Management Discussion and Analysis

Our turnover surged by 20.4% to RMB852.9 million and net profit attributable to shareholders by 41.4% to RMB175.9 million

Results

The excellent financial results in 2004 were mainly attributable to the growth in sales volume, improving gross margin and relatively stable distribution and general and administrative expenses

Financial year 2004 was a remarkable year for Dynasty. We achieved significant growth in both our turnover as well as net profit attributable to shareholders. Our turnover increased by 20.4% to approximately RMB852.9 million (2003 — RMB708.6 million) and our net profit attributable to shareholders increased by 41.4% to approximately RMB175.9 million (2003 — RMB124.4 million). Earnings per share, on a pro forma basis as if 900,000,000 shares were outstanding since 1 January 2003, was RMB0.20 per share (2003 - RMB0.14 per share). As there was no dilutive potential ordinary share outstanding as at 31 December 2004, dilutive earnings per share is not presented.

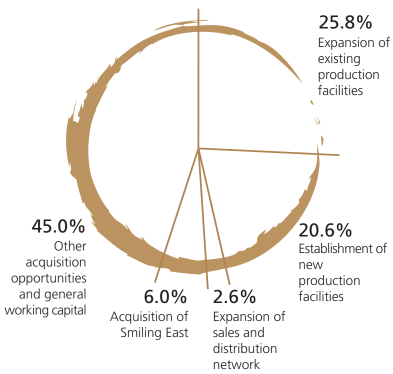
The excellent financial results in 2004 were mainly attributable to the growth in sales volume, improving gross margin and the relatively stable distribution costs and general and administrative expenses.

Initial Public Offering

Placing and Public Offer

During the year, we devoted our efforts in growing our business and preparing for the listing. With the dedication of all our staff, the Group was successfully listed on the Main Board of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") on 26 January 2005. The placing and public offer was well received by institutional and public investors and in particular, the public offer was over subscribed by more than 600 times. Upon the completion of the placing and public offer, we issued a total of 345,000,000 new shares, including the shares issued upon the exercise of the over-allotment option. The gross proceeds raised from the placing and public offer amounted to approximately HK$776.3 million (equivalent to approximately RMB822.8 million). The satisfactory results of the placing and public offer reflected the confidence of investors in the prospects of our business as well as in the grape wine industry of the People's Republic of China (the "PRC"). The listing is a new milestone in the Group's development, laying the foundation for our further growth in the industry.

Use of Proceeds



Use of proceeds

As described in the prospectus of the Company dated 17 January 2005, we intend to use the net proceeds from the placing and public offer -- approximately HK$200.0 million (equivalent to approximately RMB212.0 million) to expand the Group's production capacity, approximately HK$160.0 million (equivalent to approximately RMB169.6 million) to fund partly the establishment of new production facilities, approximately HK$20.0 million (equivalent to approximately RMB21.2 million) to expand the Group's sales and distribution network and approximately HK$47.0 million (equivalent to approximately RMB49.8 million) to fund the acquisition of Smiling East Resources Limited ("Smiling East"). The balance of the proceeds from placing and public offer has been set aside to fund possible acquisitions of complementary wine businesses and as general working capital.

The acquisition of Smiling East was completed on 23 February 2005 at HK$47.0 million (equivalent to approximately RMB49.8 million). We are also in the process to invest the rest of the net proceeds as planned although we have not yet identified any new acquisition targets.

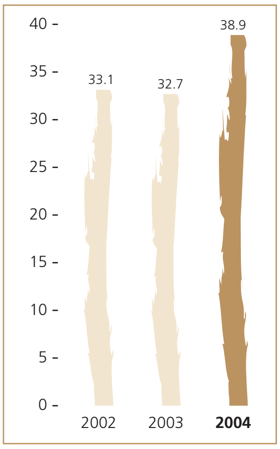
We have placed the unutilised net proceeds in short term bank deposits.

