



Strength





Chairman's Statement

Dear Shareholders,

I am pleased to present to you the first annual report of Nine Dragons Paper (Holdings) Limited ("ND Paper" or the "Company") since our listing on the Main Board of the Stock Exchange of Hong Kong Limited (the "Stock Exchange") on 3 March 2006. The year ended on 30 June 2006 marked the 10th anniversary of the operation of ND Paper and its subsidiaries (the "Group") in China. During the year, our leadership in the packaging paperboard manufacturing industry further strengthened as our business continued to expand rapidly with flying colours.

During the year under review, the Group harvested encouraging results with substantial growth in both turnover and profit compared with the last financial year. Our operating infrastructure grew rapidly and our financial performance showed positive results in line with our expansion strategy. For the year, we recorded total revenue and gross profit of approximately RMB7,902,156,000 and RMB1,860,874,000 respectively, representing an increase of 63.8% and 1.45 times over last year. Net profit attributable to equity holders of the Company was RMB1,374,782,000, an increase of 3.53 times from a year ago and was higher than the profit forecast of 30.9% stated in the listing prospectus issued by the Company on 20 February 2006 (the "Prospectus"). Our earnings per share were RMB0.41, representing 3.02 times increase over last year.

Even more encouraging is the huge success of our listing on the Stock Exchange on 3 March 2006 that received an overwhelming market response. This is an important milestone of the Group's business development. In addition, on 1 September 2006, we were added by MSCI Barra to the MSCI Standard Index Series and MSCI Global Value and Growth Index Series. We also became a constituent stock of the Hang Seng Composite Index on 11 September 2006.

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Our insightful and forward-looking management initiated first mover advantage to actively seek investment opportunities in the early 1990s and accelerate the growth of production capacity by expanding the production facilities of the Group. The advanced production equipment and technology adopted by the Group also enabled it to meet the international environmental protection standards. More recently, the Group made huge pre-investments in Dongguan and Taicang, such as developing piers and increasing land reserves, in order to build a solid foundation for the Group's future expansion. What we have achieved today manifests part of the broad picture of the long-term benefits brought about by such pre-investments. Today the Group is the biggest containerboard manufacturer in China and one of the biggest in the world, with an annual production capacity of 3.3 million tonnes. The benefits of economies of scale are working to secure the Group's leading position in the domestic and international packaging paperboard markets.

Cost-savings through in-house research and development

In addition to its remarkable production capacity, ND Paper also concentrates on strengthening its capability through in-house research and development. We are seeking to reduce the use of kraft pulp, one of our raw materials, in production through enhancing our technology by way of in-house research and development. During the year, the Group's PM12 and PM13 under construction, which are used to manufacture linerboard, will adopt the use of pure waste paper as raw materials for its default mode and are expected to help further reduce production costs. Meanwhile, the Group also implemented aggressive steps to improve and reallocate its production facilities, in an effort to reduce its investment in fixed assets and enhance its product competitiveness.

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In the past, the Group required three to six months on average to optimise the operating efficiency of a new paper machine. However, thanks to the invaluable experience and outstanding know-how of our management, the optimising time of the two paper machines, PM9 and PM10, which commenced operation in late December 2005, was substantially reduced and has achieved the designed optimal operating efficiency within merely two months. As a benchmark in the industry, this achievement has not only marked a major breakthrough for the Group in respect of production technology, but also reflects the unique “Nine Dragons Spirit” and the fruits of success achieved through the concerted efforts of all our staff. With the shorter optimising time, the Group is able to save a substantial amount of resources and costs involved and increase the stability of our overall gross margin.

Accelerating investment in capital expenditure to yield economies of scale

According to the data of RISI, China will remain a net importer of containerboard products until 2009, with an estimated annual import of approximately 1.6 million tonnes. In order to capture the enormous opportunities emerging in the market, the Group announced in April 2006 that it will accelerate its investment in capital expenditure in the financial year 2007 in order to further expand its production capacity. With the implementation of revised capital expenditure plan, the Group expects to achieve a total of 5.35 million tonnes in its production capacity in 2007, which will further allow the Group to capture the immense opportunities in the containerboard market.

Relying on the invaluable experience and expertise of our management, the Group has successfully installed and commenced the operation of ten paper machines. We have also pioneered the introduction of the dual-machine production line layout to give an additional boost to productivity and achieve substantial savings in operation and production. In the future, the Group will step up its efforts in innovation by leveraging the latest experience and expertise in the paper manufacturing industry in order to attain top standards in operating performance and minimise repair and maintenance costs.

