

## DIRECTORS' REPORT

The board of directors (the "Board") has pleasure in submitting the annual report together with the audited financial statements of First Natural Foods Holdings Limited (the "Company") and its subsidiaries (collectively the "Group") for the year ended 31 December 2005.

### PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding. The principal activities of the Company's subsidiaries are set out in note 1 to the financial statements.

### SEGMENTAL INFORMATION

The analysis of the principal activities and geographical locations of the operations of the Group are set out in note 16 to the financial statements.

### FINANCIAL STATEMENTS

The consolidated income statement of the Group for the year ended 31 December 2005 and the state of the Group's affairs as at that date are set out in the financial statements on pages 33 to 83.

### DIVIDEND

The Board has recommended the payment of a final dividend of HK\$0.015 per share (equivalent to approximately RMB0.0156 per share) for the year ended 31 December 2005 (2004: HK\$0.03 per share (equivalent to approximately RMB0.0318 per share)), subject to members' approval at the forthcoming annual general meeting to be held on 22 June 2006, to the members whose names appear on the Register of Members of the Company on 22 June 2006 and payable on or before 28 June 2006.

No interim dividend was declared for the six months ended 30 June 2005 (2004: Nil).

### CLOSURE OF REGISTER OF MEMBERS

The Register of Members of the Company will be closed from Monday, 19 June 2006 to Thursday, 22 June 2006, both days inclusive, during which period no transfer of shares will be registered. In order to qualify for the final dividend, all completed transfer forms together with the relevant share certificates must be lodged with the Company's share registrar in Hong Kong, namely, Hong Kong Registrars Limited at Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong not later than 4:00 p.m. on Friday, 16 June 2006.

### PROPERTY, PLANT AND EQUIPMENT

Details of the movements in property, plant and equipment are set out in note 17 to the financial statements.

### SHARE CAPITAL

Details of the movements in share capital of the Company are set out in note 29 to the financial statements.

# DIRECTORS' REPORT

## RESERVES

Details of the movements in reserves of the Group and the Company during the year are set out in note 30 to the financial statements.

## PRE-EMPTIVE RIGHTS

There is no provision for pre-emptive rights under the Company's Bye-laws and there is no restriction against such rights under the laws of Bermuda.

## DIRECTORS

The directors of the Company during the year and up to the date of this report were:

*Executive directors:*

Mr. Yeung Chung Lung (*Chairman*)  
Mr. Yang Le (*Chief Executive Officer*)  
Mr. Ni Chao Peng  
Mr. Yip Tze Wai, Albert

*Independent non-executive directors:*

Mr. Tsui Chun Chung, Arthur  
Mr. Lu Ze Jian  
Mr. Leung Chiu Shing

In accordance with bye-law 87 of the Company's Bye-laws, Mr. Yang Le and Mr. Ni Chao Peng will retire by rotation at the forthcoming annual general meeting and, being eligible, offer themselves for re-election.

## DIRECTORS' SERVICE CONTRACTS

Each of Mr. Yeung Chung Lung, Mr. Yang Le, Mr. Ni Chao Peng and Mr. Yip Tze Wai, Albert has entered into a service contract with the Company all dated 17 January 2002, except for Mr. Ni Chao Peng dated 18 January 2002, for a term of one year commencing on 11 February 2002 and shall continue thereafter unless and until terminated by either party giving not less than three months' notice in writing.

Each of Mr. Tsui Chun Chung, Arthur and Mr. Lu Ze Jian has entered into a letter of appointment with the Company for a term of one year commencing on 11 February 2002 and shall continue thereafter unless and until terminated in accordance with the terms and conditions stated in the letter of appointment.

Mr. Leung Chiu Shing has entered into a letter of appointment with the Company for a term of one year commencing on 27 September 2004 and shall continue thereafter unless and until terminated in accordance with the terms and conditions stated in the letter of appointment.

## DIRECTORS' REPORT

Save as disclosed above, none of the directors proposed for re-election at the forthcoming annual general meeting has an unexpired service contract which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

### BIOGRAPHICAL INFORMATION OF DIRECTORS AND SENIOR MANAGEMENT

Brief biographical information of Directors and senior management are set out on pages 14 to 16.

### DIRECTORS' INTERESTS IN COMPETING BUSINESS

During the year ended 31 December 2005, none of the Directors of the Company is interested in any business which competes or is likely to compete, either directly or indirectly, with the business of the Group.

### DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS IN SECURITIES

As at 31 December 2005, the interests and short positions of the Directors and Chief Executives in the shares, underlying shares and debentures of the Company or any associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) as recorded in the register required to be kept under Section 352 of the 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") as set out in the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules") were as follows:

#### Long positions in shares of the Company

Name of Director	Number of ordinary shares			Total	Approximately percentage of issued share capital
	Personal interests	Family interests	Corporate interests		
Yeung Chung Lung	—	—	369,300,000 (Note)	369,300,000	40.21%

Note: Held through Regal Splendid Limited which is wholly-owned by Mr. Yeung Chung Lung.

## DIRECTORS' REPORT

### Long positions in underlying shares of the Company

#### Share Options in the Company

Name of Director	Date of grant	Exercise price HK\$	Exercisable period	No. of shares in respect of options outstanding as at 31 December 2005
Yeung Chung Lung	23/07/2004	0.489	23/07/2004–22/07/2014	3,000,000
Yang Le	23/07/2004	0.489	23/07/2004–22/07/2014	2,000,000
Ni Chao Peng	23/07/2004	0.489	23/07/2004–22/07/2014	2,000,000
Yip Tze Wai, Albert	23/07/2004	0.489	23/07/2004–22/07/2014	1,000,000
Tsui Chun Chung, Arthur	19/01/2005	0.560	19/01/2005–18/01/2015	500,000

Save as disclosed above, none of the directors, chief executives 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) which are recorded in the register required to be kept by the Company under Section 352 of the SFO or which are notified to the Company and the Stock Exchange pursuant to the Model Code.

### SUBSTANTIAL SHAREHOLDERS' INTERESTS IN SECURITIES

As at 31 December 2005, so far as is known to the Directors, the following parties (other than the Directors and Chief Executives of the Company) had interests or short positions in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO:

#### Long positions in shares of the Company

Name	Capacity	Number of ordinary shares	Approximately percentage of issued share capital
Regal Splendid Limited ( <i>Note 1</i> )	Beneficial owner	369,300,000	40.21%
Wisdom Latch Limited ( <i>Note 2</i> )	Beneficial owner	48,197,300	5.25%
Tung Fai ( <i>Note 2</i> )	Beneficial owner	48,197,300	5.25%
Value Partners Limited ( <i>Note 3</i> )	Investment manager	64,555,000	7.03%
Cheah Cheng Hye ( <i>Note 3</i> )	Beneficial owner	1,100,000	7.00%
	Interest of child/ spouse	300,000	
	Corporation	62,935,000	
		<hr/> 64,335,000	

## DIRECTORS' REPORT

### Notes:

1. Regal Splendid Limited is a company incorporated in the British Virgin Islands with limited liability which is legally and beneficially owned as to 100% by Mr. Yeung Chung Lung.
2. Wisdom Latch Limited is a company incorporated in the British Virgin Islands with limited liability which is legally and beneficially owned as to 100% by Mr. Tung Fai.
3. Value Partners Limited is a company incorporated in the British Virgin Islands with limited liability which is owned as to 31.82% by Mr. Cheah Cheng Hye.

### **DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBT SECURITIES**

Other than as disclosed under the headings "Share Option Scheme" and "Directors' and Chief Executives' Interests in Securities", at no time during the year was the Company or any of its subsidiaries, or any of its fellow subsidiaries, a party to any arrangement to enable the Directors or Chief Executives of the Company (including their spouses or children under 18 years of age) to have any right to subscribe for securities of the Company or any of its associated corporations as defined in the SFO or to acquire benefits by means of acquisition of shares in, or debentures of, the Company or any other body corporate.

### **DIRECTORS' AND CONTROLLING SHAREHOLDERS' INTERESTS IN CONTRACTS**

There was no contract of significance in relation to the Company's business, to which the Company or any of its subsidiaries was a party, subsisted at the end of the year or at any time during the year, and in which a Director had, whether directly or indirectly, a material interest, nor there was any other contract of significance in relation to the Company's business between the Company or any of the Company's subsidiaries and a controlling shareholder or any of its subsidiaries.

### **CONNECTED TRANSACTION**

Neither significant related party transactions nor connected transactions under the Listing Rules had entered by the Group during the year ended 31 December 2005.

