A. OVERALL BUSINESS REVIEW

For the year ended 31st December 2005, C.P. Pokphand Co. Ltd. ("CPP" or the "Company") and its subsidiaries ("the Group") achieved a turnaround in business. Profit after tax attributable to equity holders of the Company amounted to US$4.8 million (2004: Loss after tax attributable to equity holders of the Company: US$62.4 million). Basic earnings per share was US$0.182 cent (2004: Loss per share of US$2.890 cents).

During the year under review, CPP's consolidated turnover was US$1,832.8 million, realized a 7.0% gain from US$1,713.0 million in 2004. This growth resulted primarily from the increased sales volume of the Group's core businesses, which are the feed and the food integration business. The consolidated sales volume of the feed business increased by 386,000 tonnes to 4,710,000 tonnes (2004: 4,323,000 tonnes). The Group's vertically integrated food business reported a marked increase in consolidated sales of poultry by 27,000 tonnes, or 15.5%, to 202,000 tonnes, a reflection of growing market demand for poultry and consumers' strong confidence in the Group's products.

The Group's average consolidated gross margin rose from 9.5% to 11.0% this year. The rise was the result of declining prices for major raw materials used in feed production. The average market price of corn and soybean fell 2.0% and 5.8% respectively from 2004. In addition to implementing stringent control over the purchasing costs, the Group also made rapid expansion into its more value-added downstream food products to maximize overall operating efficiency.

Selling expenses in 2005 increased 13.1% when compared with 2004, this rise was due to the increasing emphasis and resources put into promoting the Group's brand equity, as well as strengthening and expanding its sales and distribution networks. In response to the recurring threats of the bird flu epidemic, the Group organized a series of educational seminars and brand promotion events with the aim of allaying any fears or concerns that farmers and consumers might have regarding poultry rearing and to also boost their confidence in the Group's products and its scientific enclosed poultry farming model. The public was educated as to why the scientific closed-environment farm management model is the correct and most effective method in combating the spread of the bird flu disease, and how using the correct and scientific approach in preventing disease can ensure safe, healthy and hygienic products. By investing resources in these initiatives, the Group sustained the trust of its existing customers and at the same time attracted the attention and recognition of potential new customers, thereby paving the way for possible future cooperation and new business.

B. BUSINESS SEGMENT REVIEW

Feed

Riding on the improvement in the external environment and effective integration of internal resources, the feed business recorded robust growth during the year under review. This business segment constituted the largest portion, 65.9% (2004: 63.7%), of the Group's consolidated sales. Turnover increased by US$115.6 million, or 10.6%, to US$1,207.0 million. The average consolidated gross profit margin also increased by 3.0% from that of last year to 14.7%.

Turnover of the feed business improved as a result of recovery of the breeding and rearing industry and adjustments to the product structure, which drove sales. During the year, the combined sales volume of feed of the Group and its jointly controlled entities and associates reached 6,020,000 tonnes, a surge of 9.5% from 5,497,000 tonnes in 2004. The segment boasted market share of 6.0%, the largest in the feed industry in the PRC.

The Group's feed products include poultry, swine, aqua and cattle feed. During the year under review, the largest proportion of sales volume was poultry and swine feed. However, the Group did raise the sales proportion of aqua feed products by 2.0%, as compared with last year.

Food Integration

The food integration business is the Group's second largest business stream, accounting for about 21.7% of the Group's total consolidated turnover. Its consolidated turnover was US$397.2 million, which was US$70.5 million, or 21.6%, more than that in 2004. Growing consumer focus on food safety drove up the consolidated sales volume of the Group's food products by 27,000 tonnes, or 15.5%, to 202,000 tonnes. This reflected the strong confidence of consumers in the Group's branded products.

During the year under review, the combined export of cooked food sales volume reached 49,000 tonnes, an increase of 13,000 tonnes as compared with last year. The Group's advanced and comprehensive quality control and food development mechanisms explained the outstanding performance of its cooked food business. All of the Group's four cooked food processing factories have already obtained export approvals from the government to export cooked poultry products to different countries.

