

Report of the Directors

The Board of Directors (the "Directors") takes pleasure in submitting their interim report together with the unaudited financial statements of the Company and the Group for the six months ended 30 June 2005.

Interim Dividend

The Directors do not recommend the payment of an interim dividend for the six months ended 30 June 2005 (2004: nil).

Share Capital

On 16 June 2005, 257,891,532 ordinary shares of HK\$0.10 each were issued as a result of conversion of convertible instruments amounting to US\$24,663,679 (equivalent to approximately RMB204,636,000).

Directors' Interests, Long and Short Positions in Shares, Underlying Shares and Debentures

As at 30 June 2005, the interests, long and short positions of the Directors and chief executives of the Company in the shares of the Company and associated corporation as recorded in the register required to be kept under Section 352 of the Securities and Futures Ordinance ("SFO") or as otherwise notified to the Company and the Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to the Model Code for Securities Transactions by Directors of Listed Companies (the "Model Code") were as follows:

Name of Director	Company/Name of Associated Corporation	Nature of Interest	Total Number of Ordinary Shares	Percentage of the Company's Issued Share Capital
Niu Gensheng	The Company	Personal Interest	45,505,172(L)	3.33%
	The Company	Corporate Interest (<i>Note 1</i>)	253,292,187(L)	18.51%
	Mengniu	Personal Interest	21,862,810(L)	8.18%
	Mengniu	Personal Interest (<i>Note 2</i>)	7,325,670(S)	2.74%
Lu Jun	Mengniu	Personal Interest	804,646(L)	0.30%
Yang Wenjun	Mengniu	Personal Interest	1,068,646(L)	0.40%
Sun Yubin	Mengniu	Personal Interest	1,772,646(L)	0.66%

Notes:

- (1) These shares are held by Yinniu Milk Industry Limited ("Yinniu"), a substantial shareholder of the Company, and Niu Gensheng by virtue of the Xie Trust has been delegated voting rights to the shares in Yinniu in the Xie Trust. The Xie Trust has been in effect since September 2002 and is a trust declared by Xie Qiuxu in respect of Shares in Yinniu held on trust by him for a selected group of individuals comprising employees and business associates of Mengniu. Xie Qiuxu has similarly delegated the voting rights of his own shares in Yinniu to Niu Gensheng. Together with his personal interest in Yinniu, Niu Gensheng controls 81.7% of the voting rights of Yinniu.

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(2) Out of his share interests in a subsidiary of the Group, Inner Mongolia Mengniu Milk Industry (Group) Co., Ltd. ("Mengniu"), Niu Gensheng granted an option of over 7,325,670 shares in total representing approximately 2.7% of the issued capital of Mengniu to CDH China Fund. L.P., Actis China Investment Company Limited and MS Dairy Holdings ("Financial Investors") on 23 March 2004. Such options can be exercised in one or more tranches by each Financial Investor and are exercisable within 10 years. None of the options have been exercised.

(L) Indicates a long position.

(S) Indicates a short position.

Saved as disclosed above, as at 30 June 2005, none of the Directors or their associates had any interests and short positions in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO).

Substantial Shareholders' Interests

As at 30 June 2005, the interests or short positions of substantial shareholders, other than the Directors of the Company whose interests, long and short positions in the shares of the Company are set out above, in the shares and underlying shares of the Company as recorded in the register maintained under section 336 of the SFO were as follows:

Name of substantial shareholder	Number of shares issued	Percentage of share capital
Xie Qiuxu (<i>Note 1</i>)	253,292,187(L)	18.51(L)
Yinniu (<i>Note 2</i>)	253,292,187(L)	18.51(L)
Jinniu Milk Industry Limited ("Jinniu") (<i>Note 2</i>)	181,997,979(L)	13.30(L)
The Capital Group Companies, Inc.	101,975,000(L)	7.45(L)
Government of Singapore Investment Corporation Pte Ltd	74,364,000(L)	5.43(L)

Notes:

(1) Xie Qiuxu legally owned 62.7% of the issued share capital of Yinniu, which directly owned 18.5% of the Company. Accordingly, the 253,292,187 shares attributable to Xie Qiuxu above represent his indirect effective interest in the Company via his legal shareholding interest in Yinniu.

