CHINA SHENGMU ORGANIC MILK LIMITED
中國聖牧有機奶業有限公司

(Incorporated in the Cayman Islands with limited liability)

Stock Code: 1432

2016
ANNUAL REPORT


ORGANIC
FLAVORED FERMENTED
MILK
圣牧|全程有机
有机风味发酵乳
ORGANIC
YOGURT
圣牧|全程有机
有机酸牛奶

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圣牧
ORGANIC MILK
圣牧|全程有机
有机纯牛奶
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有机儿童风味发酵乳

CORPORATE INFORMATION

BOARD OF DIRECTORS

Executive Directors

Mr. YAO Tongshan *(Chairman and Chief Executive Officer)*
Mr. WU Jianye
Ms. GAO Lingfeng
Mr. CUI Ruicheng

Non-executive Directors

Mr. DONG Xianli
Mr. FAN Xiang
Mr. CUI Guiyong
Mr. SUN Qian
Mr. SHAO Genhuo
Mr. ZHANG Jiawang

Independent Non-executive Directors

Mr. WONG Kun Kau
Mr. LI Changqing
Ms. GE Xiaoping
Mr. YUAN Qing
Mr. FU Wenge

JOINT COMPANY SECRETARIES

Mr. CUI Ruicheng
Mr. AU Wai Keung

AUTHORISED REPRESENTATIVES

Mr. CUI Ruicheng
Mr. AU Wai Keung

AUDIT COMMITTEE

Ms. GE Xiaoping *(Chairman)*
Mr. LI Changqing
Mr. CUI Guiyong

REMUNERATION COMMITTEE

Mr. WONG Kun Kau *(Chairman)*
Mr. LI Changqing
Mr. SUN Qian

NOMINATION COMMITTEE

Mr. YAO Tongshan *(Chairman)*
Mr. YUAN Qing
Mr. WONG Kun Kau

REGISTERED OFFICE

P.O. Box 309
Ugland House
Grand Cayman, KY1-1104
Cayman Islands

PRINCIPAL PLACE OF BUSINESS IN HONG KONG

Room 606-607
6/F, China Merchants Building
152-155 Connaught Road Central
Hong Kong

HEADQUARTER AND PRINCIPAL PLACE OF BUSINESS IN CHINA

Food Industry Park, Deng Kou County
Bayannur City
Inner Mongolia Autonomous Region
PRC

STOCK CODE

The Main Board of The Stock Exchange of Hong Kong Limited
1432

PRINCIPAL SHARE REGISTRAR AND TRANSFER OFFICE

Maples Fund Services (Cayman) Limited
P.O. Box 1093, Boundary Hall
Cricket Square
Grand Cayman KY1-1112
Cayman Islands

HONG KONG BRANCH SHARE REGISTRAR AND TRANSFER OFFICE

Tricor Investor Services Limited
Level 22, Hopewell Centre
183 Queen's Road East
Hong Kong

PRINCIPAL BANKERS

Bank of China Limited
(Hohhot Zhongshan Branch)
China Construction Bank Corporation
(Operation Department, Inner Mongolia Autonomous Region Branch)
Bank of Communications Co., Ltd.
(Hohhot, Ulan Branch)
China Minsheng Bank Co., Ltd.
(Hohhot Branch)
China Merchants Bank Co., Ltd.
(Hohhot Branch)
Baoshang Bank Co., Ltd.
(Hohhot Branch)

AUDITOR

Ernst & Young

LEGAL ADVISOR

As to Hong Kong Law

King & Wood Mallesons

As to Cayman Islands Law

Maples and Calder

WEBSITE

http://www.youjimilk.com

LOCATION MAP OF ORGANIC PRODUCTION BASE

YAO Tongshan
Chairman

Dear Shareholders,

I, hereby on behalf of the board of the Company (the "**Board**"), am pleased to present the annual report of the Company and its subsidiaries (collectively referred to as the "**Group**") for the year ended December 31, 2016.

With increasing competition in the dairy industry in the PRC and the upstream raw milk being relatively under pressure, by leveraging on its unique desert-based grass-to-glass organic raw milk based on its unique "desert-based grass-to-glass organic production model", and by benefitting from its innovative grass-to-glass organic liquid milk products for many years and its sophisticated downstream product marketing and sales channel building strategy, China Shengmu continued to record excellent operating results in 2016. The successful development of the grass-to-glass organic liquid milk of the Group delivered an excellent brand image, market awareness and reputation of "Shengmu" brand into the minds of Chinese consumers, forming a stable and increasing consumer group.