B. BUSINESS SEGMENT REVIEW (continued)

Food Integration (continued)

Rising demand of safety processed egg products widened the price difference between branded eggs and non-branded eggs. In the light of that, the Group set up a standardized demonstration zone in Lanzhou with annual production capability of 2,500 tonnes. All poultry houses are equipped with advanced automatic heating, ventilation and water systems. They adopt enclosed management and are sanitized thoroughly and regularly. The Group also adheres strictly to the country's, as well as, the Group's own immunization and preventive policies. All egg products have to undergo a stringent grading process and the surface of the eggs has to go through ozone sterilization before they are taken to the market. All of these measures meet national standards to ensure food products are free of public health hazards.

Breeding and Rearing

During the year under review, the breeding and rearing business faced both opportunities and challenges. With the livestock farming sector rebounded at the final quarter of 2004, the segment's sales volume and gross profit margin in the first three quarters of the year improved as compared with the same period in 2004. However, as the risk of bird flu escalated in the fourth quarter, the breeding and rearing industry also felt intensified threats. Despite that, the turnover of this business segment, which accounted for 2.4% of the Group's total consolidated turnover, still increased by US$6.3 million, or 16.8%, as compared with last year. Its consolidated gross profit margin also increased from 1.9% to 8.2%.

Taking Day-Old Chicks ("DOCs") as an example, the average price for the year 2004 was RMB1.50 each, while that in the first three quarters of 2005 was RMB2.36 each, a jump of 57.3%. In the fourth quarter of the year, the average price went down to RMB0.93 each. However, the average price of DOCs in 2005 still increased 38.0% to RMB2.07 each when compared with that in 2004. This explained both the growth in turnover and gross profit margin of the segment during the year under review.

The Group stepped up efforts in promoting standardized swine rearing in 2005. It took the initiative to help establish a demonstration zone for standardized swine business in Gao Tai, Gansu province during the year. It succeeded in helping farmers increase swine harvest to approximate three times per annum, which translated into higher return on investment. As of the end of 2005, the Group established 7 demonstration zones for the standardized swine business in the provinces of Gansu, Shaanxi, Henan, Hubei and Hunan. Total sales volume was thereby increased while the gross profit margin remained at a similar level to last year.

B. BUSINESS SEGMENT REVIEW (continued)

Biochemical

Turnover of the biochemical business accounted for 4.8% of the Group's total turnover in the financial year, increased by US$2.1 million, or 2.4%, as compared with last year. The consolidated sales volume slightly reduced by 10,000 tonnes to 126,000 tonnes as compared with 2004. The Group's biochemical products include Chlortetracycline ("CTC"), Di-Calicum Phosphate and L-Lysine monohydrochloride, etc.

Pucheng Chia Tai Biochemistry Co., Ltd. ("Pucheng Chia Tai"), the Group's subsidiary, is currently one of the largest CTC producers in the PRC. Its annual production capability of CTC in different dosages was expanded during the year by 1,000 tonnes to 21,000 tonnes. Its products are mainly exported to the U.S., Europe, South America and Southeast Asia and have won the trust of both domestic and overseas customers. Its "Shihao" brand products are a renowned brand in the international feed additives industry. During the year under review, sales volume of Pucheng Chia Tai increased by 1,400 tonnes to 18,700 tonnes.

Industrial Business

The Group's industrial business is operated by its jointly controlled entities. The product range includes motorcycles, automotive accessories, carburetors and the distribution of the full range of Caterpillar products. For the year ended 31st December, 2005, the combined turnover of the industrial business was US$258.0 million, an increase of US$9.3 million, or 3.7%, as compared with US$248.7 million in 2004.

The "Dayang" brand motorcycle of Luoyang Northern Ek Chor Motorcycle Company Limited, ("Northern Ek Chor") the Group's jointly controlled entity, ranked 285th in the "2005 Top 500 Most Valuable Brands in China" co-organized by "World Brand Lab" and "World Executive Magazine". The motorcycle meets the international standards of developed countries, such as the Euro E-MARK standard and the U.S. DOT authentication, as well as the Euro II standard test. "Dayang" motorcycles have made it into the U.S. and Japan markets. In September 2005, Model DY100-A was the first motorcycle producer in China obtained Certificate for the Exemption of Import and Export Commodities from Inspection issued by General Administration of Quality Supervision, Inspection and Quarantine of the PRC. In addition, the engines produced by Northern Ek Chor were exported to Malaysia for the first time in 2005. Export sales in 2005 accounted for 15% of the segment's total sales volume.