Management Discussion and Analysis

Business Review

Growth of Sales Volume

million bottles (750ml)



Sales analysis

During the year, we recorded remarkable growth in sales volume. The number of bottles of wine sold increased from approximately 32.7 million in 2003 to approximately 38.9 million in 2004, whilst the average ex-factory sale price remained relatively stable. Our principal source of turnover continued to be red wine product sales which accounted for approximately 93.9% of the Group's turnover of the year (2003 - 90.2%). Dynasty Dry Red, the prototype of our mass market product, remained as the Group's best selling wine product, accounting for approximately 50.3% of the Group's turnover (2003 - 50.1%).

During the year, Huadong region, or Eastern region of the PRC, remained as our stronghold market. In the foreseeable future, we believe the sale of grape wine products in provinces in Huadong region will continue to be our major source of turnover. However, we will aim to develop or strengthen the sales of our products in other markets especially those provinces in the northeastern and northwestern regions of the PRC as well as to enhance our marketing and promotion efforts in other coastal provinces in order to boost sales in those markets. Overseas sales remained insignificant at 0.2% (2003 - 0.2%) of our turnover during the year as the domestic market was our primary focus.

We produce and offer over 50 types of wine products focusing on medium to high end segments. With a diversified product portfolio, we believe we will be able to capture the opportunities in the grape wine market in the PRC as it grows and become more mature, manifesting in the surge in demand of premium higher end products. Since 2003, we have launched certain premium wine products such as *Dynasty Dry Red Wine-Aged in Oak Barrels* and *Dry Red and Dry White Wine-Seven-Year Reserve*. During the year, sales of these premium wine products saw encouraging growth. Although sales of these premium wine products made up an insignificant share of our turnover during the year, we believe these products will become an increasingly significant source of our future growth.

Our firm control of quality grape supply underpins strong market positions and future growth

In 2005, we will explore acquisition opportunities of grape wine producers in the PRC and overseas so as to enlarge our product range and market share.

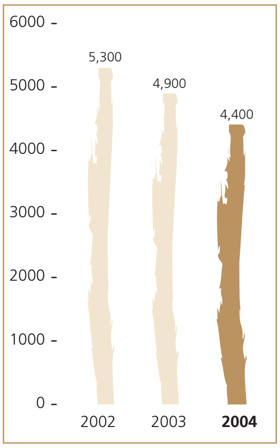
Competition

Competitions come from both local and overseas wine players. With PRC's entry into the World Trade Organisation, import tax on wine products has been decreasing over the past few years. Foreign imported wines are currently subject to 14% import tax. The continuous development of the economy and rising consumption level in the PRC have contributed and will continue to contribute to the healthy growth of the grape wine industry. We believe our reputable brand name, comprehensive product and market knowledge and extensive distribution network will enable us to enhance our competitive advantages to meet all market challenges and to maintain our leading position in this enlarging market.

Supplies of grapes or grape juice

Grapes or grape juice are the key raw materials for grape wine production and access to good quality grapes is the key factor to producing quality wines. We currently have over 10 grape juice suppliers, mainly located in Tianjin, Shandong, Hebei and Ningxia, with whom we have had long term relationships. To ensure adequate supplies of quality grapes and grape juice to support our expected increase in production capacity, we will work with our grape growing partners on enlarging their vineyards to increase harvests and also identify new suppliers who can match our quality requirements. Such measures will enable us to secure grape supplies and lower the risk of our production being interrupted by environment factors, such as seasonality and adverse weather condition, affecting the quality of our grapes. We will also explore acquisition opportunities of grape juice suppliers in the PRC or overseas.

Average Cost of Grape Juice
RMB per tonne



During the year, as a result of abundant grape supplies at lowered prices, the average cost of grape juice decreased from approximately RMB4,900 per tonne in 2003 to approximately RMB4,400 per tonne in 2004. However, based on the prevalent demand and supply situation of grapes or grape juice, we expect the average cost of grape juice to increase in 2005.