According to a research statistical report issued by the AskCI Consulting Co., Ltd. (中商產業研究院) in 2016, the concentration of high-end milk market in the PRC is high. Shengmu's grass-to-glass organic liquid milk accounted for 9.85% and ranked third in terms of overall market share in the PRC high-end milk market.In 2016, Shengmu's grass-to-glass organic liquid milk products have obtained recognition and acclaim from mass consumers and the dairy industry and won a number of awards because of its unique desert-based grass-to-glass production model certified by the E.U., its international first-class product quality and its green, organic and healthy philosophy of life.

The scarcity and advanced nature of Shengmu's unique "desert-based grass-to-glass organic production model" have obtained the recognition and popularity from leading dairy companies at home and abroad in 2016, in order to broaden its global vision, China Shengmu and Food Union (Dairy) Hong Kong Limited ("**Food Union**") established a joint-stock company, Food Union Shengmu Dairy Co., Ltd. ("**Food Union Shengmu**").Leveraging on the opportunity to cooperate with Food Union, China Shengmu will obtain more extensive markets resources and product research resources, and also improve its brand image to generate positive impact for its future development.

In 2016, China Shengmu continued to deploy its unique vertically integrated "desert-based grass-to-glass organic production model" with scientific planning in Ulan Buh Desert in line with international standards. The green ecofriendly production model is the core business model and philosophy of China Shengmu as well as the foundation for China Shengmu to produce quality organic products, enabling it to provide consumers with premium quality and safe grass-to-glass organic dairy products. China Shengmu has persisted with the aims of "being a green industry, it creates value and gives back to the society and benefits the nation and people"for many years. As at the end of 2016, Shengmu

Forage and Shengmu have successfully transformed and greened nearly 200 thousand mu of soil in the hinterland of Ulan Buh Desert and planted tens of millions of trees for sand fixation, successfully transforming barren desert into fertile oasis, which not only actively benefits the national desert treatment, but also significantly reduces the wind and sand encroachment that has been suffered by people living in the surrounding cities for many years. While achieving economic benefits and improving the natural environment, Shengmu has not forgotten to contribute to the society. Shengmu makes effort to support public welfare undertakings to send health, warmth and love to hundreds of armies covering navy, land forces, and air forces nationwide, and people at all levels of society in 2016.

In 2016, with the effort and struggle of all personnel in Shengmu, China Shengmu continued to record excellent operating results and the desert-based grass-to-glass production model developed well. China Shengmu is the largest organic dairy company in the PRC based on the herd size of organic dairy cows and the production volume of organic raw milk for the year ended December 31, 2016.China Shengmu is the only vertically integrated grass-to-glass organic dairy company in the PRC that meets the E.U. organic standards. It is also the only dairy company in the PRC that offers branded organic dairy products that are 100% processed from raw milk produced by self-owned certified organic dairy farms and the only sizeable dairy company in the PRC to operate the "desert-based grass-to-glass organic production model".

"Establishing a Time-honored Shengmu to Benefit People with Organic Products" is the core philosophy of the corporate culture of Shengmu. To realize the dream of organic business, the mission of Shengmu is no longer just for a cup of good milk, but also for the flag on our shoulders to fight for the realization of a more beautiful "desert-based organic dream". As a dreamer to develop organic business, I am proud of my choice, and all personnel in Shengmu are proud of our common ideal. In the future, we will continue to make the desert-based grass-to-glass organic production bigger and more prosperous, thus rewarding our shareholders and the investors with high achievement.

YAO Tongshan
March 20, 2017

MARKET OVERVIEW

In recent years, the problem of domestic environmental pollution in the PRC has been widely recognized and there is increasing awareness of environmental protection by the Chinese government and its people. The green ecofriendly lifestyle has gradually become a new trend, and is recognized and advocated by the Chinese government and by the society at large. With the vigorous development of the organic food market in the PRC, more and more domestic consumers have chosen to buy organic food products, which have obtained extensive recognition and popularity among mass consumers. Meanwhile, the dairy product market in the PRC has begun to generate the "organic effect" and the market share of high-end organic dairy product brands has increased significantly, showing a strong terminal market performance.

According to the "Several Opinions on the Implementation of New Concepts on the Development and the Acceleration of the Agricultural Modernization for the Realization of the Moderate Prosperity in All Respects" (中國國務院《關於落實發展新理念加快農業現代化實現全面小康目標的若干意見》) issued by the State Council of the PRC, in order to promote agricultural sustainable development, the concept that developing green agriculture equals ecological protection must be established, so as to accelerate the formation of a new agricultural development landscape of effective resource utilization, a steady ecological system, good environmental conditions of production areas and safe product quality. At an important Economic Work Conference convened in early 2016, Xi Jinping, President of the PRC, also pointed out that the fundamental purpose of supply-side structural reform was to raise the social production level and to implement the people-oriented development philosophy, "to strengthen premium supply from production areas, reduce ineffective supply and expand effective supply". The above concepts were construed as positive encouragement and explicit support from the Chinese government for a premium, safe, natural and green agricultural industrial system and product supply. The organic green industry and premium organic food market have shown a continuous and rapid growth momentum.

