YOUYUAN INTERNATIONAL HOLDINGS LIMITED

優源國際控股有限公司

*(Incorporated in the Cayman Islands with limited liability)*

(Stock Code: 2268)

# 2012 Interim Report

# Contents



# CORPORATE INFORMATION

## EXECUTIVE DIRECTORS

Mr Ke Wentuo (柯文托)
Mr Ke Jixiong (柯吉熊)
Mr Cao Xu (曹旭)
Mr Zhang Guoduan (張國端)

## INDEPENDENT NON-EXECUTIVE DIRECTORS

Prof. Zhang Daopei (張道沛)
Prof. Chen Lihui (陳禮輝)
Mr Chow Kwok Wai (周國偉)

## AUDIT COMMITTEE

Mr Chow Kwok Wai *(Chairman)*
Prof. Zhang Daopei
Prof. Chen Lihui

## REMUNERATION COMMITTEE

Prof. Chen Lihui *(Chairman)*
Prof. Zhang Daopei
Mr Ke Wentuo

## NOMINATION COMMITTEE

Prof. Zhang Daopei *(Chairman)*
Prof. Chen Lihui
Mr Ke Wentuo

## COMPANY SECRETARY

Mr Wong Yat Sum, *ACCA, HKICPA*

## AUTHORISED REPRESENTATIVES

Mr Ke Wentuo
Mr Wong Yat Sum

## CAYMAN ISLANDS SHARE REGISTRAR AND TRANSFER OFFICE

Butterfield Fulcrum Group (Cayman) Limited
Butterfield House
68 Fort Street
PO Box 609
Grand Cayman KY1-1107
Cayman Islands

## HONG KONG SHARE REGISTRAR

Computershare Hong Kong Investor Services Limited
Shops 1712-1716, 17th Floor
Hopewell Centre
183 Queen's Road East
Wanchai, Hong Kong

## REGISTERED OFFICE

Cricket Square, Hutchins Drive
PO Box 2681
Grand Cayman, KY1-1111
Cayman Islands

## HEADQUARTERS IN THE PRC

Xibin Industrial Zone
Jinjiang City
Fujian Province
The People's Republic of China

## PRINCIPAL PLACE OF BUSINESS IN HONG KONG

Unit 1601, 16th Floor
Bonham Trade Centre
50 Bonham Strand
Sheung Wan, Hong Kong
(effective from 13 February 2012)

# CORPORATE INFORMATION

## COMPANY'S WEBSITE

www.youyuan.com.hk

## PLACE OF LISTING AND STOCK CODE

The Stock Exchange of Hong Kong Limited
2268

## PRINCIPAL BANKERS

Bank of China, Quanzhou Branch
China Merchants Bank, Quanzhou Branch
China CITIC Bank, Quanzhou Branch

## AUDITOR

Deloitte Touche Tohmatsu
*Certified Public Accountants*

## LEGAL ADVISORS

**Hong Kong law:**

Orrick, Herrington & Sutcliffe

**PRC law:**

King & Wood Mallesons

**Cayman Islands law:**

Conyers Dill & Pearman

## INVESTORS AND MEDIA RELATIONS

iPR Ogilvy Ltd.

# BUSINESS REVIEW AND OUTLOOK

## BUSINESS REVIEW

An absence of a clear direction as to how the European sovereign debt crisis can be curbed and resolved constituted an unfavorable backdrop to the world's consumer goods sector as a whole. Coupled with the indecisiveness on the part of the United States in launching a third phase of quantitative easing measures to avert the country's slippage into a recession, and the uncertainty surrounding the slowdown of the economy of China, the paper making industry faced a stalemate under which the majority of the participants were short of clues on what measures to enact in the next stage of development.

An overtly benign sentiment on the sustainability of China's domestic consumption momentum prevailed since 2010 had resulted in modest overinvestment in papermaking production capacities. These overbuilt capacities had gradually commenced operation since the beginning of this year. This, when added to the softening of pulp prices in the international market, has precipitated heavy pressure on paper product prices.

According to statistics released by the China Paper Association, the capacity utilization rate of the paper making industry as a whole had been on the decline during the first half of the year, from 99.0% in December 2011 to 97.3% in June 2012. Prices of raw pulp and finished paper products of various categories were treading downwards as well.

Meanwhile, the specialty paper segment, which the Company focuses on, continued to exhibit stronger resilience than other segments. This is further accentuated by an announcement in July 2012 by the Ministry of Industry and Information Technology of China of a full list of obsolete or low-efficiency production capacities that need to be phased out. This will help concentrate production resources among stronger participants, including the Company, and restore order in product pricing.

While persisting in its core competences in wrapping tissue paper businesses, the Company continued to achieve notable progresses in constructing capacities for high-end wall-paper backing paper according to its schedule. In June 2012, the Company also acquired a land plot adjacent to its existing facilities in the Xiyuan production base to be part of its land reserves to support future development.

### Segmental Analysis

**Double-sided and single-sided machine-finished tissue paper**

Revenues generated from double-sided and single-sided machine-finished ("MF") tissue paper were RMB351.6 million and RMB131.5 million, contributed to approximately 51.8% and 19.4% of the Group's revenue for this reporting period, respectively.

Selected dryer equipment had been installed on two production lines of single-sided MF tissue paper with planned annual production capacities of 7,000 tonnes each, which enhanced the quality of the products to the same grade as double-sided MF tissue paper.

One single-sided MF tissue paper production line with a planned annual production capacity of 8,000 tonnes commenced operation in June 2012. The Group has also invested in a new double-sided MF tissue paper production line with a planned annual production capacity of 25,000 tonnes, scheduled to commence operation in the second half of 2012.

**Copy paper**

During this reporting period, revenue generated from copy paper was RMB115.2 million, representing an increase of 69.4% when compared with that of the same period of last year, and contributed to approximately 17.0% of the Group's revenue.

