

MANAGEMENT DISCUSSION AND ANALYSIS

Review of Results

The Board hereby announces that, for the year ended 31 December 2006, the Group recorded an audited turnover of approximately RMB863.7 million (2005: RMB654.0 million), representing an increase of approximately 32.1% over last year, and a gross profit margin of 33.1%, as compared with 36.5% for last year. The Group has attained an audited profit attributable to equity holders of the parent of approximately RMB65.8 million for the year under review (2005: RMB122.7 million), representing a decrease of 46.4% over last year.

For the year ended 31 December 2006, the Group recorded an increase in turnover by approximately 32.1% to approximately RMB863.7 million. Such increase was mainly attributable to the increase in sales price of apple juice concentrate and related products of the Group.

The commencement of operation of a new factory in Yuncheng, Shanxi and the expansion of the factory in Qianxian, Shaanxi in 2005 made a full year contribution in 2006 and resulted in the increase in the production volume as well as the sales volume.

During the year under review, the selling price of the Group's products continued to increase, especially in Europe. The shortage of production of apple juice concentrate in Europe resulted in the increase in the demand for apple juice concentrate from the PRC. The Group strategically shifted its sales to the Europe market and the percentage of sales in such markets increased.

Due to the continued effect on the increase in apple cost which was attributable to the shortage of apples in the last pressing season and the increasing market price of apple juice concentrate, the apple purchase cost increased significantly in the year under review compared to that of last year. The Group's gross profit

margin decreased from approximately 36.5% in 2005 to approximately 33.1% in 2006 despite the increase in selling price of the Group's products.

Other income decreased from approximately RMB27.7 million in 2005 to approximately RMB5.3 million in 2006. The decrease was mainly attributable to the decrease in PRC Government subsidies which was non-recurrent and dependent on the prevailing policy of the PRC Government.

Distribution and selling costs were increased by 67.2% from approximately RMB62.5 million in 2005 to approximately RMB104.5 million in 2006. The increase in distribution and selling costs was driven by the increase in sales. The increase in proportion of sales with CIF terms also increased the freight charges of the Group.

Administrative expenses increased by 27.2% from approximately RMB46.3 million in 2005 to approximately RMB58.9 million in 2006. The commencement of operation of the new factory in Yuncheng in the fourth quarter of 2005 resulted in the increase in the administrative expenses including staff cost and depreciation expenses.

Finance cost for the Group amounted to approximately RMB54.1 million in 2006, representing an increase of 66.0% over last year. The increase is attributable to the increase in average bank borrowings during the year under review.

The Group has attained an audited profit attributable to equity holders of the parent of approximately RMB65.8 million for the year under review (2005: RMB122.7 million), representing a decrease of 46.4% over last year. The decrease in profit attributable to equity holders of the parent was mainly attributable to the increase in cost of raw material and distribution and selling cost and decrease in other income of the Group during the year.

Liquidity, Financial Resources, Gearing and Capital Commitments

As at 31 December 2006, the Group's borrowings amounted to approximately RMB1,206.8million (2005: RMB703.4 million), among which, approximately RMB581.0 million (2005: RMB281.3 million) were secured by way of charge of the Group's assets and approximately RMB175 million were denominated in US dollars while approximately RMB1,032 million were denominated in Renminbi. The maturity profile of the Group's borrowings is set out below:

	As at 31 December	
	2006	2005
	RMB'000	RMB'000
Repayable:		
On demand or within one year	1,147,100	440,015
In the second year	40,721	71,900
More than two years but not more than three years	19,000	53,922
More than three years but not more than four years	–	50,017
More than four years but not more than five years	–	25,018
In more than five years	–	62,545
Total borrowings	1,206,821	703,417

The total equity of the Group increased from approximately RMB685.0 million as at 31 December 2005 to approximately RMB720.6 million as at 31 December 2006. Such increase was attributable to the profit attributable to equity holders of the parent net of dividend paid during the year under review.