Production capacity

The expansion of our production capacity from 30,000 tonnes (equivalent to approximately 40.0 million bottles) to 50,000 tonnes (equivalent to approximately 66.7 million bottles) per annum is well in progress and is expected to be completed around mid-2006. The management will put all its efforts into ensuring the timely, or even early, completion of the project. In 2005, we will also commission a feasibility study on the establishment of a new production facility and we will also identify an appropriate site for that purpose. The new production facility, expected to be completed by the end of 2008, will further increase our production capacity to 70,000 tonnes (equivalent to approximately 93.3 million bottles) per annum.

Quality control

We believe maintaining the high quality of our products is one of the keys to our success. To ensure the quality of our products, we implement a set of quality control standards for our wine products, from grape growing to sourcing of bottles and packaging boxes. Our quality control efforts and high operational and management standards are reflected in the minimal sales returns from our customers and our securing of the ISO9001 accreditation. We will continue to strengthen our controls to ensure the high quality of our products.

Business Outlook

Looking ahead, Dynasty will capitalise on the huge potential of China's wine market to maximise business growth

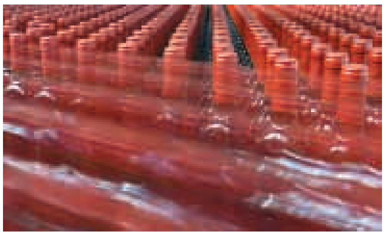
Looking ahead, the Group will capitalise on the surging market demand of grape wine products in the PRC to maximise business growth. Leveraging on our solid foundation, reputable brand name, comprehensive product and market knowledge and extensive distribution network, we will further strengthen our leading position and grow our business in the grape wine market in the PRC. We expect to complete expanding our production capacity from 30,000 tonnes (equivalent to approximately 40.0 million bottles) to 50,000 tonnes (equivalent to approximately 66.7 million bottles) per annum by around mid-2006. The enlarged production capacity will enable us to promptly respond to the surge of market demand.

To fully exploit a market that promises us organic growth, we will also explore appropriate acquisition opportunities in synergy with our business strategies to help us enhancing our shareholders' value. Leveraging on our competitive advantages and sound financial position, we have full confidence in delivering good results in the coming years.

Financial Review

Selected Financial information

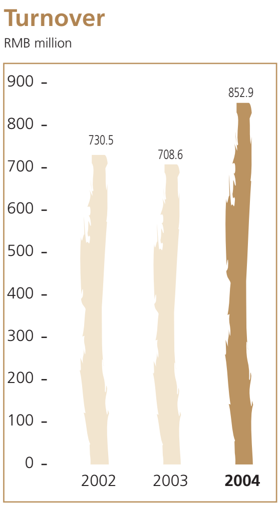
Key components of our financial results as well as other financial and operating data as at and for the year ended 31 December 2004 are extracted or calculated from our proforma accounts as set out on page 71 to 95 of this annual report and presented as follows:



	2004	2003
	RMB'000	RMB'000
Financial results:		
Turnover	**852,907**	708,571
Cost of sales	**(400,361)**	(347,667)
Gross profit	**452,546**	360,904
Distribution costs	**(179,363)**	(158,980)
General and administrative expenses	**(40,437)**	(37,694)
Taxation	**(60,618)**	(46,006)
Profit attributable to shareholders	**175,913**	124,393
Dividends declared in respect of the year	**78,800**	78,805

	2004	2003
Other financial and operating data:		
Sales volume (million bottles)	**38.9**	32.7
Gross profit margin (%)	**53.1**	50.9
Net operating margin (%)	**20.6**	17.6
Return on average equity (%)	**37.5**	26.5
Debtors' turnover (days)	**48**	45
Creditors' turnover (days)	**55**	40
Inventories turnover (days)	**288**	267
Gearing ratio		
— total bank borrowings to shareholders' funds (%)	**3.4**	3.0