**Wall paper backing paper**

With reference to the Group's expansion plan, a new wall paper backing paper production line with a planned annual production capacity of 35,000 tonnes is scheduled to commence operation in the second half of 2012.

**Other products**

***Paper towel***

During this reporting period, revenue generated from paper towel was RMB40.3 million and contributed to approximately 5.9% of the Group's revenue.

***Ivory boards***

During this reporting period, revenue generated from ivory boards was RMB40.6 million and contributed to approximately 6.0% of the Group's revenue.

### Geographical Analysis

The entire Group's revenue was generated from the mainland China. Eastern China and Southern China are the largest markets of the Group (breakdown by locations from which sales were originated), with over 93% of Group's revenue for this reporting period being derived from these two regions.

**Operational Analysis**

As at 30 June 2012, the Group operated 31 production lines with designed annual production capacities aggregating 260,000 tonnes, including 158,000 tonnes for double-sided and single-sided MF tissue paper, 44,000 tonnes for copy paper, 38,000 tonnes for paper towel and 20,000 tonnes for ivory boards.

The Group is also equipped with two de-inked pulp production lines with designed annual production capacities aggregating 90,000 tonnes for its own use at the Huaxiang factory. A new de-inked pulp production line with a designed annual production capacity of 60,000 tonnes at the Xiyuan factory is under construction and is expected to commence operation in the second half of 2012. This expansion of in-house de-inked pulp production capacity enables the Group to reap further benefits on costs.

All the future expansion of production capacities will be surrounding the Group's existing three production bases. The Group acquired a piece of land during this reporting period to support future development in the Xiyuan factory.

## PROSPECTS

Looking ahead, it is expected that the stress surrounding the paper making industry in China will continue in the second half of 2012. The modest declines in fuel costs and raw pulp prices seen during the first half had reached a tailspin and had started to exhibit signs of reversal. Product prices, meanwhile, are expected to continue to be under pressure given the relatively weak momentum in domestic consumption and perpetuation of the industry's overcapacity situation in general.

This environment presents a real challenge to industry participants on their ability to survive through the difficulties. The Central Government's determination to phase out obsolete and low-efficiency capacities in the industry had forced many participants to invest in new facilities in the last two years. Most of them ended up with total debt to total assets ratios at a relatively high level. The challenge for them had been especially steep during the credit tightening cycle in the last two years featuring significantly much higher financing costs.

Yet on the contrary, participants with visions to invest in environmentally-friendly, high-efficiency capacities, including the Company, will be better positioned to capture bigger market shares, leveraging their robust financial positions and better cost-efficiency dynamics. For those with the ability to manufacture some of the raw materials for their own use, the advantage has become more apparent.

With regards to the decision of the Group to diversify into high-end wall paper backing paper business announced in early 2011, the first batch capacity, at 35,000 tonnes by design, should be able to commence production in the second half of 2012 on schedule. The Group remains immensely optimistic and is looking forward to the imminent launch of this business which will evolve as another strong income stream.

In relation to the latest production capacity expansion plan of the Group, its total production capacity will increase by approximately 60,000 tonnes from 260,000 tonnes at 30 June 2012 to 320,000 tonnes by the end of 2012. The Group believes that it is well-positioned to leverage its leading industry and market positions and strong production capacities to benefit from the sustaining growth in demand for wrapping tissue paper and other specialty paper in the mainland China.

# MANAGEMENT DISCUSSION AND ANALYSIS

## RESULTS

Revenue of the Group for the six months ended 30 June 2012 was RMB679.2 million, representing a decrease of approximately 1.0% from RMB686.3 million for the six months ended 30 June 2011. Profit and total comprehensive income attributable to owners of the Company decreased by approximately 17.4% from RMB148.6 million for the six months ended 30 June 2011 to RMB122.7 million for the six months ended 30 June 2012. The decrease in profit and total comprehensive income attributable to owners of the Company was as a result of the lower of overall average selling price of the Group's products, which was softened by an increase in sales volume of approximately 8,200 tonnes during the reporting period.

Basic earnings per share for the six months ended 30 June 2012 edged slightly down to RMB0.123 per share when compared with RMB0.149 per share for the same period of last year, based on the profit attributable to owners of the Company of RMB122.7 million (For the six months ended 30 June 2011: RMB148.6 million) and the weighted average of 1,000,000,000 shares (For the six months ended 30 June 2011: 1,000,000,000 shares) in issue during the reporting period.

### Gross profit

Gross profit of the Group slightly decreased from RMB216.4 million for the six months ended 30 June 2011 to RMB202.0 million for the six months ended 30 June 2012.

Overall gross profit margin of the Group narrowed from 31.5% for the six months ended 30 June 2011 to 29.7% for the six months ended 30 June 2012. The decline was primarily a result of the lower overall average selling price of the Group's products during the reporting period.

### Other income and other gains and losses

Other income and other gains and losses of the Group changed from a net loss of RMB1.9 million for the six months ended 30 June 2011 to a net gain of RMB0.8 million for the six months ended 30 June 2012, mainly due to reduction in net foreign exchange losses.

### Selling and distribution costs

Selling and distribution costs of the Group increased by approximately 7.5% from RMB3.8 million for the six months ended 30 June 2011 to RMB4.1 million for the six months ended 30 June 2012, representing approximately 0.6% of the Group's revenue for both reporting periods. The increase was primarily due to an increase in marketing resources allocated to promotional activities.

### Administrative expenses

Administrative expenses of the Group increased by approximately 9.0% from RMB28.9 million for the six months ended 30 June 2011 to RMB31.5 million for the six months ended 30 June 2012, representing approximately 4.2% and 4.6% of the Group's revenue for the reporting periods, respectively. The increase was primarily due to increases in depreciation charges for property, plant and equipment and general expenses.

### Finance costs

Finance costs of the Group increased by approximately 64.6% from RMB9.1 million for the six months ended 30 June 2011 to RMB14.9 million for the six months ended 30 June 2012, primarily due to an increase in the average bank borrowings and higher average interest rates during this reporting period.

