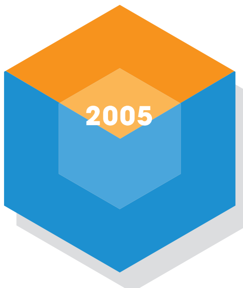
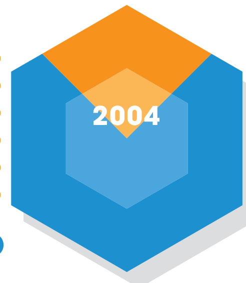
Sales and Gross Profit Analysis

Sales volume (mt)

590,256 (33%)
Lysine *94,793 (5%)*
Protein lysine *148,684 (8%)*
Modified starch *73,708 (4%)*
Corn sweeteners *244,538 (14%)*
HFCS *25,118 (1%)*
Others *3,415(0.09%)*
1,210,634 (67%)



352,890 (25%)
Lysine *48,994 (3%)*
Protein lysine *98,357 (7%)*
Modified starch *42,310 (3%)*
Corn sweeteners *146,927 (11%)*
HFCS *16,135 (1%)*
Others *167 (0.01%)*
1,031,124 (75%)



Sales amount (HK$'000)

2,267,418 (56%)
Lysine *890,963 (22%)*
Protein lysine *668,212 (16%)*
Modified starch *230,755 (6%)*
Corn sweeteners *394,022 (10%)*
HFCS *45,044 (1%)*
Others *38,422 (1%)*
1,811,472 (44%)

1,871,479 (55%)
Lysine *751,431 (22%)*
Protein lysine *728,589 (22%)*
Modified starch *131,659 (4%)*
Corn sweeteners *231,587 (6%)*
HFCS *26,548 (1%)*
Others *1,665 (0.05%)*
1,506,591 (45%)

Gross Profit (HK$'000)

653,016 (62%)
Lysine *223,715 (21%)*
Protein lysine *178,089 (17%)*
Modified starch *107,089 (10%)*
Corn sweeteners *128,701 (12%)*
HFCS *13,539 (1%)*
Others *1,883 (0.02%)*
398,942 (38%)

978,050 (75%)
Lysine *385,375 (30%)*
Protein lysine *438,410 (34%)*
Modified starch *65,911 (5%)*
Corn sweeteners *82,187 (6%)*
HFCS *5,941 (0.5%)*
Others *226 (0.02%)*
323,616 (25%)

Downstream products   Upstream products

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

Global Bio-chem Technology Group Company Limited (the "Company"), its subsidiaries (collectively referred to as the "Group") and its share of each of the jointly-controlled entities are principally 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 wide range of high value-added downstream products including amino acids, corn sweeteners, modified starch and polyol chemical products.

BUSINESS ENVIRONMENT

During the year under review (the "Year"), economic growth of the People's Republic of China (the "PRC") remained strong, which sustained a favorable business environment for the Group.

In view of the high oil price during the Year, the prices of oil-related materials for the production and transportation remained high. This pushed up the production and operating cost of the Group. At the same time, certain type of the Group's products, especially lysine and protein lysine, faced continuous downward price adjustment owing to global oversupply and outburst of animal diseases (e.g. bird flu). Meanwhile, the increasing interest margin of the US dollars also imposed additional pressure on the finance costs of the Group.

Although the PRC remained the principal market, the Group further extended its sales to other regions to effect a strategic allocation of client base and in view of keen demand from overseas markets. During the Year, sales to regions other than the PRC accounted for approximately 19% (2004: 14%) of the Group's turnover.

FINANCIAL PERFORMANCE

The Group's consolidated revenue of approximately HK$4.1 billion (2004: HK$3.4 billion) increased approximately 21% as compared to last year, which mainly resulted from the expansion of the Group's capacity in both upstream and downstream operation in last year. However, due to the continuous price slip of lysine and increase in transportation cost and finance costs, the gross profit of approximately HK$1.1 billion (2004: HK$1.3 billion) and net profit of approximately HK$466 million (2004: HK$815 million) for the Year decreased by approximately 19% and 43% respectively.