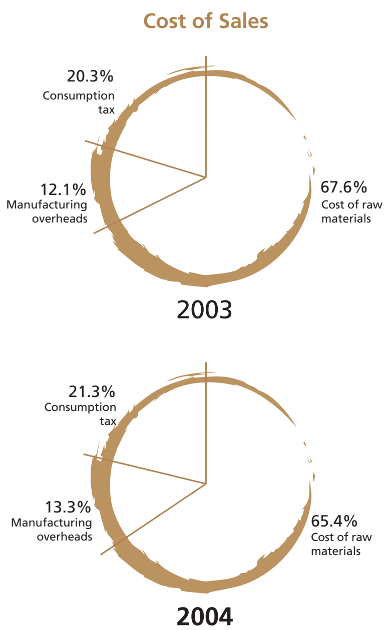
Management Discussion and Analysis



Turnover

During the year, we achieved significant growth in turnover due to increase in sales volume. The Group's turnover grew from approximately RMB708.6 million in 2003 to approximately RMB852.9 million in 2004. The significant turnover surge was partly due to positive growth of the overall grape wine market in the PRC and partly due to the lower comparative base in second quarter of 2003 when our turnover was adversely impacted by the outbreak of Severe Acute Respiratory Syndrome ("SARS").

The Group's average ex-factory sales prices for red and white wine products had been relatively stable during the two years ended 31 December 2004, at approximately RMB22.1 per bottle (750ml) (2003 - RMB22.0). The average ex-factory sales prices of the Group's red wine products are, however, in general higher than the Group's white wine products. With consumers in the PRC having a prevalent preference for red wine products, the Group is able to set higher prices for its red wine products.



Cost of sales

The following table sets forth the major components of our cost of sales:

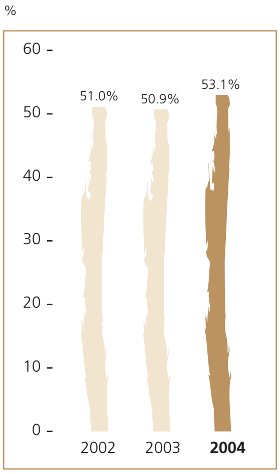
	2004	2003
	%	%
Cost of raw materials		
• Grapes and grape juice	**35.8**	39.6
• Yeast and additives	**1.9**	1.7
• Packaging materials	**26.2**	24.6
• Others	**1.5**	1.7
Total cost of raw materials	**65.4**	67.6
Manufacturing overheads	**13.3**	12.1
Consumption tax	**21.3**	20.3
Total cost of sales	**100.0**	100.0

The major raw materials required by the Group in producing wine products are grapes, or grape juice, yeast and additives and packaging materials. During the year, as a result of abundant grape supplies at lowered prices, the average cost of grape juice decreased from approximately RMB4,900 per tonne in 2003 to approximately RMB4,400 per tonne in 2004. The average cost of packaging materials was relatively stable in 2004 as compared with the preceding year.

Manufacturing overheads consist primarily of depreciation or rental of fixed assets, supplies, utilities, repair and maintenance expenses, salaries and related personnel expenses for the production and related departments and other incidental expenses for production. During the year, manufacturing overheads did not fluctuate significantly as a percentage of our turnover.

The Group is subject to a 10% consumption tax on the invoiced domestic sale amount.

Gross Margin



Gross profit margin

During the year, the overall gross margin attributable to the Group, calculated based on cost of sales inclusive of consumption tax over gross invoiced sales, amounted to approximately 53.1% (2003 - 50.9%) while the gross margin of red wine products and white wine products were 53.9% and 40.1% respectively (2003 - 52.5% and 39.9% respectively). The higher gross margin of the red wine products was attributable to their higher sales prices.

Distribution costs

Distribution costs consist primarily of advertising and market promotion expenses, transportation and delivery charges in connection with the sales of wine products, salaries and related personnel expenses for the sales and marketing department and other incidental expenses. During the year, distribution costs increased in line with the Group's turnover and accounted for approximately 21.0% (2003 - 22.4%) of the Group's turnover. In particular, advertising and market promotion expenses accounted for approximately 13.2% (2003 - 14.7%) of the Group's turnover. We expect advertising and marketing promotion expenses to increase in the foreseeable future to allow the Group to sustain consumer awareness of the "Dynasty" brand and boost sales and also to facilitate the launch of new products. We will, however, strive to keep the increase in line with the increase in turnover of the Group in the foreseeable future.