(2) 10 founding individuals, namely Niu Gensheng, Deng Jiuqiang, Hou Jiangbin, Sun Yunbin, Qiu Lianjun, Yang Wenjun, Pang Kaitai, Lu Jun, Sun Xianhong and Xie Qiuxu, have been acting as a controlling group over the business since its inception in 1999. Therefore, they as a group are controlling shareholders of the Company. As at 30 June 2005, Niu Gensheng, Deng Jiuqiang, Lu Jun, Sun Yubin, Yang Wenjun, Sun Xianhong and Qiu Lianjun who are shareholders of Jinniu together control approximately 81.2% of Jinniu. Niu Gensheng, Xie Qiuxu, Pang Kaitai, Hou Jiangbin and Deng Jiuqiang who are shareholders of Yinniu together control approximately 87.7% of Yinniu. Jinniu and Yinniu in aggregate control approximately 31.8% of the voting power at the general meeting of the Company.

(L) Indicates a long position.

Saved as disclosed above, as at 30 June 2005, no other interests or short positions in the shares or underlying shares of the Company were recorded in the register maintained under section 336 of the SFO.

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Share Option Scheme

The Company adopted a share option scheme to provide incentives to the employees of the Group in June 2005. As at 30 June 2005, no options has been granted.

Purchase, Sale or Redemption of the Company's Listed Shares

During the six months ended 30 June 2005, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities.

Public Float

As at the date of this report, the Company has maintained the prescribed public float under the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules"), based on information that is publicly available to the Company and to the knowledge of the Directors.

Human Resources and Remuneration of Employees

As at 30 June 2005, the Group employed a total of approximately 26,000 employees (30 June 2004: 16,583 employees) in China and Hong Kong. Total staff costs for the first half of 2005 amounted to approximately RMB174,625,000, excluding that for the Directors, as compared with approximately RMB97,903,000 in the corresponding period in 2004.

The Group invests in continuing education and training programs for its management staff and other employees to constantly improve their skills and knowledge. An internal vocational training centre, Mengniu Commercial College, has been set up to develop and implement training programs for the Group's personnel.

Remuneration is maintained at competitive levels with incentive bonuses payable on a merit basis for innovations and improvements which is in line with industry practice. Other staff benefits provided by the Group include a pension contribution plan and insurance schemes.

Foreign Currency Risk

The Group's businesses are principally located in the PRC and all transactions are conducted in RMB, except for the purchases of machinery and equipment and sales to Hong Kong and Macau. As at 30 June 2005, all of the Group's assets and liabilities were denominated in RMB except that cash and cash equivalents of approximately RMB8,067,000 and RMB84,512,000 were denominated in US dollars and Hong Kong dollars, respectively and bank loans of approximately RMB165,530,000 were denominated in US dollars. Management has set up procedures to periodically review and monitor the foreign currency risk exposure.

Pledge of Assets and Contingent Liabilities

Details of assets pledged and contingent liabilities are set out in Notes 10 and 19 to the condensed consolidated financial statements respectively.

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Subsequent Events and Commitments

There was no significant subsequent event. Details of commitments are set out in Note 20 to the condensed consolidated financial statements.

Audit Committee

The audit committee comprises three non-executive Directors, two of whom are independent. The current committee members are Mr Zhang Julin (chairman), Mr Li Jianxin and Mr Jiao Shuge (alias Jiao Zhen). The audit committee has reviewed with the Company management and the external auditors the accounting principles and practices adopted by the Company and discussed auditing, internal control and financial report matters including the review of the unaudited interim financial statements for the six months ended 30 June 2005.

Investor Relations and Communications

The Company adopts a proactive policy in promoting investor relations and communications. Regular meetings are held with institutional investors and financial analysts to ensure two-way communications on the Company's performance and development.

Compliance with the Code on Corporate Governance Practice

Save and except that one of the resolutions which was passed at the Company's annual general meeting held on 28 June 2005 by way of a show of hands rather than by poll as required by the Listing Rules, details of which had been disclosed in an announcement dated 11 July 2005, none of the Directors of the Company is aware of any information that would reasonably indicate that the Company was not at any time during the six months ended 30 June 2005 in compliance with the Code on Corporate Governance Practice as set out by the Hong Kong Stock Exchange in Appendix 14 to the Listing Rules.

Compliance with Model Code

The Company has adopted the Model Code set out in Appendix 10 of the Listing Rules as the Company's code of conduct and rules governing dealings by all Directors in the securities of the Company. Having made specific enquiry of all Directors of the Company, during this reporting period, the Directors of the Company had strictly complied with the Model Code.

By order of the Board of Directors

Niu Gensheng

Chief Executive Officer

Hong Kong, 23 August 2005