The infrastructure development projects being undertaken in western China are stimulating demand for construction machinery and the Group has been granted the sole agent of Caterpillar construction machinery products there. Braced by all of these favourable factors, continued growth is expected for this segment.

MANAGEMENT'S DISCUSSION AND ANALYSIS

CHANGE OF ASSETS

For the year ended 31st December, 2005, the Group had total assets of US$925.4 million, increasing 3.2% as compared with US$897.1 million at the end of 2004.

LIQUIDITY AND FINANCIAL RESOURCES

Total debt and debt to equity ratio (debt to equity ratio is calculated by dividing the total borrowings by the net asset value) were US$525.4 million and 347.4% respectively, as compared to US$553.9 million and 538.7% as at 31st December, 2004.

Most of the borrowings by the Group are in U.S. dollars and RMB, and the interest rates ranged from 4.7% to 8.4% per annum.

The Group had not engaged in any derivative for hedging against both the interest and exchange rate.

All sales in the PRC are denominated in RMB, and export sales are denominated in foreign currencies. Foreign currencies are required for purchase of imported raw materials, parts and components, and the Group keeps necessary foreign currencies to meet its operational needs.

CAPITAL STRUCTURE

The Group finances its working capital requirements through a combination of funds generated from operations, short term and long term bank loans and from disposal of certain assets and investments. The Group had cash and cash equivalents of US$66.0 million as at 31st December, 2005 (31st December, 2004: US$74.4 million), a decrease of US$8.4 million.

DEBT RESTRUCTURING

In April 2005, the Company secured a US$140.0 million bank loan facility with two banks in Thailand on the condition that the Company has to obtain new equity of US$30.0 million to repay its debts and the floating rate notes. All loans under the restructuring of total amount approximately US$167.7 million were retired by the end of April 2005. The US$140.0 million bank loan facility will be repaid in 14 semi-annual installments over 7 years.

In 2005, the Company repaid US$5.6 million of the principal and US$4.5 million of interest of the US$140.0 million bank loan facility. The average interest rate was 6.3% p.a.

After the restructuring, the Group's total borrowings as at 31st December, 2005, were reduced to US$525.4 million (31st December, 2004: US$553.9 million). Debt to equity ratio was lowered to 347.4%, as compared with 538.7% as at 31st December, 2004. Total liabilities to equity ratio was lowered to 511.9%, as compared with 772.5% as at 31st December, 2004.

CAPITAL REORGANISATION

In April 2005, the nominal value of the Company's issued and paid-up capital was reduced from US$0.05 to US$0.01 by cancelling issued and paid-up capital to the extent of US$0.04 on each issued and paid-up share of the Company.

The credit of US$86.3 million arising from the capital reduction was applied to the contributed surplus account of the Company to eliminate the accumulated losses of the Company.

CHARGES ON GROUP ASSETS

As at 31st December, 2005, out of the total borrowings of US$525.4 million (2004: US$553.9 million) obtained by the Group, only US$143.3 million (2004: US$175.0 million) were secured and accounted for 27.3% (2004: 31.6%) of the total. Certain of the Group's property, plant and equipment and land lease prepayments located in the Mainland China with net book value of US$218.7 million (2004: US$250.0 million) have been pledged as security for various short and long term bank loans.

CONTINGENT LIABILITIES

As at 31st December, 2005, the guarantees provided by the Group was US$7.4 million (31st December, 2004: US$14.4 million).

EMPLOYEE AND REMUNERATION POLICIES

As at 31st December, 2005, the Group employed around 44,000 staff (including 14,000 staff from the jointly controlled entities and associates) in the PRC and Hong Kong. A Remuneration Committee has been set up to review the remuneration policies and packages of directors and senior management. The Group remunerates its employees based on their performance, experience and prevailing market rate while performance bonuses are granted on a discretionary basis. Other employee benefits include insurance and medical cover, subsidized training programme as well as share option scheme.