General and administrative expenses

General and administrative expenses consist primarily of salaries and related personnel expenses for administrative, finance and human resources department, provision for doubtful debts and write off for obsolete inventories, depreciation and amortisation expense and other incidental administrative expenses.

During the year, general and administrative expenses remained relatively stable and accounted for approximately 4.7% (2003 - 5.3%) of the Group's turnover. The Directors expect the Group's general and administrative expenses to increase in 2005 as additional costs in relation to legal, accounting and other requirements applicable to a listed company in Hong Kong will be incurred. However, given the anticipated increase in the Group's turnover, the Directors do not expect the Group's general and administrative expenses to increase significantly as a percentage of turnover.

Effective tax rate for Dynasty in 2004 was approximately 25.6%

Taxation expense

Under the current laws of the Cayman Islands and the British Virgin Islands, neither the Company nor Grand Spirit Holdings Limited is subject to tax on its income or capital gains. In addition, payment of dividends by either company is not subject to withholding tax in those jurisdictions. Pursuant to the PRC law, state enterprise income tax is generally assessed at the statutory rate of 30% of the taxable income. The applicable tax rate for Sino-French Joint-Venture Dynasty Winery Limited ("Dynasty Winery"), our major operating subsidiary, however is 24%, which is the preferential income tax rate for foreign investment production enterprises established in a coastal region. The applicable income tax rate for Shandong Yu Huang Grape Wine Co., Ltd., another subsidiary of the Group, is 30%. During the year, the effective income tax rate of the Group was slightly lowered to approximately 25.6% (2003 - 27.0%).

Dividends

Prior to the Reorganisation and placing and public offer, the board of directors of Dynasty Winery declared a special cash dividend of approximately RMB145.4 million on 8 November 2004. The declaration of dividends was considered a return of investments to the shareholders of Dynasty Winery for their long-term support to the Group. This special dividend, comprising approximately RMB66.6 million in respect of undistributed retained earnings carried forward to 31 December 2003 and RMB78.8 million in respect of the net profit for the year ended 31 December 2004, was attributable to the then equity owners of Dynasty Winery. Approximately RMB66.6 million was paid in December 2004 and the remaining approximately RMB78.8 million was paid in April 2005.

Taking into account of the dividend of approximately RMB78.8 million in respect of the net profit for the year ended 31 December 2003 which was declared on 12 May 2004 and paid in July 2004, the total dividends declared during the year ended 31 December 2004 were approximately RMB224.2 million. All dividends were paid out of the Group's internally generated cash flow from operating activities.

As the Company was recently listed on the Stock Exchange and the Group was not legally established until 13 January 2005, the Directors do not recommend the payment of dividend by the Company for the period from 29 July 2004 (date of incorporation) to 31 December 2004.

Dynasty's exposure to doubtful debt is minimal based on our credit policy

Credit policy

Since 1999, the Group has implemented a policy under which the larger customers, comprising mainly regional distributors, are required to place deposits in accordance with the targeted sales levels upon entering into a sales contract with the Group to enjoy certain credit terms, in general ranging from 30 days to 90 days. Smaller customers, with whom the Group has long-term trading relationships and who have good payment history, are also entitled to, in general, credit terms of 30 days. All other customers are required to pay cash on delivery. Up to 31 December 2004, the Group has received deposits from its customers of approximately RMB90.2 million (2003 - RMB87.8 million). Such amounts are recorded as other payables and accruals and are only refundable upon termination of the sales contracts. In addition, the Group may deduct from the deposit if the customer does not pay for the purchase within the credit period granted and the same customer would have to top up the deposit if it wishes to continue purchasing wine products from the Group. As a result of the Group's credit policy, our exposure to doubtful debt is minimal.