Upstream Products Segment

Sales amount: approximately HK$1,811 million (2004: HK$ 1,507 million)
Gross profit: approximately HK$398 million (2004: HK$ 324 million)

Although the internal consumption of corn starch for the production of downstream products increased approximately 91% as compared to prior year, the turnover of upstream products segment increased by approximately 20% to approximately HK$1,811 million. Such outstanding performance mainly resulted from the full scale operation of Jinzhou corn processing plant in 2005.

Although during the Year, costs of sales increased by approximately 19% mainly due to the high utility cost of production, gross profit increased by approximately 23% to approximately HK$398 million which was, as mentioned before, contributed by the additional production capacity. With a substantial portion of the increased cost being successfully passed on to the customers, the gross profit percentage improved slightly by approximately 1%.

As the Group operates in a mature industry, a stable gross profit margin at the current level was within the expectation of the management.

Downstream Products Segment

Sales amount: approximately HK$2,267 million (2004: HK$1,871 million)
Gross profit: approximately HK$653 million (2004: HK$978 million)

During the Year, the sales volume of all types of the downstream products recorded increases of more than 50%.

However, the performance of lysine series was significantly affected by the continuous slip of lysine price. As compared to the prior year, the average selling price dropped by approximately 36% to approximately HK$6,400 per metric tonne. Although the volume sold increased substantially by approximately 65%, only a slight increase in turnover of approximately 5% was recorded while gross profit was dragged down by approximately HK$422 million representing a decrease of approximately 51%.

On the other hand, the cumulative turnover of other downstream products increased over 81% to approximately HK$708 million, which contributed to additional gross profit of approximately HK$97 million as compared to the previous year.

In view of the above, the overall gross profit from downstream products decreased substantially by approximately 33% to HK$653 million.

Overall Gross Profit

Resulted from the continuous fall of lysine prices which was partially compensated by capacity expansion during the Year, sales amount and gross profit from downstream products segment accounted for approximately 56% (2004: 55%) and 62% (2004: 75%) of the Group's turnover and gross profit respectively. Accordingly, the overall gross profit percentage lowered substantially to approximately 26% (2004: 39%).

Operating expenses, tax and profit shared by minority shareholders

Due to the increase in overseas sales and transportation charge, the percentage of selling and distribution expenses over turnover increased to approximately 7% (2004: 5%). In spite of increase in transportation cost, the percentage of operating expenses over turnover only increased slightly to approximately 9% (2004: 8%). Such performance mainly resulted from the continuous and stringent control over other operating expenses, enhancement in operating efficiency arising from expansion.

The increase of finance costs (after netting-off the amount capitalised as construction in progress of approximately HK$37 million (2004: HK$17 million)) over turnover of approximately 2% was mainly attributable to the enlarged borrowing portfolio and the increase in interest rate.

With the prevailing income tax laws and regulations, most of the subsidiaries established in the PRC still enjoy income tax relief. As the profit generated from subsidiaries with lower income tax rate decreased, the overall effective tax rate of the Group was pushed up slightly by approximately 1% to 7% (2004: 6%).

During the Year, the Group entered into an agreement to acquire 100% equity interest in Changchun Dacheng Industrial Group Co., Ltd. ("Dacheng Industrial") at a consideration of HK$900 million. The major assets of Dacheng Industrial mainly included equity interests ranging from 10%–30% in eight subsidiaries of the Company. The transaction was completed in September 2005 and the profit shared by Dacheng Industrial before the completion amounted to approximately HK$74 million (2004: HK$115 million) although portion of the consideration has not yet settled.