Interest rates of bank loans ranged from 3.70% to 8.86% for the six months ended 30 June 2012, compared with 4.78% to 6.63% for the six months ended 30 June 2011.

### Other expenses

Other expenses represented research and development expenses on energy conservation, consumption reduction, environmental protection system and application of recycled materials as raw materials across the production process.

### Taxation

Tax charge decreased by approximately 1.6% from RMB22.7 million for the six months ended 30 June 2011 to RMB22.4 million for six months ended 30 June 2012, primarily due to the lower taxable profits of the Group's subsidiaries in the mainland China. The Group's effective tax rates for the six months ended 30 June 2011 and 30 June 2012 were 13.3% and 15.4%, respectively. The increase in effective tax rate was mainly due to the expiry of preferential tax rate of 15% for one subsidiary in the mainland China on 31 December 2011.

### Profit attributable to owners of the Company

Profit and total comprehensive income attributable to owners of the Company decreased from RMB148.6 million for the six months ended 30 June 2011 to RMB122.7 for the six months ended 30 June 2012. The ratio of profit attributable to owners the Company to revenue narrowed down from approximately 21.7% for the six months ended 30 June 2011 to approximately 18.1% for the six months ended 30 June 2012 mainly due the lower overall average selling price of the Group's products.

### Inventories, trade receivables and payables turnover cycle

The Group's inventories mainly comprise raw materials including wood pulp, recovered paper for de-inked pulp production and finished products. For the six months period ended 30 June 2012, the inventory turnover cycle was approximately 79.8 days (For the year ended 31 December 2011: 69.7 days). The turnover cycle was lengthened primarily due to an increase in stock of finished products during the reporting period.

The turnover cycle for trade receivables for the six months ended 30 June 2012 lengthened to 79.4 days (For the year ended 31 December 2011: 67.2 days) primarily due to slightly longer credit periods granted to customers. The Group's standard credit term to customers is 60 days.

The turnover cycle for trade and bills payables was shortened to 54.5 days (For the year ended 31 December 2011: 56.0 days), which is within the 60-day credit period granted by our suppliers.

### Borrowings

As at 30 June 2012, the Group's bank borrowings balance amounted to RMB843.0 million, of which RMB515.0 million will be due for repayment within the next twelve months (As at 31 December 2011: RMB532.1 million, of which RMB 452.1 million will be due for repayment within the next twelve months).

As at 30 June 2012, the Group's bank borrowings amounted to RMB221.0 million, carried at fixed interest rates (As at 31 December 2011: RMB193.0 million).

As at 30 June 2012, the Group's gross gearing ratio was approximately 29.2 % (As at 31 December 2011: 21.1%), which was calculated on the basis of total borrowings as a percentage of total assets. The net gearing ratio, which was calculated on the basis of total borrowings less bank balances and cash and pledged bank deposits as a percentage of shareholder equity, was 25.4 % (As at 31 December 2011: 24.2%).

### Pledge of assets

As at 30 June 2012, the Group pledged certain of its property, plant and equipment and land use rights with aggregate carrying value of RMB417.5 million and RMB244.2 million respectively (As at 31 December 2011: RMB460.1 million and RMB262.9 million respectively) as collaterals backing the credit facilities granted to the Group.

### Cash flow management

As at 30 June 2012, the Group had net current assets of RMB168.6 million (As at 31 December 2011: net current liabilities of RMB17.5 million), the turnaround was mainly due to an extension of the terms of bank borrowings, which were classified as non-current liabilities. The Group raised over RMB300.0 million through bank borrowings in this reporting period with the majority of repayment due beyond twelve months from the reporting date. The management will closely monitor the cash flow position to ensure that the Group has adequate working capital to support its daily operations.

### Capital expenditure

For the six months ended 30 June 2012, the Group invested RMB134.3 million (For the six months ended 30 June 2011: RMB 185.5 million) in construction of production facilities and equipment.

## DIVIDEND

The Board has resolved to declare of an interim dividend for the six months ended 30 June 2012 of HK3.5 cents per share, totaling HK$35,000,000 (amounted to approximately RMB28,700,000) (For the six months ended 30 June 2011: Nil). It is expected that the interim dividend will be paid on or about 20 September 2012 to shareholders whose names appear on the register of member of the Company on 13 September 2012.

## CLOSURE OF REGISTER OF MEMBERS

The register of members of the Company will be closed from 10 September 2012 to 13 September 2012 (both days inclusive), during which period no transfer of shares will be registered. In order to establish entitlement to the interim dividend (which is expected to be paid on or about 20 September 2012), all transfers accompanied by the relevant share certificates must be lodged with the Company's share registrar, Computershare Hong Kong Investor Services Limited, at Shops 1712–1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, no later than 4:30 pm on 7 September 2012 for registration of the transfers.

## HUMAN RESOURCES MANAGEMENT

As at 30 June 2012, the Group employed 2,006 staff (As at 30 June 2011: 2,248 staff) and the total remuneration for the six months ended 30 June 2012 amounted to approximately RMB32.1 million (For the six months ended 30 June 2011: RMB30.5 million). The Group's remuneration packages are commensurate with the experience and qualifications of individual employees and general market conditions. Bonuses are linked to the Group's financial results as well as individual performances. The Group also ensures that all employees are provided with adequate training and professional development opportunities to satisfy their career development needs.

## SHARE OPTION SCHEME

Pursuant to the written resolutions passed by all the shareholder of the Company on 30 April 2010, the Company approved and adopted a share option scheme (the "Scheme") for the purpose of giving the eligible persons an opportunity to have a personal stake in our Company helping in motivate them to optimise their future performance and efficiency to our Group and/or to reward them for their past contributions, to attract and retain or otherwise maintain on-going relationships with such eligible person who are significant to and/or whose contributions are or will be beneficial to the performance, growth or success of our Group, and additionally in the case of executives, to enable our Group to attract and retain individuals with experience and ability and/or to reward them for their past contributions.