Trade receivables, credit period and debtors' turnover

Trade receivables increased by approximately 30.1% during the year ended 31 December 2004 and amounted to RMB112.5 million (2003 - RMB86.5 million). The increase was primarily a result of substantial increase in sales demand of the Group's wine products in preparation for the Chinese New Year in early 2005. During the year, most customers were given a credit period ranging from one to three months and receivables which are less than three months old accounted for approximately 91.7% of the net trade receivables as at 31 December 2004 (2003 - 100.0%). During the year, debtors' turnover remained relatively stable at approximately 48 days (2003 - 45 days).

Trade payables, payment period and creditors' turnover

Trade payables increased by approximately 58.6% during the year ended 31 December 2004 and amounted to approximately RMB47.9 million (2003 - RMB30.2 million). During the year, payments to most suppliers were subject to a payment period of one to two months reflected in creditors' turnover of approximately 55 days (2003 - 40 days). The higher trade payable balance and creditors' turnover days in 2004 was primarily a result of more purchases of unprocessed wines and packaging materials towards the year end in preparation of the expected increase in sale demand in 2005.

Inventories and inventory turnover

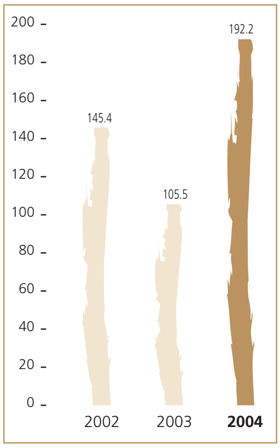
Inventories of the Group increased by approximately 22.5% during the year ended 31 December 2004 and amounted to approximately RMB248.5 million (2003 - RMB202.9 million). Inventories mainly comprise unprocessed wines of approximately RMB99.2 million and finished goods of approximately RMB127.9 million. During the year, inventory turnover was approximately 288 days (2003 - 267 days). The slightly longer inventory turnover period during the year was primarily the result of the general stocking up of unprocessed wines in preparation of the increase in sales demand in 2005.

Cash flow

In 2004, the Group's principal source of cash flow was derived from its operating activities. The Group's cash has principally been applied to fund capital expenditure, to pay dividends to shareholders and to repay an amount due to a former holding company in preparation of the placing and public offer.

Net Cash Generated from Operating Activities

RMB million



The significant increase in cash inflow from operating activities from approximately RMB105.5 million in 2003 to approximately RMB192.2 million in 2004 was primarily attributable to the increase in turnover of the Group, with consumer spending rebounding after the subsidisation of the adverse impact caused by SARS as well as the effects of the changes in working capital, mainly other payables and accruals.

Net cash used in investment activities was primarily attributable to the acquisition of fixed assets pursuant to our expansion plan and amounted to approximately RMB87.9 million (2003 - RMB30.5 million).

Net cash used in financing activities was primarily attributable to the payment of dividends to shareholders of approximately RMB145.4 million (2003 - RMB76.1 million) and the repayment of an amount of approximately RMB41.3 million (2003 - nil) due to a former holding company.

Future dividend will be recommended at approximately 30% to 50% of net profit available for distribution

Dividend policy

We intend to declare and pay dividends in the future. The payment and the amount of any dividends will be recommended by the Directors in accordance with the relevant rules and regulations and dependent on the Group's results of operations, cash flows, financial condition, acquisition opportunities, among others. Subject to the factors described above, the Board of Directors currently intends to recommend at the relevant shareholders' meetings an annual dividend amount at approximately 30% to 50% of the net profit available for distribution to the shareholders in the foreseeable future.

Financial management and treasury policy

As at 31 December 2004, almost all of the Group's assets, liabilities, revenues and expenses are denominated in RMB. Accordingly, there is no significant exposure to foreign exchange fluctuation. With the strong cash and bank balances, we are in a net cash position and thus are exposed to minimal financial risk on interest rate fluctuation.