The joint venture project with Cagill Inc. ("Cargill") respectively recorded an operating profit of approximately HK$8 million while there was a slim loss from the joint venture project with Mitsui Group during the Year. In view of the recent upward movement of sugar prices and the commencement of production of sorbitol, improvement in operating results of these joint ventures is expected. Due to the adoption of HKAS 31 — interests in joint ventures, the incomes and expenses items, including the comparative figures of last year, of these jointly-controlled entities had been combined on a line-by-line basis in the consolidated financial statements.

Decrease in net profit attributable to shareholders

In view of the decrease in lysine price of which the effect was partially compensated by capacity expansion and stringent control over operating expenses, the net profit attributable to shareholders dropped by approximately 43% to approximately HK$466 million.

IMPORTANT TRANSACTIONS

Acquisition of Dacheng Industrial

During the Year, the Group entered into an agreement to acquire the entire equity interest in Dacheng Industrial at a consideration of HK$900 million. Completion of the acquisition had already been taken place as at the date of this report.

The major assets of Dacheng Industrial mainly comprise minority interests in eight subsidiaries of the Company and certain vacant sites for industrial uses near the main production plant of the Group in Changchun. Through the acquisition, the Group acquired the remaining interests in those subsidiaries held by Dacheng Industrial so that the Group obtained full control of, and financial benefits from, those non-wholly owned subsidiaries and their future expansion plans.

It is the Group's intention to use the lands owned by Dacheng Industrial for the expansion of polyol project and related facilities, including but not limited to, a corn kernel warehouse and a corn processing refinery. The board ("Board") of directors considers that the acquisition would not only enlarge the profit attributable to the shareholders from the Group's well established subsidiaries at relatively lower risk compared with other investment opportunities, but also enhance management's flexibility in managing and integrating the operation of various subsidiaries, thus strengthening the Group's competitive power in the market.

According to HKFRS 3, a goodwill of approximately HK$306 million, which represented the excess of acquisition consideration over Dacheng Industrial's identifiable assets, liabilities and contingent liabilities, was recognised at the date of completion and subject to subsequent impairment reassessment.

In view of the huge capital expenditure incurred in 2005 and the intention to satisfy certain financial covenants of the Syndicated Loan as mentioned below, the management of the Group managed to get the consent from the vendors that part of the consideration amounting to HK$630 million will not be payable before third quarter in 2006 and no interest will be charged.

Syndicated banking facilities

On 2 September 2005, the Company accepted an offer of loan facilities (the "Syndicated Loan") from a syndicate of banks and financial institutions which comprise a term loan facility in the sum of US$120 million and revolving loan facility of up to an aggregate principal amount of US$60 million for a term of 36 and 35 months respectively, both with interest rate equal to London Interbank Offered Rate plus 0.88% per annum.

In view of the huge capital expenditure and additional working capital requirement of various expansion and products development plans, the Syndicated Loan not only provides the Group with additional working capital, but also strengthens the Group's financial capability. In addition, the competitive borrowing costs enhance the Group's profitability and return of equity.

However, in view of mainly the continuous slip of lysine price and increased financial costs, certain financial covenants of the Syndicated Loan cannot be satisfied. Relaxation to these covenants have been proposed. As at the date of this report, unanimous consent from the lenders of the Syndicated Loan for the relaxation of the relevant financial convenants had not yet been obtained. For the sake of prudence, the whole balance of the Syndicated Loan were classified as a current liability so net current liabilities resulted as at 31 December 2005. Risk of insolvency is considered minimal because sufficient and additional financial support had been sought.

Polyol Joint Venture Project

During the Year, the Group entered into a supplemental joint venture agreement with International Polyol Chemicals, Inc. and Icelandic Green Polyols Ehf. (collectively, the "IPP") for the joint construction and operation of a new plant in Changchun with an initial annual production capacity of 200,000 metric tonnes of the polyol chemical products.