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Promoting healthy corporate growth with stronger corporate governance, social responsibility and environmental protection

ND Paper is committed to maintaining and enhancing the quality of our corporate governance. To fulfill our pledge to our shareholders and deliver our regulatory obligations, in the past year our Board established a number of committees, including the Executive Committee, Audit Committee, Remuneration Committee and Risk Control Committee. These committees carry out their duties in accordance with the Articles of Association to strictly monitor the internal control systems of the Company and ensure that such systems is in compliance with the Code of Best Practices.

Given our unique mode of operation, ND Paper takes a proactive approach to disclose and explain the details of our connected transactions to our major business partners and shareholders. We believe that it is beneficial for all parties to know more about ND Paper and our industry, so that they can better understand our competitive advantage. The successful listing of ND Paper in Hong Kong was just the first step in taking our commitment to shareholders to the next level. We will continue to review and enhance our internal and external control measures to maintain our corporate governance at international standards.

In respect of social responsibility, we believe that "give and take" is the appropriate attitude of a good corporate citizen. Hence, ND Paper is always supportive of various charity activities. We are eager to fully apply our corporate philosophy of creativity to such functions and events and to arouse and foster a sense of social participation and dedication among our staff. The benefits and implications of such activities are extensive. As such, ND Paper will continue to participate in charity events for a good cause and will include social responsibility as part of our agenda for corporate development.

"No environment, no paper" is the concept that we hold dear. Since its establishment, the Group has been demanding of itself in maintaining a high standard of environmental protection by keeping up its investment in conservation, including the introduction of internationally advanced environmentally friendly equipment and technology. Despite the continued rapid growth of our business volume and coverage, we never compromise regarding the environment. With the idea of environmental protection forming a global trend, ND Paper will be increasingly active in its green efforts. We will continue to promote the use of recycled paper as the raw materials for manufacturing to ensure harmony with nature and continuous renewal.

Future plans and prospects

Looking ahead, the Company will maintain its commitment to the expansion of its packaging paperboard production base and search domestically and internationally for a suitable kraft pulp resource production base. Apart from the production bases in the Pearl River Delta and the Yangtze River Delta, the Group will establish new production bases in central-western and northern China in the next three to five years. The target of the Group for the coming year is to expand its annual production capacity by 62.1% from the current 3.3 million tonnes to 5.35 million tonnes. We are also planning to invest in four additional paper machines in the financial year 2008 so as to further expand our annual production capacity by 1.8 million tonnes from 5.35 million tonnes to 7.15 million tonnes. Such 1.8 million tonnes of additional annual production capacity consists of a capacity of one million tonnes of kraftlinerboard and 800,000 tonnes of high performance corrugating medium. It is expected that this production capacity expansion plan will be completed by the end of December 2008. We intend to finance such future capital expenditure by internally generated funds and bank loans. The above production capacity expansion plans are expected to help further strengthen our leading position in the international and domestic packaging paperboard market, as well as enhance the bargaining power of the Group. In addition, the Group is in negotiations with authorities in Dongguan regarding the construction of a local pier to improve the ancillary operation of the Group.

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To ensure a stable supply of unbleached kraft pulp, the Company has, through a joint venture, established an unbleached kraft pulp plant with an existing annual production capacity of up to 100,000 tonnes and a target production of up to 300,000 tonnes, in Inner Mongolia, where abundant resources are available. Looking ahead, the Group intends to engage in resources investment, including the development of upstream operations and bleached kraft pulp production. The Group targets to have mass production of bleached kraft pulp in three to five years. When contemplating any investment opportunity, the Group will first consider whether the project possess a long-term competitive edge to generate a stable rate of required returns.

Leveraging on economies of scale and the benefits brought about by pre-investments, the Group is confident that it will be able to sustain continuous business growth as it increases the use of recovered paper and carries out in-house research and development for cost saving technologies. Looking ahead, ND Paper will continue our long-lasting responsibility, and with the united effort of our management and staff, strive to become the largest and most efficient packaging paperboard manufacturer in the world.

Appreciation

The outstanding results of the Group in the past decade were attributable to the concerted efforts of the management and the staff. I would like to take this opportunity to express my sincere gratitude to the local governments for their continued support in providing us a favourable operating environment, as well as to the staff of the Group for their dedication, loyalty and contribution during the year. I would also like to thank our customers, business partners, shareholders and associates in the financial sector for their unreserved support in making this year another fruitful one for ND Paper.

Cheung Yan

Chairman

Hong Kong, the PRC, 20 September 2006