As at 30 June 2012, no options had been granted or agreed to be granted under the Scheme.

## DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS IN THE SHARES AND UNDERLYING SHARES AND DEBENTURES OF OUR COMPANY OR ANY ASSOCIATED CORPORATION

As at 30 June 2012, the interests of each Director and chief executive of our Company in the Shares, underlying Shares and debentures of our Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) as recorded in the register required to be kept under Section 352 of the SFO, or as otherwise notified to our Company and Stock Exchange pursuant to the Model Code set out in Appendix 10 to the Listing Rules, were as follows:

| Name of director | Capacity/Nature of interest | Number of Shares | Approximate percentage of interest in our Company |
|---|---|---|---|
| Mr Ke Wentuo | Interest in controlled corporation and interest of spouse[1] | 573,750,000 | 57.38% |
| Mr Ke Jixiong | Interest in controlled corporation[2] | 33,000,000 | 3.30% |

Note 1: The interest in 573,750,000 Shares comprise of:

(i) 550,050,000 Shares held by Smart Port Holdings Limited ("Smart Port"), which is wholly owned by Mr Ke Wentuo; and

(ii) 23,700,000 Shares held by Denron International Limited ("Denron"), which in turn is wholly beneficially owned by Ms Cai Lishuang, and Mr Ke Wentuo, being the spouse of Ms Cai Lishuang, is deemed to be interested in the said 23,700,000 Shares held by Denron.

Note 2: The interest in 33,000,000 Shares refer to the 33,000,000 Shares held by Everproud International Limited, which is wholly owned by Mr Ke Jixiong.

Except as disclosed above, none of the Directors nor the chief executives of our Company or their associates had any interest or short positions in any of the shares, underlying shares or debentures of our Company or any of its associated corporations as defined in the SFO.

## SUBSTANTIAL SHAREHOLDERS' INTERESTS AND SHORT POSITIONS IN THE SHARES AND UNDERLYING SHARES

The register of substantial shareholders required to be kept by our Company under Section 336 of Part XV of the SFO shows that as at 30 June 2012, in addition to the interests disclosed under the paragraph headed "Directors and Chief Executives' Interests in the Shares and Underlying Shares and Debentures of our Company or any Associated Corporation", our Company was notified of the following substantial shareholders' interests and short positions in the Shares and underlying Shares, being interests of 5% or more.

| Name | Capacity/Nature of interest | Number of Shares | Approximate percentage of shareholding |
|---|---|---|---|
| Smart Port Holdings Limited | Beneficial interest[1] | 550,050,000 | 55.01% |
| Ms Cai Lishuang | Interest in controlled corporation and interest of spouse[2] | 573,750,000 | 57.38% |
| Cathay Special Paper Limited | Beneficial interest[3] | 88,350,000 | 8.84% |

Note 1: Mr Ke Wentuo is deemed to be interested in the Shares held by Smart Port by virtue of Smart Port being wholly owned by Mr Ke Wentuo.

Note 2: Ms Cai Lishuang is deemed to be interested in the Shares held by Denron by virtue of Denron being wholly owned by Ms Cai Lishuang. In addition, she is deemed to be interested in the Shares held by Smart Port, which is wholly owned by Mr Ke Wentuo, by virtue of her being the spouse of Mr Ke Wentuo.

Note 3: Cathay Special Paper Limited is wholly owned by Cathay Capital Holdings II, L.P., a limited liability partnership.

Except as disclosed above, as at 30 June 2012, our Company has not been notified by any person or corporation who had interests or short positions in the Shares or underlying Shares as recorded in the register required to be kept by our Company under Section 336 of Part XV of the SFO.

## CODE OF CORPORATE GOVERNANCE PRACTICE

The Stock Exchange of Hong Kong Limited has made various amendments to the Code on Corporate Governance Practices (the "Old Code") contained in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") and renamed it the Corporate Governance Code (the "New Code"). The New Code took effect on 1 April 2012.

Our Company has adopted the New Code as set out in Appendix 14 to the Listing Rules as its own code of corporate governance. For the six months ended 30 June 2012, the Directors consider that our Company has complied with all the code provisions as set out in the Old Code for the period from 1 January 2012 to 31 March 2012, and those set out in the New Code for the period from 1 April 2012 to 30 June 2012.

Our Directors are committed to upholding the corporate governance of our Company to ensure that formal and transparent procedures are in place to protect and maximise the interests of the shareholders of our Company.

## MODEL CODE FOR SECURITIES TRANSACTIONS

Our Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 of the Listing Rules as the code of conduct for Directors in their dealings in the securities of our Company. Having made specific enquiry to all our Directors, all our Directors confirmed that they have complied with the required standard of dealings as set out in the Model Code throughout the period under review.

## PURCHASE, SALE OR REDEMPTION OF THE LISTED SECURITIES OF OUR COMPANY

For the six months ended 30 June 2012, neither our Company nor any of its subsidiaries has purchased, sold or redeemed any of the listed securities of our Company.

## AUDIT COMMITTEE

The Company has established an audit committee on 30 April 2010 with written terms of reference in compliance with the Code. The primary responsibilities of our Audit Committee are to review and supervise financial reporting processes and internal control system of the Group. As at 30 June 2012, the audit committee comprises Mr Chow Kwok Wai, Prof. Zhang Daopei and Prof. Chen Lihui, being the three independent non-executive Directors. Mr. Chow Kwok Wai is the chairman of our audit committee.

The members of audit committee reviewed the Company's financial reporting system and internal control system and the Group's audited financial statements for the year ended 31 December 2011 and interim report for the six months ended 30 June 2012 in conjunction with the Company's external auditor. They were of the opinion that these statements had complied with the applicable accounting standards, rules and regulations, and that adequate disclosures had been made.