Li Keqiang, Premier of the State Council of the PRC, attended the opening ceremony of the Summer Davos Forum 2016 and delivered a special speech, clearly pointing out that the rapid development of "five happiness industries", including tourism, culture, sports, health and pension, not only boosted the growth of consumption, but also promoted consumption upgrade. Organic food, generally recognized as a representative of heathy food in today's society because of its unique qualities of being premium, safe, natural and green, has obtained popularity and extensive recognition among mass consumers, while organic dairy products, for the characteristics of being green, ecofriendly, natural and being associated with pollution-free production and quality safety, as well as for the significant health care effects of dairy products, have become a high-end representative of a green ecofriendly dairy industry of health and happiness with great future development potential.

The raw milk production base of China Shengmu is located in the Inner Mongolia Autonomous Region, the PRC, the government of which, in early January 2017, issued the "Government Work Report of the Inner Mongolia Autonomous Region 2017", which stated that "the Inner Mongolia Autonomous Region Government had made a good effort to develop modern agriculture and animal husbandry industry in 2016, where the production volume of organic food accounted for more than 1/3 of the production volume of the country" under the conclusion of speeding up industrial transformation and upgrade; the report also specified the work focus of its government in 2017, that is "to promote supply-side structural reform of agriculture and animal husbandry industry, to pay more attention on increasing in the supply of green premium agricultural and livestock products, to vigorously develop modern agriculture and animal husbandry industry, to adjust the structure of agriculture and animal husbandry industry, and to expand the production of green, organic, pollution-free agricultural and livestock products in line with the trend of consumption upgrade".

We believe that based on the support and promotion of national and local governments' industrial policies and the pursuit of people of a happy life, there will be a great potential for the green, healthy, safe, and ecofriendly organic industry.

BUSINESS REVIEW

China Shengmu is the largest organic dairy company in the PRC in terms of the herd size of organic dairy cows and the production volume of organic raw milk for the year ended December 31, 2016. China Shengmu is the only vertically integrated grass-to-glass organic dairy company in the PRC that meets the E.U. organic standards. It is also the only dairy company in the PRC that offers branded organic dairy products that are 100% processed from raw milk produced by self-owned certified organic dairy farms and the only sizeable dairy company in the PRC to operate the "desert-based grass-to-glass organic production model" (沙漠全程有機產業體系).

With increasing competition in the dairy industry in the PRC and the upstream raw milk being relatively under pressure, by leveraging on its unique desert-based grass-to-glass organic raw milk based on its unique "desert-based grass-to- glass organic production model", and by benefitting from its innovative grass-to-glass organic liquid milk products for many years and its sophisticated downstream product marketing and sales channel building strategy, China Shengmu continued to record excellent operating results in 2016. The revenue of the Group amounted to RMB3,466.5 million, representing an increase of 11.8% as compared to 2015, and its gross profit amounted to RMB1,675.4 million, representing an increase of 13.4% as compared to 2015, of which the revenue of grass-to-glass organic liquid milk under its self-owned brand amounted to RMB2,054.3 million, representing an increase of 24.1% as compared to 2015, accounted for 59.3% of the total revenue of the Group in 2016 from 53.4% in 2015. The successful development of the grass-to-glass organic liquid milk of the Group delivered an excellent brand image, market awareness and reputation of "Shengmu" brand into the minds of Chinese consumers, forming a stable and increasing consumer group with a bright prospects.

High-End Organic Liquid Milk Based on China Shengmu's Unique "Desert-Based Grass-to-Glass Organic Production Model" Certified by the E.U. Has Obtained Popularity among Mass Consumers and Markets and Won a Number of Awards

According to a research statistical report issued by the AskCI Consulting Co., Ltd. (中商產業研究院) in 2016, the concentration of high-end milk market in the PRC is high. Through monitoring the market sales data of nationwide large-scale retail enterprises, the top ten brands in the high-end milk market in the PRC accounted for 90.01% market share in total, where Shengmu's grass-to-glass organic liquid milk accounted for 9.85% and ranked third in terms of overall market share in the PRC market, and its market share accounted for 16.24% and its market coverage reached 5.59%. The research data from the AskCI Consulting Co., Ltd. showed that Shengmu's grass-to-glass organic liquid milk was active in the market and obtained popularity among mass consumers.