As at the date of this report, almost all of our cash and bank balances are denominated either in RMB, Hong Kong dollars or United States dollars. The proceeds from the placing and public offer that were not already used for the intended purposes have been placed on short term deposits with authorised financial institutions in Hong Kong. The Group has established an investment policy with the objective of monitoring the investments of the Group's uncommitted funds to ensure the achievement of the highest practicable return on the investments with priority on capital preservation and liquidity.

Capital structure further enhanced after our recent initial public offering

Capital structure

For the year ended 31 December 2004, the Group financed its operations and capital expenditures with its operating cash inflow and did not heavily rely on external borrowings. Upon the completion of the placing and public offer, the net proceeds from our listing further strengthened our capital structure and we expect our cash to be sufficient for meeting our operating and capital expenditure requirements in the foreseeable future.

Capital commitments, contingencies and charges on assets

The Group has made capital expenditure commitments mainly for machineries of approximately RMB14.4 million which are authorised but not contracted for and approximately RMB8.7 million which are contracted but not provided for in the financial statements as at 31 December 2004. These commitments, mainly related to the expansion of the Group's production capacity, are expected to be paid within one year. The funding of such capital commitments will be sourced from the proceeds generated from the placing and public offer, as further disclosed in the section headed "Use of proceeds", or cash flow internally generated from operating activities.

As at 31 December 2004, the Group had no material contingent liabilities and had not pledged any assets.

Mergers and Acquisitions

On 23 February 2005, we completed the acquisition of Smiling East by acquiring its entire issued share capital and shareholder's loan according to the sales and purchase agreement entered into between Tianjin Development Holdings Limited and the Group on 10 January 2005. Accordingly, Tianjin Tianyang Grape Extracting Company Limited, an unprocessed wine producer held by Smiling East, became a 60% owned subsidiary of the Group. We believe the acquisition will enable us to secure stable sources of unprocessed wine for our production.

People are our most important assets and are indispensable to Dynasty's success in the competitive marketplace

Staff and remuneration policies

People are our most important assets and are indispensable to our success in the competitive marketplace. As part of our corporate culture, we strive to ensure a strong team spirit among our employees for them to contribute towards our corporate objectives. In achieving that goal, we offer competitive remuneration packages commensurate with industry level and provide various fringe benefits, including trainings, medical, insurance coverage as well as retirement benefits to all employees in Hong Kong and in the PRC.

As at 31 December 2004, we employed a work force of 352 staff (including Directors) in Hong Kong and the PRC. During the year, the total staff costs amounted to approximately RMB37.1 million (2003 - RMB35.5 million).

The Company also adopted a share option scheme on 6 December 2004 for the purposes of providing incentives and rewards to eligible participants who have contributed to the success of our operations. The Directors may, at their discretion, invite any Directors or employees of the Group and other selected participants, as set out in the scheme, to subscribe for shares of the Company. Up to the date of this report, 23,100,000 share options were granted under the scheme.

Recent Accounting pronouncement

The Group's audited financial statements have been prepared in accordance with accounting principles generally accepted in Hong Kong and comply with Statements of Standard Accounting Practice ("SSAPs") issued by Hong Kong Institute of Certified Public Accountants ("HKICPA"). The HKICPA has announced, as part of its programme to converge with International Financial Reporting Standards, a number of new Hong Kong Financial Reporting Standards and revised Hong Kong Accounting Standards (herein collectively referred to as "new HKFRSs"). The Company has not early adopted these new HKFRSs in the financial statements for the period/year ended 31 December

2004. The Company has already commenced an assessment of the impact of these new HKFRSs but is not yet in a position to state whether these new HKFRSs would have a significant impact on its results of operations and financial position.

To be a socially responsible corporate citizen to the environment

and the community where we operate

Harvesting, Crushing & Pressing,
Fermentation & Separation,
Filtration Processing,
Cold Stabilization & Aging,
Sterilization & Bottling