## NOMINATION COMMITTEE

Our Company established a nomination committee on 22 December 2011 with written terms of reference in compliance with the Code. As at 30 June 2012, the nomination committee comprised Mr. Prof. Zhang Daopei, Prof. Chen Lihui and Mr Ke Wentuo. Prof. Zhang Daopei is the chairman of the nomination committee. The nomination committee considers and recommends to the Board suitably qualified persons to become Directors and is responsible for reviewing the structure, size and composition of the Board at least annually and making recommendations on any proposed changes to the board to complement the Company's corporate strategies.

## REMUNERATION COMMITTEE

Our Company established a remuneration committee on 30 April 2010 with written terms of reference in compliance with the Code. As at 30 June 2012, the remuneration committee comprised Mr Ke Wentuo, Prof. Zhang Daopei and Prof. Chen Lihui. Prof. Chen Lihui is the chairman of the remuneration committee. The primary responsibilities of our remuneration committee are to make recommendations to the Board on the remuneration packages of the Directors and senior management personnel of our Group and to ensure that no Director or any of his associates is involved in deciding his own remuneration.

## USE OF NET PROCEEDS FROM INITIAL PUBLIC OFFERING

The Shares were listed on 27 May 2010 on the Main Board of The Stock Exchange of Hong Kong Limited. The total net proceeds from the Listing after the issue of the Shares amounted to approximately RMB510.5 million, which had been intended to be applied as set out in the section headed "Use of Proceeds" of the Prospectus of the Company dated on 14 May 2010. As at 30 June 2012, RMB489.1 million have been used in the manner as described in the Prospectus and RMB21.4 million remained unutilized.

## SUFFICIENCY OF PUBLIC FLOAT

Based on the publicly available information and to the best of the Directors' knowledge, information and belief and at the date of this report, our Company has maintained sufficient public float during the six months ended 30 June 2012.

## REVIEW OF INTERIM RESULTS

The unaudited condensed consolidated interim financial report has been reviewed by the Company's audit committee and the Company's auditors, Deloitte Touche Tohmatsu, in accordance with Hong Kong Standard on Review Engagements 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Hong Kong Institute of Certified Public Accountants.

On behalf of the Board
**Ke Wentuo**
*Chairman*

Hong Kong, 16 August 2012

# REPORT ON REVIEW OF CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

**TO THE BOARD OF DIRECTORS OF**
**YOUYUAN INTERNATIONAL HOLDINGS LIMITED**
**優源國際控股有限公司**
*(incorporated in the Cayman Islands with limited liability)*

## INTRODUCTION

We have reviewed the condensed consolidated financial statements of Youyuan International Holdings Limited (the 'Company') and its subsidiaries (collectively referred to as the 'Group') set out on pages 14 to 26, which comprises the condensed consolidated statement of financial position as of 30 June 2012 and the related condensed consolidated statement of comprehensive income, statement of changes in equity and statement of cash flows for the six-month period then ended, and certain explanatory notes. The Main Board Listing Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of a report on interim financial information to be in compliance with the relevant provisions thereof and International Accounting Standard 34 "Interim Financial Reporting" ("IAS 34"). The directors of the Company are responsible for the preparation and presentation of these condensed consolidated financial statements in accordance with IAS 34. Our responsibility is to express a conclusion on these condensed consolidated financial statements based on our review, and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

## SCOPE OF REVIEW

We conducted our review in accordance with Hong Kong Standard on Review Engagements 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Hong Kong Institute of Certified Public Accountants. A review of these condensed consolidated financial statements consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly we do not express an audit opinion.

## CONCLUSION

Based on our review, nothing has come to our attention that causes us to believe that the condensed consolidated financial statements are not prepared, in all material respects, in accordance with IAS 34.

**Deloitte Touche Tohmatsu**
*Certified Public Accountants*
Hong Kong
16 August 2012

# CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

*For the six months ended 30 June 2012*

| | NOTES | Six months ended 30 June 2012 RMB'000 (unaudited) | 2011 RMB'000 (unaudited) |
|---|---|---|---|
| Revenue | | **679,222** | 686,326 |
| Cost of sales | | **(477,265)** | (469,974) |
| Gross profit | | **201,957** | 216,352 |
| Selling and distribution expenses | | **(4,083)** | (3,797) |
| Administrative expenses | | **(31,518)** | (28,906) |
| Other income and other gains and losses | 4 | **790** | (1,949) |
| Finance costs | 5 | **(14,942)** | (9,077) |
| Other expenses | | **(7,088)** | (1,268) |
| Profit before tax | | **145,116** | 171,355 |
| Income tax expense | 6 | **(22,383)** | (22,738) |
| Profit and total comprehensive income for the period attributable to owners of the Company | 7 | **122,733** | 148,617 |
| Earnings per share - Basic (RMB) | 9 | **0.123** | 0.149 |

# CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

*At 30 June 2012*

| | NOTES | At 30 June 2012 RMB'000 (unaudited) | At 31 December 2011 RMB'000 (audited) |
|---|---|---|---|
| **NON-CURRENT ASSETS** | | | |
| Property, plant and equipment | 10 | 1,462,789 | 1,355,972 |
| Prepaid lease payments | | 344,252 | 275,269 |
| Deposits paid for acquisition of property, plant and equipment | | 176,061 | 177,754 |
| Deposits paid for acquisition of land use right | | 16,000 | 60,683 |
| | | 1,999,102 | 1,869,678 |
| **CURRENT ASSETS** | | | |
| Inventories | 11 | 183,121 | 237,684 |
| Trade and other receivables | 12 | 321,832 | 307,780 |
| Prepaid lease payments | | 7,227 | 5,800 |
| Pledged bank deposits | | 45,908 | 4,857 |
| Bank balances and cash | | 329,617 | 98,121 |
| | | 887,705 | 654,242 |
| **CURRENT LIABILITIES** | | | |
| Trade and other payables | 13 | 189,001 | 210,575 |
| Tax liabilities | | 15,096 | 9,038 |
| Bank borrowings | 14 | 514,990 | 452,120 |
| | | 719,087 | 671,733 |
| **NET CURRENT ASSETS (LIABILITIES)** | | 168,618 | (17,491) |
| **TOTAL ASSETS LESS CURRENT LIABILITIES** | | 2,167,720 | 1,852,187 |
| **NON-CURRENT LIABILITY** | | | |
| Bank borrowings | 14 | 328,000 | 80,000 |
| | | 1,839,720 | 1,772,187 |
| **CAPITAL AND RESERVES** | | | |
| Share capital | 15 | 87,680 | 87,680 |
| Reserves | | 1,752,040 | 1,684,507 |
| **TOTAL EQUITY** | | 1,839,720 | 1,772,187 |

# CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

*For the six months ended 30 June 2012*

| | Attributable to owners of the Company | | | | | | |
|---|---|---|---|---|---|---|---|
| | **Share capital** | **Share premium** | **Capital reserve** | **Special reserve** | **Statutory surplus reserve** | **Accumulated profits** | **Total** |
| | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| At 1 January 2011 (audited) | 87,680 | 451,469 | 257,299 | 67,866 | 68,037 | 563,869 | 1,496,220 |
| Profit and total comprehensive income for the period | — | — | — | — | — | 148,617 | 148,617 |
| At 30 June 2011 (unaudited) | 87,680 | 451,469 | 257,299 | 67,866 | 68,037 | 712,486 | 1,644,837 |
| At 1 January 2012 (audited) | **87,680** | **396,269** | **257,299** | **67,866** | **96,068** | **867,005** | **1,772,187** |
| Profit and total comprehensive income for the period | — | — | — | — | — | **122,733** | **122,733** |
| Dividends recognised as distribution (Note 8) | — | — | — | — | — | **(55,200)** | **(55,200)** |
| Transferred to accumulated profits (Note a) | — | **(28,700)** | — | — | — | **28,700** | — |
| At 30 June 2012 (unaudited) | **87,680** | **367,569** | **257,299** | **67,866** | **96,068** | **963,238** | **1,839,720** |

Note a: Pursuant to board resolutions of directors passed on 21 June 2012, the directors were authorised, and resolved, to transfer RMB28,700,000 from share premium account to accumulated profits. Under the Companies Law of the Cayman Islands, the share premium account is distributable to the shareholders of the Company provided that immediately following the date on which the dividend is proposed to be distributed, the Company will be in a position to pay off its debts as they fall due in the ordinary course of business of the Company.

# CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

*For the six months ended 30 June 2012*

| | Six months ended 30 June | |
|---|---|---|
| | **2012** | 2011 |
| | **RMB'000** | RMB'000 |
| | **(unaudited)** | (unaudited) |
| **NET CASH FROM OPERATING ACTIVITIES** | **189,413** | 98,454 |
| **INVESTING ACTIVITIES** | | |
| Purchases of property, plant and equipment | **(125,231)** | (280,469) |
| Addition of prepaid lease payments | **(12,533)** | — |
| Increase in deposits paid for acquisitions of prepaid lease payments | **(16,000)** | (65,305) |
| Withdrawal of pledged bank deposits | **4,124** | 3,426 |
| Placement of pledged bank deposits | **(45,175)** | (2,295) |
| Interest received | **448** | 600 |
| **NET CASH USED IN INVESTING ACTIVITIES** | **(194,367)** | (344,043) |
| **FINANCING ACTIVITIES** | | |
| Dividend paid | **(55,016)** | — |
| New bank borrowings raised | **591,990** | 193,000 |
| Repayments of bank borrowings | **(281,120)** | (200,200) |
| Interest paid | **(19,404)** | (14,273) |
| Payments of transaction costs attributable to issue of new shares | **—** | (17,068) |
| **NET CASH FROM (USED IN) FINANCING ACTIVITIES** | **236,450** | (38,541) |
| **NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS** | **231,496** | (284,130) |
| **CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD** | **98,121** | 463,634 |
| **CASH AND CASH EQUIVALENTS AT END OF PERIOD** | **329,617** | 179,504 |

## 1. BASIS OF PREPARATION

The condensed consolidated financial statements have been prepared in accordance with International Accounting Standard 34 ("IAS34"), Interim Financial Reporting and with the applicable disclosure requirements of Appendix 16 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Stock Exchange") (the "Listing Rules").

## 2. PRINCIPAL ACCOUNTING POLICIES

The condensed consolidated financial statements have been prepared on the historical cost basis.

Except as described below, the accounting policies and methods of computation used in the condensed consolidated financial statements for the six months ended 30 June 2012 are the same as those followed in the preparation of the Group's annual financial statements for the year ended 31 December 2011.

In the current interim period, the Group has applied, for the first time, the following amendments to International Financial Reporting Standards ("IFRSs").

| | |
|---|---|
| Amendments to IFRS 7 | Disclosures – Transfers of Financial Assets |
| Amendments to IAS 12 | Deferred Tax: Recovery of Underlying Assets |

The application of the above amendments to IFRSs in the current interim period has had no material effect on the amounts reported in these condensed consolidated financial statements and/or disclosures set out in these condensed consolidated financial statements.

## 3. SEGMENT INFORMATION

Information is reported to the Chief Executive Officer of the Company, being the chief operating decision maker, for the purposes of resources allocation and performance assessment. The segment information is prepared based on the types of goods delivered.

Specifically, the Group's reportable and operating segments under IFRS 8 are as follows:

- Double-sided MF tissue paper - manufacturing and trading of double-sided MF tissue paper;
- Single-sided MF tissue paper - manufacturing and trading of single-sided MF tissue paper;
- Copy paper - manufacturing and trading of copy paper; and
- Other products - manufacturing and trading of paper towels and ivory boards.