Pursuant to the supplemental joint venture agreement, the expected total investment of the joint venture amounts to US$95 million, which would be totally injected by the Group on cash basis while the IPP would make their contribution by way of their technology know-how, as an intangible asset. The Group and the IPP would hold 81.25% and 18.75% of the equity interest in this new joint venture respectively. Under the supplemental joint venture agreement, a call option would be granted by the Group to the IPP pursuant to which the IPP may request the Group to sell to them up to 30.25% equity interest in the joint venture. The call option is exercisable at any time during the term of the supplemental joint venture agreement while the acquisition price shall be determined with reference to the prospective price earning ratio to be determined by a recognised investment banking company or a certified public accounting company and as agreed by the Group and the IPP.

FINANCIAL RESOURCES AND LIQUIDITY

Net Borrowing position

In view of the continuous depression of lysine price, the Group realised that over-dependence on lysine business might affect the stability of operating profit. Thus, new projects of other products accelerated in 2005 and the Board expected that additional income will be generated from those projects in coming years. In order to support the huge capital expenditure on projects including the construction of facilities and/or expansion projects in relation to lysine series, glutamic acids, corn sweeteners, a new corn refinery, other amino acids and enhancement of existing facilities of approximately HK$470 million, HK$640 million, HK$180 million, HK$310 million, HK$75 million and HK$200 million respectively, the net borrowing as at 31 December 2005 increased to approximately HK$996 million (31 December 2004: HK$308 million).

Structure of interest bearing borrowings

As at 31 December 2005, the Group's bank borrowings amounted to approximately HK$3.1 billion (31 December 2004: HK$1.6 billion), of which approximately 48% (31 December 2004: 42%) were denominated in Hong Kong dollars or US dollars while the remainder was denominated in Renminbi ("RMB"). The average interest rate paid during the Year was approximately 4% (2004: 4%). As the interest rate of the Syndicated Loan amounting to US$180 million is on LIBOR basis, the Board expects that there will be increasing pressure in finance costs in 2006.

The percentage of interest bearing borrowings wholly repayable within one year, in the second to the fifth years, and beyond five years were approximately 89% (31 December 2004: 59%), 11% (31 December 2004: 40%) and nil (31 December 2004: 1%) respectively. The change is mainly due to the classification of the whole balance of the Syndicated Loan as a current liability as at 31 December 2005. Save for the re-classification of the whole balance of the Syndicated Loan as a current liability, there has not been any material change in repayment pattern. As at 31 December 2005, certain borrowings were secured by the Group's fixed assets with a carrying value/aggregate net book value of approximately HK$260 million (2004: HK$274 million).

Turnover days, liquidity ratios and gearing ratios

To obtain a better liquidity position and reduce the collection risk of trade receivables, levels of inventories and trade receivables reduced substantially. As a result, the turnover days of inventory and trade receivables shortened to approximately 63 days (31 December 2004: 116 days) and approximately 28 days (31 December 2004: 87 days). In addition, the trade creditors turnover days increased to approximately 38 days (31 December 2004: 27 days).

As a result of the classification of the whole balance of the Syndicated Loan as a current liability and the outstanding consideration for the acquisition of Dacheng Industrial amounting to approximately HK$630 million, the current ratio and the quick ratio as at 31 December 2005 dropped to approximately 0.7 (31 December 2004: 1.9) and 0.6 (31 December 2004: 1.4) respectively. In spite of the unfavorable ratios, the risk of insolvency is considered minimal because sufficient and additional financial support had been sought.

Meanwhile, 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 were pushed up to approximately 33% (31 December 2004: 24%), 65% (31 December 2004: 39%) and 21% (31 December 2004: 8%), respectively. Drop in interest coverage (i.e. EBIDTA over finance costs) to approximately 10 times (2004: 35 times) mainly resulted from the decrease in profit from lysine operation and increase in transportation cost, bank borrowing level and interest rate.

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 unfavorable 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 2005.