As a result, the gearing ratio, defined as total liabilities divided by total assets, was slightly increased from approximately 60.7% as

at 31 December 2005 to 67.3% as at 31 December 2006 and debt to equity ratio, defined as total borrowings divided by total equity, was increased from 1.0 as at 31 December 2005 to 1.7 as at 31 December 2006.

The treasury policy of the Group is centrally managed and controlled at the corporate level. As of 31 December 2006, the Group has RMB452.1 million capital commitments (2005: RMB20.5 million) and has no significant contingent liabilities.

Charges on assets

The Group has pledged the following assets for security of the Group's borrowings, which amounted to approximately RMB581.0 million:

	As at 31 December	
	2006	2005
	RMB'000	RMB'000
Property, plant and equipment	563,838	194,858
Prepaid lease payments	27,361	4,725
Pledged bank deposits	65,889	115,997
Trade receivables	–	27,616
Inventories	109,769	21,678
Total	766,857	364,874

In addition, the borrowings from non-bank financial institutions was secured by the 67.64% equity interest of Qingdao Haisheng Fresh Fruit Juice Co., Ltd., a non wholly-owned subsidiary, which is held by another non wholly-owned subsidiary of the Group.

In order to obtain the guarantee from a third party to guarantee the bank borrowings of RMB100 million, the Group pledged the 99.6% equity interest of Shaanxi Haisheng Fresh Fruit Juice Co., Ltd. ("Shaanxi Haisheng"), a non wholly-owned subsidiary of the Group, to that third party. In addition, a Director, Mr. Gao Liang also provided personal guarantee to that third party.



Business Review

As of 31 December 2006, the Group's production capacity was 205,000 tons. The efficiency and the economy of scale achieved with the Group's highly efficient and standardised equipment was further reflected. The newly established factory in Yuncheng and the extended factory in Qianxian were operating smoothly. Currently, the Group has factory in each of Qianxian of Shaanxi, Weinan of Shaanxi, Qingdao of Shandong, Dalian of Liaoning and Yuncheng of Shanxi. They are well positioned as being located in the provinces which are the richest in apple resources in the PRC, hence a complementary effect to each other in its strengths and a diversification of risk was attained.

Production

Due to the shortage of apples in the 2005/2006 pressing season, the Group's production utilisation rate was relatively low in 2005. The supply of apples was normal in the new 2006/2007 pressing season which commenced in 2006. In addition to the effective production plant management and technical innovation carried out by the Group, each of the factories commenced operation on time and was well operated. The utilisation rate of production capacity of all the five factories of the Group was largely increased. The average production utilisation rate was over 90%.

Sales and marketing

In 2006, the Group maintained remarkable sales performance. The Group's major markets in the world were North America, Europe, Australia, Japan and Russia. Apart from the continued consolidation of its original customer base and maintaining good relationship with customers in each market, the Group extended its market share in Europe and Russia. The Group's percentage of sales in Europe and Russia was increased from 22.3% in 2005 to 44.8% in 2006. At the same time, the Group developed its market in South Africa. According to the statistics from the Custom in

the PRC, the percentage of the Group's sales to South Africa to that of the PRC was zero in 2005 and 49% in 2006. The percentage of the Group's export to Russia to that of the PRC was increased from less than 1.0% in 2005 to 20.2% in 2006. Comprehensive and diversified sales network avoided the risk of depending on sole market. It has also enabled the Group to adjust the direction and focus of its sales, which will ensure that a higher profit margin can be obtained.

Raw material

The production of apples in western China was normal in the 2006/2007 pressing season while the apple production in Dalian of Liaoning was decreased. Due to the continued effect on the increase in apple cost which was attributable to the shortage of apples in the last pressing season and the increasing market price of apple juice concentrate, the apple purchase cost increased significantly in the year under review compared to that of last year. In order to better assure the adequate supply of raw material and the quality of apple being sourced, the Group kept on the construction of raw material. The Group's apple sourcing region was located over each of the major apple production area in the PRC. The proportion of apples purchased from Dalian region was less than 15%. Therefore, the shortage of apple production in Dalian has no significant effect on the Group's overall performance.