### **SHARE OPTION SCHEME**

Details of the share option scheme of the Company and movement in share options are set out in note 31 to the financial statements.

### **2.5% COUPON BONDS WITH DETACHABLE WARRANTS**

Details of coupon bonds and movements in warrants are set out in note 25 and 32 respectively to the financial statements.

## DIRECTORS' REPORT

### **PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES**

During the year ended 31 December 2005, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities.

### **BANK LOANS AND OTHER BORROWINGS**

Particulars of bank loans and other borrowings of the Group as at 31 December 2005 are set out in note 24 to the financial statements.

### **DISCLOSURE PURSUANT TO RULE 13.18 OF THE LISTING RULES**

On 1 December 2003, the Company had entered into a facility agreement (the "Facility Agreement") with a syndicate of banks relating to a 3-year term loan facility of up to HK\$60,000,000. Under the Facility Agreement, it would be an event of default if Mr. Yeung Chung Lung, the controlling shareholder of the Company as defined in the Listing Rules, ceases to be the single largest and controlling shareholder of the Company.

As at 31 December 2005, the outstanding amount owed by the Company in respect of this loan facility was approximately HK\$28,500,000 (equivalent to approximately RMB29,640,000).

### **MAJOR CUSTOMERS AND SUPPLIERS**

The information in respect of the Group's sales and purchases attributable to the major customers and suppliers respectively during the financial year are as follows:

	Percentage of the Group's total	
	Sales	Purchases
The largest customer	29%	
Five largest customers in aggregate	72%	
The largest supplier		19%
Five largest suppliers in aggregate		50%

At no time during the year have the directors, their associates or any shareholder of the Company (which to the knowledge of the directors own more than 5% of the Company's share capital) had any interest in these major customers and suppliers.

### **FINANCIAL SUMMARY**

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on page 84 of the annual report.

## RETIREMENT SCHEME

Details of the retirement benefit scheme of the Group and the employer's costs charged to the consolidated income statement for the year ended 31 December 2005 are set out in note 15 to the financial statements.

## MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted the Model Code for Securities Transactions by Directors as set out in Appendix 10 to the Listing Rules as its own code of conduct regarding securities transactions by the directors of the Company (the "Model Code"). Having made specific enquiry of the directors of the Company, all the directors confirmed that they had complied with the required standards as set out in the Model Code during the year ended 31 December 2005.

## INDEPENDENCE OF INDEPENDENT NON-EXECUTIVE DIRECTORS

The Company has received from each of the Independent Non-executive Directors an annual confirmation for independence pursuant to rule 3.13 of the Listing Rules. The Independent Non-executive Directors have confirmed that they are independent.

## PUBLIC FLOAT

On the basis of information that is publicly available to the Company and within the knowledge of the Directors as at the date of this report, the Company has maintained sufficient public float.

## REMUNERATION COMMITTEE

The Board of the Company has established a remuneration committee. The remuneration committee, currently comprising executive director Mr. Yeung Chung Lung, and independent non-executive directors Mr. Tsui Chun Chung, Arthur and Mr. Leung Chiu Shing, is responsible for advising the Board on the remuneration policy and framework of the Company's directors and senior management, as well as review and determine the remuneration of all executive directors and senior management with reference to the Company's objectives from time to time.

## AUDIT COMMITTEE

The audit committee comprises three independent non-executive directors of the Company, namely, Mr. Tsui Chun Chung, Arthur, Mr. Lu Ze Jian and Mr. Leung Chiu Shing. The audit committee is responsible to review the Company's accounting principles and practices adopted by the Group and to discuss auditing, internal control and financial reporting matters with the management. The audited annual financial statements of the Company for the year ended 31 December 2005 have been reviewed by the audit committee.

## POST BALANCE SHEET EVENTS

No significant post balance sheet events of the Group are recorded.

## DIRECTORS' REPORT

### AUDITORS

The financial statements were audited by CCIF CPA Limited, Certified Public Accountants, who will retire at the conclusion of the forthcoming annual general meeting and being eligible, offer themselves for re-appointment. A resolution for the re-appointment of CCIF CPA Limited as auditors of the Company is to be proposed at the forthcoming annual general meeting.

On behalf of the Board

**Yeung Chung Lung**  
*Chairman*

Hong Kong, 25 April 2006