PROSPECT

It is the Group's mission to become one of the leading vertically integrated corn based biochemical product manufacturers in the Asia-Pacific Region and one of the major players in the global market. 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

Currently, the Group has annual production capacities of 140,000 metric tonnes of lysine and 220,000 metric tonnes of protein lysine. Although the current consumption of lysine in the PRC had been over 250,000 metric tonnes, overshadowed by the outburst of animal diseases and global oversupply, the price of lysine faced downward adjustment in 2005. The Board believes that the risk for further drop in lysine price is unlikely. Moreover, rebound from the bottom is foreseeable because additional demand arises when feed producers lift up their consumption rate of lysine to follow the western or national countries' indicated additive proportion and have to restore buffer stock.

In addition, in order to stabilise the selling price during the transitional period for the change of the feed formula, to mitigate the risk of over-concentration in a single market and to attain worldwide recognition of the Group's products, the Group enlarged the share of overseas market. During the Year, lysine (including protein lysine) of approximately 50,000 metric tonnes (2004: 15,000 metric tonnes) was exported to regions other than the PRC, which accounted for approximately 21% of the Group's production capacity. The Group intends to further increase its export volume of lysine to markets in the US, Europe and Africa.

Polyol 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 include polyester fiber, polymer resin and anti-freezer, chemicals applied in the production of coatings, PVC stablisers, detergents, paint driers, etc. Usually, polyol chemicals are refined from petroleum. In view of the expected insufficient and expensive supply of petroleum in the foreseeable future, the use of agricultural products as raw material of polyol becomes a feasible remedy to this issue.

The Board is of the opinion that the PRC and other regions in Asia are markets with enormous potential for the polyol chemical products. With the continuing effort in developing the technology of using corn starch as raw materials to produce such chemical products and with quality supply of raw materials, integrated infrastructure and the experience in the development under the pilot plant, further development on this project will generate strong contribution to the Group in the future. The Group will continue to place its effort in the development of the technology and knowhow for the production of polyol products.

Sorbitol Project

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

The 51:49 sorbitol project with Mitsui Group is mainly for the manufacture of sorbitol products in Changchun and sale of these products in the PRC and other regions. Mitsui Group will also act as worldwide distributor except for the PRC market.

The construction work of the sorbitol plant, with initial annual production capacity of 60,000 metric tonnes, has been completed and commercial production has commenced in the late 2005. The Board is considering to develop additional grades and types for sorbitol products.

Glutamic Acid Project and other Amino Acids

The construction of the glutamic acid plant in Dehui has been completed and commercial production also commenced in the first quarter of 2006. The production capacity of this glutamic acid plant is 100,000 metric tones per annum. Synergy effect will be expected by locating the production facilities of lysine and glutamic acid at the same production base, Dehui. To grasp the cost benefits by sourcing corn kernel and producing corn starch locally, construction work of another corn processing plant with sweeteners production capability in Dehui has been commenced in 2005.

The Group is also dedicated to the research and development of many other high value-added amino acids, including arginine, threonine and valine to fuel our growth momentum. The production plant of theronine with annual capacity of 10,000 metric tonnes commenced commercial production in late 2005.

High Fructose Corn Syrup ("HFCS") Project

In addition to the HFCS refinery in Shanghai, a new HFCS refinery, that will invest together with Cargill is under consideration. The new refinery situated adjacent to Jinzhou Plant will relieve the heavy transportation cost because of its close proximity to customers. In addition, unlike Shanghai HFCS refinery using dry starch, starch slurry from the Group's plant at Jinzhou would be used directly for production and further cost will be saved.

SHARE OPTIONS

During the Year, approximately 47 million ordinary shares of the Company were subscribed by a wholly-owned subsidiary of Cargill, from which approximately HK$105 million was received by the Group pursuant to the exercise of the share option granted thereto.

In addition, approximately 32 million share options were exercised during the Year at a subscription price of HK$1.316 by full time employees of the Group, from which approximately HK$42 million was received by the Group. As at 31 December 2005, no share options are outstanding.

NUMBER AND REMUNERATION OF EMPLOYEES

As at 31 December 2005, the Group has approximately 4,300 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 to develop 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.