Shengmu's grass-to-glass organic liquid milk products have obtained recognition and acclaim from mass consumers and the society because of its unique desert-based grass-to-glass production model certified by the E.U., its international first-class product quality and its green ecofriendly organic healthy life philosophy. In the BIOFACH CHINA Organic Trade Fair (中國國際有機食品博覽會) held in May 2016, China Shengmu was awarded Gold Medal jointly by the China Green Food Development Center (中國綠色食品發展中心) and the NürnbergMesse Group for the fifth time. Shengmu grass-to-glass organic liquid milk products won this international honor again because of its excellent product quality and adherence to global highest organic standard, receiving unanimous recognition and acclaim from consumers and professionals at home and abroad. Meanwhile, China Shengmu was also awarded the "Outstanding Exhibitors" award by the Organization Committee of the this expo in recognition of the continuous efforts made by China Shengmu to maintain excellent product quality for many years.

In July 2016, the China Children and Women Industry Expo (中國(北京)國際婦女兒童產業博覽會) 2016 was grandly held at the Beijing National Convention Center with the theme of "green dream +", covering many areas such as women and infants' food, commodities, education and services. Because of its excellent product quality, Shengmu's grass-to-glass organic liquid milk products have won the "2016 Public Thumb Award" in this children and women's expo.

In August 2016, Shengmu's sea buckthorn flavored organic fermented milk was awarded the 2016 "Technical Progress Second Prize" and 2016 "Excellent New Product Award" by the China Dairy Industry Association, showing that Shengmu's grass-to-glass organic liquid milk products have once again obtained the recognition and acclaim from the PRC dairy industry.

The Scarcity and Advanced Nature of Shengmu's Unique "Desert-Based Grass-to-Glass Organic Production Model" Have Obtained the Recognition and Popularity from Leading Dairy Companies

In 2016, in order to broaden its global vision, China Shengmu and Food Union (Dairy) Hong Kong Limited ("**Food Union**") established a joint-stock company, Food Union Shengmu Dairy Co., Ltd. ("**Food Union Shengmu**"), as to which 20% equity interests were owned by the Group. Food Union Shengmu will produce organic products, such as high-end children's dairy products, which are 100% processed from organic raw milk purchased from China Shengmu. Shengmu's unique desert-based grass-to-glass organic production model certified by the E.U. has been recognized by internationally renowned dairy companies such as Food Union because of its scarcity and advanced nature all over the world. Food Union has extensive product research and development experience in the processing field of high-end dairy products, together with excellent brand awareness and abundant resources of market channels. Leveraging on the opportunity to cooperate with Food Union, China Shengmu will obtain more extensive markets resources and product research resources, and also improve its brand image to generate positive impact for its future development.

Being a Green Industry, It Creates Value and Gives Back to the Society and Benefits the Nation and People

The "desert-based grass-to-glass organic production model" was initiated by China Shengmu in the PRC, which provides the foundation for China Shengmu to produce quality organic products and is also necessary for China Shengmu to establish its sustainable ecological circle. Based on the theory of "sand-to-grass industry" initiated by Mr. Qian Xuesen, a renowned scientist, China Shengmu has transformed barren land in the desert into an oasis to grow economic crops. As such, economic benefits have been generated while sustainable green development has been achieved. As at the end of 2016, Shengmu Forage and Shengmu has successfully transformed and greened nearly 200 thousand mu of soil in the hinterland of Ulan Buh Desert and planted tens of millions of trees for sand fixation, successfully transforming barren desert into fertile oasis, which not only actively benefits the national desert treatment, but also significantly reduces the wind and sand encroachment that has been suffered by people living in the surrounding cities for many years.

While achieving economic benefits and improving the natural environment, Shengmu has not forgotten to contribute to the society and make effort to support public welfare undertakings to send health, warmth and love to people at all levels of society.

When meeting the national model representatives of the National Double Support Models in July 2016, the General Secretary, Xi Jinping, pointed out that "double support work is a unique good tradition and political advantage for our party, our military and our people. Rock-firm unity of the military and government, as well as the military and people, has always been crucial for us to overcome all difficulties and continue to succeed from one to another." In response to the General Secretary's call for double support work and to learn the army's spirit of fearlessness of danger and difficulties, as well as overcoming difficulties and marching forward bravely, and to incorporate such spirits into the management culture of the Company, China Shengmu spontaneously organized a large team to support the military,along with many enterprises and civil bodies and institutions including religious groups, to encourage hundreds of armies covering navy, land forces, and air forces nationwide, and also donated Shengmu's best grass-to-glass organic liquid milk products to the most lovable people defending our homeland, which brought enthusiastic social response and encouraged a new trend for social teams to express patriotism spontaneously.