Accreditation

In 2006, all the five factories of the Group has kept on passing the annual accreditation by KOSHER, and all of them passed the FPA accreditation's biennial examination and obtained SGP accreditation. Except for the factory in Yuncheng which was newly established and had been under auditing, all the remaining four factories has obtained environmental management certificate of accreditation (ISO14001).



Exchange rate risk

Facing the increase in value of Renminbi, the Group exercised the following measures to decrease the adverse effect on the profit that attributable to the appreciation of Renminbi.

The Group used various currencies for settlement. The proportion of settlement in Euro was increased from 5.2% in 2005 to 10.4% in the year under review.

The Group aggressively increased its bank loans denominated in US dollars and at 31 December 2006, the Group has US\$ borrowings approximately of US\$22.4 million.

Terms and conditions related to changes in exchange rate were included in the sales contracts.

Human resources and staff remuneration

As of 31 December 2006, the Group has 1146 staff (31 December 2005: 888 staff). The increase in number of staff was attributable to the expansion of the Group.

The Group commits resources every year to provide continuing education and training for the management and core business staff as such will improve their technical know how and managerial skills.

In 2006, the Group cooperated with Hewitt Associates Consulting Co., Ltd., a famous consulting firm in the world, which put in place a relatively comprehensive human resources structure and established an effective performance assessment guides and competitive remuneration standards in order to attract candidates with higher caliber, raise staff welfare and increase staffs' sense of belongings. In turn, the Group's management became more scientific and formal and the management efficiency will be enhanced. The Group has also provided the statutory pension insurance, medical insurance, accidental insurance, unemployed insurance and accommodation pension for all staff.

Future prospect

Looking forward, the competition in the apple juice concentrate industry in the PRC will still be fierce. The consolidation of industry will be increased. The Group strongly believes that the advanced production facilities, perfect human resources system, well implemented financial management rules and workflow, further improved operational management structure and enhanced investment effectiveness and will lead to a bigger market share

and much higher profitability of the Group. In the coming year, the Group's plan on the production capacity, sales and raw materials are as follows:

Expansion of production capacity

In 2007, the Group planned to extend its production capacity by establishing two new factories in Anhui and Henan. The Group's production capacity will be increased from 205,000 tons to 305,000 tons in order to better fulfill the customers' demand and enlarge its market share.

Product diversification

In 2006, apple juice concentrate is still the major source of profit of the Group. In 2007, the Group will base on the market demand and the domestic resource privilege to broaden pear juice concentrate production capacity. Dalian Haisheng Fresh Fruit Juice Co., Ltd. has entered into an agreement with a Japanese strategic cooperator to jointly construct a production line for a variety of products including strawberry juice concentrate, peach juice concentrate and carrot juice concentrate in order to increase new drivers of profit. The Group also planned to further improve the production techniques of apple aroma, which has high added value, standardise the apple aroma product and further enlarge its profit margin.

Market development

In 2007, the Group, apart from maintaining and consolidating existing markets and customer base, kept on increasing its effort to developing and enlarging the market share in Japan and Russia and went on to enlarge the market share and customer base in the newly developed market in South Africa. Due to the large potential of domestic market and the increasing trend of value of Renminbi, the Group will continue to highly focus on the domestic market and further increase its domestic market share. Based on the increase in both production capacity and production volume and an effective developing strategy, the Group is looking forward to enlarge market share in fruit juice concentrate industry.

Construction of raw material growth base

In order to tackle risk on shortage of apple supply and quality of apples being sourced, the Group kept on its planned construction of raw material base. The Group also aggressively discovers new models of raw material base to effectively increase the area of the base, increase the quality of apple and assure the adequate supply.