## 3. SEGMENT INFORMATION (Continued)

The following is an analysis of the Group's revenue and results by reportable and operating segments:

| | Segment revenue Six months ended 30 June | | Segment results Six months ended 30 June | |
|---|---|---|---|---|
| | **2012 RMB'000 (unaudited)** | 2011 RMB'000 (unaudited) | **2012 RMB'000 (unaudited)** | 2011 RMB'000 (unaudited) |
| Double-sided MF tissue paper | **351,604** | 313,535 | **114,087** | 106,525 |
| Single-sided MF tissue paper | **131,491** | 211,809 | **43,138** | 73,455 |
| Copy paper | **115,198** | 68,012 | **36,521** | 19,744 |
| Other products | **80,929** | 92,970 | **8,211** | 16,628 |
| | **679,222** | 686,326 | **201,957** | 216,352 |
| Selling and distribution expenses | | | **(4,083)** | (3,797) |
| Administrative expenses | | | **(31,518)** | (28,906) |
| Other income and other gains and losses | | | **790** | (1,949) |
| Finance costs | | | **(14,942)** | (9,077) |
| Other expenses | | | **(7,088)** | (1,268) |
| Profit before tax | | | **145,116** | 171,355 |

Segment revenue and segment results reported above represents revenue and gross profit generated from external customers, respectively. There were no intersegment sales during both periods.

## 4. OTHER INCOME AND OTHER GAINS AND LOSSES

| | Six months ended 30 June | |
|---|---|---|
| | **2012** | 2011 |
| | **RMB'000** | RMB'000 |
| | **(unaudited)** | (unaudited) |
| Bank interest income | **448** | 600 |
| Loss on disposal of property, plant and equipment | **(58)** | (9) |
| Net foreign exchange losses | **(316)** | (2,763) |
| Government grants (note) | **646** | 190 |
| Others | **70** | 33 |
| | **790** | (1,949) |

Note: Government grants represented incentives granted by the local authorities to the Group's subsidiaries located in the PRC for developing innovative production technology and maintaining a good reputation in the business community. There are no unfulfilled conditions and other contingencies attaching to such grants.

## 5. FINANCE COSTS

| | Six months ended 30 June | |
|---|---|---|
| | **2012** | 2011 |
| | **RMB'000** | RMB'000 |
| | **(unaudited)** | (unaudited) |
| **Interest on:** | | |
| Bank borrowings wholly repayable within five years | **20,088** | 14,101 |
| Less: Amounts capitalised | **(5,146)** | (5,024) |
| | **14,942** | 9,077 |

During the six months ended 30 June 2012, the borrowing costs RMB5,146,000 (six months ended 30 June 2011: RMB5,024,000) capitalised are attributable to funds borrowed specifically for the purpose of obtaining particular qualifying assets such as its production facilities.

## 6. INCOME TAX EXPENSE

| | Six months ended 30 June | |
|---|---|---|
| | **2012** | 2011 |
| | **RMB'000** | RMB'000 |
| | **(unaudited)** | (unaudited) |
| **Current tax:** | | |
| PRC Enterprise Income Tax ("EIT") | **22,383** | 22,738 |

Pursuant to the relevant laws and regulations in the PRC, Fujian Jinjiang Youlanfa Paper Co., Ltd. ("Youlanfa"), a subsidiary of the Company, obtained a high and new technology enterprise certificate in 2010 and was entitled to a preferential tax rate of 15% for the three years from 2009 to 2011, subject to annual review by the relevant tax authority. As this certificate expired at the end of 2011, Youlanfa is subject to EIT tax rate of 25% for this interim period.

Pursuant to the relevant laws and regulations in the PRC, Fujian Xiyuan Paper Co., Ltd. and Quanzhou Huaxiang Paper Industry Co., Ltd., the subsidiaries of the Company, are entitled to an exemption from EIT for two years starting from their first exemption year, followed by a 50% tax relief for the following three years. Years 2008 and 2009 were the exemption years, and these two subsidiaries are subject to 50% reduced tax rate of 12.5% in the years 2010 to 2012.

Under the EIT Law, withholding tax is imposed on dividends declared in respect of profits earned by the Group's PRC subsidiaries from 1 January 2008 onwards. Deferred taxation has not been provided for in the condensed consolidated financial statements in respect of temporary differences attributable to accumulated distributable profits of the Group's PRC subsidiaries amounting to RMB 947,545,000 as at 30 June 2012 (31 December 2011: RMB820,468,000), as the Company is able to control the timing of the reversal of the temporary differences and it is probable that the temporary differences will not reverse in the foreseeable future.

Other than above, the Group has no significant provided or unprovided deferred tax at the end of the reporting periods.

## 7. PROFIT FOR THE PERIOD

Profit for the period has been arrived at after charging (crediting) the following item:

| | Six months ended 30 June | |
|---|---|---|
| | **2012** | 2011 |
| | **RMB'000** | RMB'000 |
| | **(unaudited)** | (unaudited) |
| Depreciation of property, plant and equipment | **27,454** | 19,650 |
| Release of prepaid lease payments | **2,806** | 2,874 |
| Total depreciation and amortisation expenses | **30,260** | 22,524 |
| Research and development cost recognised as an expense (included in other expenses) | **7,088** | 4,360 |
| Overprovision of listing expenses in prior years (included in other expenses) | — | (3,092) |
| Cost of inventories recognised as expenses | **477,265** | 469,974 |

## 8. DIVIDENDS

During the current interim period, a final dividend of HK6.8 cents per share in respect of the year ended 31 December 2011 has been declared and paid. The aggregate amount of the final dividend declared and paid in the current interim period amounted to approximately HK$68,000,000 (amounted to approximately RMB55,200,000) and HK$67,774,000 (amounted to approximately RMB55,016,000), respectively.

Subsequent to the end of the current interim period, the directors have recommended the payment of an interim dividend of HK3.5 cents per share for the six months ended 30 June 2012 (six months ended 30 June 2011: Nil).