Desert before improvement

Desert after improvement

In 2016, while performing its corporate responsibilities, China Shengmu continued to participate in many social welfare activities such as organizing to visit the elderly and physically handicapped persons in domestic charity houses, donating to Hope Primary School and primary schools for peasant workers' children, encouraging cleaner teams and donating to various charities, and actively carried out public welfare undertakings, as well as actively gave back to the society and benefited the people while creating economic value.

Shengmu's Unique Vertically Integrated "Desert-Based Grass-to-Glass Organic Production Model" Continued to Develop in 2016

In 2016, China Shengmu continued to deploy its unique vertically integrated "desert-based grass-to-glass organic production model" with scientific planning in Ulan Buh Desert in line with international standards. The green ecofriendly production model is the core business model and philosophy of China Shengmu as well as the foundation for China Shengmu to produce quality organic products, enabling it to provide consumers with premium quality and safe grass-to-glass organic dairy products.

In 2016, China Shengmu continued to achieve its organic quality control across the vertically integrated production chain covering planting, farming and processing from farming of organic cows to production of organic liquid milk through developing an organic environment, monitoring the growing of organic forage and establishing self-owned dairy farms.

Farming Business

Organic Dairy Farming

As the key component of China Shengmu's "desert-based grass-to-glass organic production model", the Group continued to invest in and manage organic dairy farming and organic raw milk production in 2016.

Since its establishment seven years ago, China Shengmu has persisted with a scientific and innovative development strategy. Our dairy farming business is premised on scale of economy, and most farms have 3,500-4,500 dairy cows. Meanwhile, our dairy farming business has always persisted with the breeding of dairy cows in the golden regions of milk resources which is the most suitable place for dairy cows to grow. Especially, Shengmu's organic dairy farms are all located in the hinterland of Ulan Buh Desert whose unique geographic location has many more advantages as compared with the PRC's traditional farming environment of golden regions of milk resources. In this region, Shengmu has persisted with the combination model of planting and farming, being "to plant forage with farming and to breed cows with forage". On one hand, the dairy cow dung in the organic farm can be used as fertilizer to form an organic ecological circle. On the other hand, the strong and long-time sunshine in the desert helps forage grow and enables dairy cows to transform plant protein to animal protein so as to increase the calcium content in the milk to further improve the quality of milk.

In 2016, the Group used internationally advanced feed management system and equipment, in conjunction with its self-developed feed formulae and scientific management model, to ensure that each of its organic dairy cows grows healthily. To promote the health of dairy cows, ensure the milk production quality and provide a more comfortable environment for dairy cows to grow, Shengmu continued to manage the farm in a refined and precise way and carried out over 20 technical innovation projects such as "automatically feeding equipment for acidified milk", "automatically milking system" and "application equipment of air power" in 2016, thereby increasing production efficiency and obtaining good operation optimization on the premise of improving wellbeing of dairy cows.

Herd Size and Production

As at December 31, 2016, the Group had 23 organic dairy farms in operation, and 12 non-organic farms in operation. The organic and non-organic herd size of the Group have changed from 72,843 and 38,552 dairy cows as at December 31, 2015 to 94,815 and 34,514 dairy cows as at December 31, 2016, respectively.

	As at 31 December							
	2016				2015			
	Number of Dairy farms	Calves and heifers	Milkable cows	Dairy Cows Subtotal	Number of Dairy farms	Calves and heifers	Milkable cows	Dairy Cows Subtotal
Organic	23	45,534	49,281	94,815	21	30,049	42,794	72,843
Non-organic	12	13,908	20,606	34,514	12	14,556	23,996	38,552
Total	35	59,442	69,887	129,329	33	44,605	66,790	111,395

The Group produced 421,023 tonnes of organic raw milk and 177,356 tonnes of premium non-organic raw milk in 2016, and produced 357,434 tonnes of organic raw milk and 179,866 tonnes of premium non-organic raw milk in 2015.

Organic Forage Planting

Forage is an essential raw material in organic dairy farming. Pursuant to a long-term strategic cooperation agreement entered into with us, Shengmu Forage continues to exclusively supply organic forage to us. In 2016, in order to persist in the philosophy that "all staff participate in the organic management", Shengmu Forage has entered into the Organic Management Agreement with its staff to divide responsible areas of organic management and carry out non-scheduled internal checks so as to ensure the precise and effective implementation of the organic management. In order to achieve its precise and refined management objectives, during this year, Shengmu Forage sowed seeds in its sprinkler irrigation fields with comprehensive adoption of a GPS system, thereby enhancing its precise sowing standard in its drip irrigation fields, and installed scribers to enhance planting uniformity and adopt rational close planting, while continuing to use green organic cow dung to thicken the humus layer of soil, so as to improve the fertility of original organic planting fields to make them more suitable for the growth of natural plants, which ensured the improvement of production volume and quality of forage planting.

