim profit was generated since the last quarter in 2004. It is expected that HFCS JV can improve its performance in the near future.

Most of the Group's companies operate either within economic technological development zones or in open costal areas in the PRC, and are enjoying income tax relief according to relevant income tax laws and regulations. Since the profit arising from the operation of protein lysine, one of the high profit margin products of the Group, was free from income tax in two years commencing from year 2004, the effective tax rate of the Group, as a whole, remained at approximately 6% (2003: 7%).

There has been no material change in the shareholding percentage held by minority shareholder in subsidiaries within the Group, so 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 the effect of capacity expansion of lysine series, stringent control over operating expenses and finance costs, the net profit attributable to shareholders substantially increased by approximately 57% to HK\$815 million.

FINANCIAL RESOURCES AND LIQUIDITY

Placement of shares

In mid October 2004, the Company successfully raised additional net proceeds of approximately HK\$830 million through a placement of shares of the Company. It is the intention of the Directors to use such net proceeds for future investment projects including, but not limited to, the building of polyol products production facilities of approximately HK\$500 million, the expansion of production capacity of corn refinery of approximately HK\$200 million, the remaining balance was used for the general working capital of the Group.

Design and foundation work of a new corn refinery with an annual production capacity of 600,000 metric tonnes in Dehui had been commenced during the Year. The expansion in polyol products production will be carried out upon the satisfactory result from the pilot plant in Changchun.

Acquisition of a Sweetener Plant

In the second half of the Year, the Group acquired 75% interest in Changchun Dihao Foodstuff Development Co., Ltd. ("Changchun Dihao"), of which the principal business is the manufacture and sale of a series of corn sweetener products in the PRC. The consideration amounted to approximately HK\$128 million and goodwill of approximately HK\$33 million was resulted which would be amortised over 20 years.

Changchun Dihao currently has corn sweetener production capacity of approximately 500,000 metric tonnes per annum and is considered the largest corn sweeteners manufacturer in the PRC. The huge capacity of Changchun Dihao provides effective and efficient vertical integration support to other downstream products production which involves fermentation process such as amino acids, sorbitol and polyol products. The acquisition can in fact accelerate the development of the Group and help Changchun Dihao become the Group's regional production and distribution center of corn sweetener.

In addition, the acquisition provided the Group a great opportunity to further expand its corn sweetener business in terms of capacity and market share and minimise potential competition in the market.

FINANCIAL RESOURCES AND LIQUIDITY (continued)

Structure of interest bearing borrowings

As at 31 December 2004, the Group's interest bearing borrowings amounted to approximately HK\$1,610 million (2003: HK\$1,133 million), of which 41% (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 Year was 3% (2003: 4%).

The percentage of interest bearing borrowings wholly repayable within one year, in the second to the fifth years and beyond five years were 59% (31 December 2003: 44%), 40% (31 December 2003: 55%), 1% (31 December 2003: 1%) respectively. The change of repayment pattern was mainly attributable to syndicated loan facilities of US\$100 million, of which US\$40 million will be repayable during year 2005.

As at 31 December 2004, certain borrowings were secured by the Group's fixed assets with a carrying value/aggregate net book value of approximately HK\$274 million (31 December 2003: HK\$280 million).

Net borrowing position

Despite the remarkable profit generated from operation, net proceeds from share placement and proceeds from exercise of share options of approximately HK\$815 million, HK\$830 million and HK\$123 million during the Year respectively, the net borrowing position of approximately HK\$367 million (31 December 2003: HK\$397 million) as at 31 December 2004 remained at a similar level as compared to 31 December 2003. It resulted mainly from (i) the huge capital expenditure incurred during the Year of approximately HK\$1.5 billion and (ii) additional working capital tied up against those expansion projects of the Group.

Capital expenditure

In view of the strong operating results, share placement and the support from external financing resources, the Group accelerated its expansion plan. During the Year, capital expenditure on non-current assets amounted to HK\$1.5 billion, which were mainly used for (i) amino acids series in Dehui, (ii) corn processing plant in Jinzhou, (iii) sorbitol project in Changchun, (iv) lysine series in Changchun, (v) acquisition and expansion of a sweetener plant Changchun and (vi) polyol products project in Changchun. The expenditure for these projects amounted to approximately HK\$880 million, HK\$227 million, HK\$59 million, HK\$46 million, HK\$183 million and HK\$44 million respectively.

FINANCIAL RESOURCES AND LIQUIDITY (continued)

Turnover days, liquidity ratios and gearing ratios

Same as previous year, the Group adopted the strategy to keep high raw materials level since the harvest seasons (i.e. fourth quarter) in order to avoid the anticipated upward price movement of corn kernels in the second half of 2005. To support additional raw material demand from Jinzhou and Dehui which commenced operation in mid 2004 and early 2005 respectively, a higher inventory level was kept as at year end date and the inventory turnover days and creditors turnover days increased to 115 days (31 December 2003: 91 days) and 26 days (31 December 2003: 23 days) respectively. Due to continuous depression of lysine price since mid 2004 and additional supply from Dehui in early 2005, extensive promotion campaign with longer credit terms granted to customers were carried out in late 2004 in order to stabilise the market condition in coming future. As a result, trade receivables turnover days extended to 86 days (31 December 2003: 72 days).

As a portion of syndicated loan facilities, amounting to US\$40 million, was reclassified from long term liabilities in year 2003 to current liabilities in year 2004, current ratio and quick ratio as at 31 December 2004 dropped to 1.8 (31 December 2003: 2.1) and 1.4 (31 December 2003: 1.7) respectively.