## 9. EARNINGS PER SHARE - BASIC

The calculation of basic earnings per share attributable to the owners of the Company is based on the following data:

| | Six months ended 30 June | |
|---|---|---|
| | **2012** | 2011 |
| | **RMB'000** | RMB'000 |
| | **(unaudited)** | (unaudited) |
| **Earnings** | | |
| Profit for the period attributable to owners of the Company for the purpose of basic earnings per share | **122,733** | 148,617 |

| | Six months ended 30 June | |
|---|---|---|
| | **2012** | 2011 |
| | **(unaudited)** | (unaudited) |
| **Number of shares** | | |
| Weighted average number of ordinary shares for the purpose of basic earnings per share | **1,000,000,000** | 1,000,000,000 |

No diluted earnings per share are presented as there were no potential ordinary shares outstanding during both periods.

## 10. PROPERTY, PLANT AND EQUIPMENT

| | **Carrying values RMB'000** |
|---|---|
| At 1 January 2012 (audited) | 1,355,972 |
| Additions | 134,329 |
| Depreciation for the period | (27,454) |
| Disposals | (58) |
| At 30 June 2012 (unaudited) | 1,462,789 |

During the six months ended 30 June 2012, the Group mainly incurred approximately RMB132 million (six months ended 30 June 2011: RMB178 million) on the construction of new production facilities in the PRC and capitalised interest in order to enlarge its production capabilities.

## 11. INVENTORIES

| | At 30 June 2012 RMB'000 (unaudited) | At 31 December 2011 RMB'000 (audited) |
|---|---|---|
| Raw materials | 140,240 | 204,693 |
| Work in progress | 148 | 228 |
| Finished goods | 42,733 | 32,763 |
| | 183,121 | 237,684 |

## 12. TRADE AND OTHER RECEIVABLES

Trade and other receivables mainly represent approximately RMB314,816,000 (31 December 2011: approximately RMB281,212,000), trade receivables.

The Group allows an average credit period of 60 days to its trade customers. The following is an analysis of trade receivables by age, presented based on the invoice date.

| | At 30 June 2012 RMB'000 (unaudited) | At 31 December 2011 RMB'000 (audited) |
|---|---|---|
| 0 to 30 days | 133,900 | 135,612 |
| 31 to 60 days | 169,609 | 119,431 |
| 61 to 90 days | 11,307 | 26,169 |
| | 314,816 | 281,212 |

## 13. TRADE AND OTHER PAYABLES

| | At 30 June 2012 RMB'000 (unaudited) | At 31 December 2011 RMB'000 (audited) |
|---|---|---|
| Trade payables | 128,575 | 139,630 |
| Bills payables | — | 19,103 |
| | 128,575 | 158,733 |
| Other payables for acquisition of plant and equipment | 20,316 | 18,057 |
| Other tax payables | 13,142 | 7,737 |
| Other payables and accrued operating expenses | 26,968 | 26,048 |
| | 189,001 | 210,575 |

Other payables and accrued operating expenses mainly represent accrued staff costs and utilities expenses.

The following is an analysis of trade payables by age, presented based on the invoice date.

| | At 30 June 2012 RMB'000 (unaudited) | At 31 December 2011 RMB'000 (audited) |
|---|---|---|
| Within 30 days | 67,510 | 87,010 |
| 31 to 90 days | 61,065 | 52,620 |
| | 128,575 | 139,630 |

The bills payables as at 31 December 2011 are due within 120 days.

## 14. BANK BORROWINGS

| | At 30 June 2012 RMB'000 (unaudited) | At 31 December 2011 RMB'000 (audited) |
|---|---|---|
| Secured bank borrowings | 572,990 | 502,120 |
| Unsecured bank borrowings | 270,000 | 30,000 |
| | 842,990 | 532,120 |
| The amount is repayable as follows: | | |
| Within one year | 514,990 | 452,120 |
| More than one year | 145,800 | 45,000 |
| More than two years, but not exceeding five years | 182,200 | 35,000 |
| | 842,990 | 532,120 |
| Less: Amounts due within one year shown under current liabilities | (514,990) | (452,120) |
| | 328,000 | 80,000 |

All unsecured bank borrowings are cross guaranteed by the group companies. The remaining bank borrowings are secured by property, plant and equipment and prepaid lease payments with carrying amount of approximately RMB662 million (31 December 2011: approximately RMB 723 million).

## 15. SHARE CAPITAL

| | Number of shares | Share capital HK$ |
|---|---|---|
| Ordinary shares of HK$0.1 each | | |
| Authorised: | | |
| At 1 January 2011, 30 June 2011, 31 December 2011, 1 January 2012 and 30 June 2012 | 10,000,000,000 | 1,000,000,000 |
| Issued and fully paid: | | |
| At 1 January 2011, 30 June 2011, 31 December 2011, 1 January 2012 and 30 June 2012 | 1,000,000,000 | 100,000,000 |

## 15. SHARE CAPITAL (continued)

| | At 30 June 2012 RMB'000 (unaudited) | At 31 December 2011 RMB'000 (audited) |
|---|---|---|
| Presented in RMB Share capital | **87,680** | 87,680 |

All shares issued rank pari passu with other shares in issue in all respects.

## 16. CAPITAL COMMITMENTS

| | At 30 June 2012 RMB'000 (unaudited) | At 31 December 2011 RMB'000 (audited) |
|---|---|---|
| Capital expenditure contracted for but not provided in the condensed consolidated financial statements in respect of acquisition of: | | |
| Property, plant and equipment | **346,901** | 357,917 |
| Land use right | **15,620** | — |
| | **362,521** | 357,917 |

## 17. COMPARATIVE FIGURES

Certain comparative information has been reclassified to conform to current period presentation in the condensed consolidated statement of comprehensive income.

The effects of the reclassification on line items presented in the condensed consolidated statement of comprehensive income for the six months ended 30 June 2011 of the Group are as follows:

| | As originally stated RMB'000 (unaudited) | Adjustments RMB'000 (unaudited) | As restated RMB'000 (unaudited) |
|---|---|---|---|
| Administrative expenses | (33,266) | 4,360 | (28,906) |
| Other income and other gains and losses | 1,143 | (3,092) | (1,949) |
| Other expenses | — | (1,268) | (1,268) |
| | (32,123) | — | (32,123) |