Shengmu Forage has greened nearly 200 thousand mu of organic planting fields in aggregate in the hinterland of Ulan Buh Desert as at the end of 2016. With continuous production of organic forage and expansion of new planting fields, the green area in the hinterland of Ulan Buh Desert has been enlarged significantly, with annual precipitation having obviously increased, showing a remarkable achievement of desert control. On the other hand, in order to safeguard the organic planting environment in the desert and to block the wind and sand encroachment, Shengmu Forage and Shengmu have also continued to proceed with sand fixation afforestation in the hinterland of Ulan Buh Desert and to plant tens of millions of trees for all types of sand fixation, greening and safeguarding these areas to create plant zones for sand fixation and windbreaks, thus achieving a glorious transformation from barren desert to fertile oasis and facilitating the desert control of the country.

Liquid Milk Business

All the raw milk used by China Shengmu to produce grass-to-glass organic liquid milk products under its self-owned brand was supplied internally by its organic dairy farms without adding any preservatives, artificial coloring and artificial flavoring during the production process. Each of our organic milk products is stamped with a code of Certification and Accreditation Administration of the People's Republic of China for consumers to trace the production origin of every batch of products at any time, which provides for the safety of products and also provides that the grass-to-glass organic process can be traceable.

In 2016, the liquid milk business department implemented refined and precise management based on the theme of "refined practice and efficient operation" for the purposes of guaranteeing the quality of organic products, optimizing the standardization process of key businesses, overcoming and preventing equipment failures, carrying out clear and detailed overhaul, maintenance and inspection of work, and upgrading equipment to a leading level among industry peers. While enhancing efficiency, the Group achieved a flat management and performance management system with respect to all staff through precise management, optimization of work process and consolidation of management structure, thereby leading to the quality of grass-to-glass organic liquid milk products further improving during this year.

There is an aggregate of 16 production lines of liquid milk products operated by the Group during the year, and the production volume of organic liquid milk products under its self-owned brand which were entirely processed from raw milk produced by self-owned certified organic dairy farms increased to 197,276 tonnes as compared to 135,960 tonnes for the year of 2015.

Unique Sales Channel Development and Brand Promotion Development for Grass-to-Glass Organic Liquid Milk Products

In 2016, based on its current sales network covering first and second tier cities and major third and fourth tier cities, the Group continued to expand its market network to third and fourth tier cities. Furthermore, the Group continued to optimize its market network management at all levels, to consolidate and further develop its sales channels and to improve the management of individual shops so as to increase the sales revenue from such markets, channels and shops. The Group has upgraded its model for distribution network development from horizontal expansion at early stage to vertical deepening.

In 2016, the Group continued to implement the "blue ocean" strategy and community flagship store strategy to develop large chain-community stores. Shengmu products have entered into over 100,000 large chain-community stores and community flagship stores with independent promotional counters and a good image across the country, which effectively enhanced the awareness of its liquid milk products among target consumers and made substantial contribution to the increase in the sales of its liquid milk products.

In 2016, with the increase in the downstream sales business, the Shengmu organic liquid milk brand continued to make headlines in the market and gained extensive attention across the whole society. The feature film *Conquering the Flaming Mountain with Bare Feet (《赤腳踏平火焰山》),* produced by CCTV jointly with China Shengmu, was on the air on CCTV 7 and the website of CCTV, to publicise China Shengmu's unique desert-based grass-to-glass organic production model, premium organic liquid milk products and its organic, green and ecofriendly production and the lifestyle and values consistently followed by China Shengmu. China Shengmu's organic planting fields located in the hinterland of Ulan Buh Desert was also chosen by CCTV as the representative of autumn harvest scene for nationwide advertisement. In addition, many renowned media at home and abroad also reported positive hot news about China Shengmu.

In 2016, China Shengmu hosted the large scale event, "Shengmu Desert Organic Journey", and accommodated a number of consumers at its production base in the Ulan Buh Desert to gain personal experience of its "grass-to-glass organic production model" in order to promote the organic concept and promote the industrial, green and ecofriendly philosophy, so as to further facilitate the people of the PRC to understand our green, organic and sustainable industry model. Through "Shengmu Desert Organic Journey", in addition to the visitors' better knowledge of the "desert-based grass-to-glass organic production model" of China Shengmu, the understanding of and confidence in the Group's products by the market have been enhanced, and the brand awareness and reputation of China Shengmu have been increased.