Because of the share placement that completed during the Year, the gearing level of the Group improved substantially. Those ratios included (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 reduced from 27%, 45% and 16% as at 31 December 2003 to 24%, 39% and 9% as at 31 December 2004 respectively. High interest coverage (i.e. profit from operating activities over finance costs) of 36 times (2003: 28 times) reflected that the leverage level remained healthy.

Foreign Exchange Exposure

Although most of the operations were carried out in the PRC in which transactions were denominated in RMB, the Directors consider 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 Year, the Group did not use any financial instrument for hedging purposes and the Group did not have any hedging instrument outstanding as at 31 December 2004.

Management Discussion and Analysis

PROSPECT

It is the Group's mission 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 realise this objective, the Group will strive to enlarge its market share and diversify its product mix, as well as enhance its capability in developing high value-added downstream products through research and development and through strategic business alliances with prominent international market leaders.

Lysine Series

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

In view of the strong growth in global demand for lysine in recent years while over 40% of demand in the PRC currently being met by imports, certain international and domestic lysine producers, showed their intention to expand their lysine production capacity. In the PRC, the annual feed market size is approximately 100 million metric tonnes with a growth rate of 10% while the content of lysine, as feed additive, is around 1.6 kg per metric tonne. If feed production follows the PRC indicative additive proportion of 3 kg per metric tonne, immediate market demand for lysine is approximately 300,000 metric tonnes per annum. Additional demand is expected if feed production follows the indicative additive proportion according to western countries' preferences of 5-8 kg per metric tonne.

In order to capture the rising demand in the global market and to enlarge its market share ahead of others players, the Group has accelerated its development of lysine production capacity. During the Year, a new lysine plant with a production capacity of 120,000 metric tonnes per annum in Dehui had completed while commercial production was commenced in the early 2005. Then, the annual lysine production capacity of the Group reached around 240,000 metric tonnes.

For stabilising the selling price in the PRC, as well as mitigating the risk of over-concentration in a single market and attaining worldwide recognition of its products, the Group also increased its export of lysine to US, Europe and Africa markets. During the Year, over 15,000 metric tonnes lysine and protein lysine were sold to foreign countries other than the PRC, which accounted for over 10% of the Group's production capacity.

Polyol Products Project

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

PROSPECT (continued)

Polyol Products Project (continued)

In view of the expected insufficient and expensive supply of petroleum in the foreseeable future, the use of renewable resources as raw material of polyol products becomes the feasible remedy to this issue. In 2003, a joint venture company with overseas partners was established in Changchun which engaged principally in the commercialisation of polyol products. A 20,000 metric tonnes pilot plant was constructed during the Year and trial run had started in the third quarter of 2004. The polyol products are currently sold to antifreeze manufacturers and their quality is well recognised in the industry. The Group began to supply them to the polyester industry in early 2005. The Group is one of the pioneers to commercially produce polyol products by using corn starch as principal raw material.

Based on the results of pilot plant and the Group's preliminary development schedule, a 200,000 metric tonnes annual production capacity plant is expected to be built. Such project will become a new driver for the Group's continuous growth.

Sorbitol Project

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

During the Year, the Group entered into a joint venture agreement with Mitsui to carry out a sorbitol project in the PRC. The project is engaged mainly in the manufacture of sorbitol products in Changchun and sale of these products in the PRC and other regions. Mitsui will act as the worldwide distributor except for the PRC market. The Group holds 51% equity interest of the joint venture and the total investment amounts 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 an initial annual production capacity of 60,000 metric tonnes, had been commenced and the commercial production of sorbitol is expected to commence in the second half of 2005.

Glutamic Acid Project

In 2003, the Group decided to construct a glutamic acid plant, with an annual capacity of 100,000 metric tonnes, adjacent to Jinzhou plant. However, the Directors considered that the plant constructed near to the coastal region may create serious environmental pollution. Therefore, the Group had re-selected Dehui for the location of this project with the same planned capacity. The construction work was commenced in the third quarter 2004 and it is expected that the trial run will begin in late 2005 or early 2006.

PROSPECT (continued)

HFCS Project

In addition to the existing HFCS joint venture project between the Group and Cargill incorporated (“Cargill”) in Shanghai, a new HFCS plant situated adjacent to Jinzhou corn processing plant is under consideration. It is expected that the project will enjoy lower cost through vertical integration, and significantly reduce transportation cost due to the close proximity to the customers.

EXERCISE OF SHARE OPTIONS

During the Year, 36.8 million ordinary shares of the Company had been subscribed by a wholly owned subsidiary of Cargill pursuant to the exercise of share options granted thereto, from which HK\$67 million had been received by the Group. At as 31 December 2004, options granted to that wholly owned subsidiary of Cargill for subscription of approximately 47.4 million shares remained outstanding. If these options are fully exercised, an aggregate amount of approximately HK\$105 million would be raised, which can enhance the Group’s financial position and provide additional resources to the Group for its future development.

In addition, during the Year, shares options were exercised at a subscription price of HK\$1.316 by certain full time employees of the Group pursuant to which 42 million shares had been issued by the Company, from which approximately HK\$55 million had been received by the Group.

NUMBER AND REMUNERATION OF EMPLOYEES

As at 31 December 2004, the Group had approximately 3,000 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 capability and development 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 Year, no share options had been granted to any staff. As at 31 December 2004, a total of approximately 32 million shares options were outstanding with exercisable period up to August 2011 at an exercise price of HK\$1.316 per share.