At the same time, China Shengmu continued its refined and precise marketing strategy and carried out a comprehensive, extensive and precise brand promotion campaigns through opening standardized large chain-community stores and launching large nationwide "product-experience" promotion activities, with the support from broadcasting advertisements through online, offline and media (including TV) channels. Meanwhile, we delivered speeches on the theme of "having courage to challenge the impossible and pursue an organic dream in the desert" in over 20 universities nationwide in 2016 to encourage undergraduates to confront challenges and practice green ecology. The implementation of every precise marketing strategy by the Group for the year has substantially enhanced the brand recognition and awareness of the "Shengmu" brand among a wide range of consumers and has effectively established its image of "No. 1 organic milk brand" in the PRC.

Revolutionary Innovation in the Industry — Shengmu Yogurt Machines

In May 2016, China Shengmu grandly launched its unique yogurt machines, the technology of which is owned by China Shengmu. China Shengmu yogurt machines can produce fresh and delicious low-temperature organic liquid milk products immediately on site with China Shengmu organic liquid milk products through refrigerating them and adding active lactobacillus, dispensing with the shackles of traditional cold-chain logistic transportation and storage in cold warehouses of supermarkets for low temperature organic milk products. China Shengmu yogurt machines can offer healthy, fresh and delicious low-temperature organic liquid milk products directly to crowded public venues such as restaurants and canteens, office and entertainment areas, which effectively further develops the "blue ocean" marketing strategy by offering premium fresh low-temperature organic liquid milk products directly to consumers while deducting the middle sales and logistic sections and effectively lowering cost of sales. As at the end of 2016, China Shengmu yogurt machines have already been placed in public venues such as crowded restaurants and canteens, as well as office and entertainment areas across dozens of cities including Beijing, Shanghai, Guangzhou, Shenzhen, etc. The launch of this revolutionary product with its independent research and development technology guides brand new development direction for the sales of high-end liquid milk products and provides steady sales channels of liquid milk for dairy companies with whole industrial chain model, effectively enhancing the ability to use its own raw milk and providing unique and positive support for the continuous and rapid growth of China Shengmu.

FINANCIAL REVIEW

The Group recorded a revenue of RMB3,466.5 million in 2016, representing an increase of 11.8% from RMB3,100.7 million in 2015. Gross profit of the Group increased by 13.4% from RMB1,477.5 million in 2015 to RMB1,675.4 million in 2016. Profit attributable to owners of the parent decreased by 15.0% from RMB800.7 million in 2015 to RMB680.6 million in 2016.

Analysis on Consolidated Statement of Profit or Loss and Other Comprehensive Income

Revenue

Unit: RMB in thousands, except percentages

	Dairy farming business				Liquid milk business				
For the year ended December 31,	Segment revenue	Inter-segment sales[(1)]	External sales	External sales as % of total revenue	Segment revenue	Inter-segment sales	External sales	External sales as % of total revenue	Total revenue
2016	**2,662,954**	**1,302,553**	**1,360,401**	**39.2%**	**2,106,143**	**—**	**2,106,143**	**60.8%**	**3,466,544**
2015	2,521,395	1,076,373	1,445,022	46.6%	1,655,689	—	1,655,689	53.4%	3,100,711

(1) Represents self-produced raw milk sold to the Group's liquid milk business.

In 2016, revenue of the Group continuously increased by 11.8% from 2015. Revenue from self-owned brand liquid milk business increased by approximately 27.2% from 2015, and accouted for 60.8% of total revenue (2015: 53.4%), implicating a rising core position of the self-owned brand liquid milk business in the overall businesses of the Group and in contributing to the overall growth of the Group's revenue. Against the backdrop of intensified competition in the PRC dairy industry and relatively higher pressure on upstream raw milk, the Group has developed its unique "desert-based-grass-to-glass organic production model" in a stable and healthy manner, which was proved to be strategically forward-looking.

Dairy Farming Business

	For the year ended 31 December							
	2016				2015			
	Revenue (RMB'000)	Sales volume (Tonnes)	Average selling price (RMB/Tonne)	Revenue as % of dairy farming segment revenue	Revenue (RMB'000)	Sales volume (Tonnes)	Average selling price (RMB/Tonne)	Revenue as % of dairy farming segment revenue
Organic raw milk								
External sales	**784,631**	**166,986**	**4,699**	**29.5%**	712,677	139,290	5,116	28.3%
Inter-segment sales[(1)]	**1,222,020**	**228,761**	**5,342**	**45.9%**	1,076,373	202,352	5,319	42.7%
Subtotal	**2,006,651**	**395,747**	**5,071**	**75.4%**	1,789,050	341,642	5,237	71.0%
Premium non-organic raw milk								
External sales	**575,770**	**156,455**	**3,680**	**21.6%**	732,345	173,026	4,233	29.0%
Inter-segment sales[(2)]	**80,533**	**18,765**	**4,292**	**3.0%**	—	—	—	0.0%
Subtotal	**656,303**	**175,220**	**3,746**	**24.6%**	732,345	173,026	4,233	29.0%
Dairy farming segment	**2,662,954**	**570,967**	**4,664**	**100.0%**	2,521,395	514,668	4,899	100.0%

(1) Represents self-produced organic raw milk sold to the Group's organic liquid milk business.

(2) Represents self-produced premium non-organic raw milk sold to the Group's high-end non-organic liquid milk business.

Revenue from dairy farming segment continued to record an increase from RMB2,521.4 million in 2015 to RMB2,663.0 million in 2016. By benefitting from the stable and quick development of Shengmu's "desert-based-grass-to-glass organic production model", up to 57.8% of total growing organic raw milk sales volume was sold for the production of self-owned brand organic liquid milk products in order to meet growing end market needs. Revenue from inter-segment sales to organic liquid milk processing plant accounted for 45.9% of revenue from dairy farming segment (2015: 42.7%). With further market expansion and penetration of Shengmu's self-owned brand organic liquid milk products, the self-owned brand organic liquid milk business will continue to drive the growth of dairy farming business.

Liquid milk business

Revenue from liquid milk business increased by 27.2% from RMB1,655.7 million in 2015 to RMB2,106.1 million in 2016, accounting for 60.8% of total revenue of the Group (2015: 53.4%). Revenue from self-owned brand organic liquid milk business increased by 24.1% from RMB1,655.7 million in 2015 to RMB2,054.3 million in 2016, accounting for 59.3% of total revenue of the Group. The stable development of liquid milk business was mainly attributable to the brand awareness, market profile and reputation of Shengmu's organic liquid milk products, which secures stable and growing consumers in the PRC. Meanwhile, the unique construction of distribution channels and brand marketing by the Group further improved the market share of its self-owned brand organic liquid milk products. Driven by liquid milk business, revenue from organic business (comprising organic liquid milk business and organic raw milk business) accounted for 81.9% of total revenue of the Group (2015: 76.4%). The "desert-based grass-to-glass organic production model" of Shengmu is more mature, representing a momentum for business growth of the Group.

Organic liquid milk business

	For the year ended December 31,		
	2016	2015	Increase/ (Decrease)
Revenue (RMB'000)	**2,054,292**	1,655,689	24.1%
Sales volume (Tonnes)	**186,393**	145,214	28.4%
Average selling price (RMB/Tonne)	**11,021**	11,402	(3.3%)

Revenue from Organic/Non-organic Business and Percentages

Unit: RMB in thousands, except percentages

	For the year ended December 31,			
	2016		2015	
	Amount	Percentage	Amount	Percentage
Organic products				
Organic liquid milk	2,054,292	59.3%	1,655,689	53.4%
Organic raw milk	784,631	22.6%	712,677	23.0%
Subtotal of organic products	2,838,923	81.9%	2,368,366	76.4%
Non-organic products				
Premium non-organic raw milk	575,770	16.6%	732,345	23.6%
High-end non-organic liquid milk	51,851	1.5%	—	—
Subtotal of non-organic products	627,621	18.1%	732,345	23.6%
Total	3,466,544	100.0%	3,100,711	100.0%

Cost of Sales, Gross Profit and Gross Margin

	For the year ended December 31,					
	2016			2015		
	Cost of sales	Gross profit	Gross margin	Cost of sales	Gross profit	Gross margin
	(RMB in thousands, except percentages)					
Dairy farming business						
Organic raw milk						
Before elimination	965,276	1,041,375	51.9%	902,814	886,236	49.5%
After elimination(1)	407,299	377,332	48.1%	368,084	344,593	48.4%
Premium non-organic raw milk						
Before elimination	434,862	221,441	33.7%	456,719	275,626	37.6%
After elimination(3)	388,292	187,478	32.6%	456,719	275,626	37.6%
Subtotal of dairy farming business						
Before elimination	1,400,138	1,262,816	47.4%	1,359,533	1,161,862	46.1%
After elimination	795,591	564,810	41.5%	824,803	620,219	42.9%
Liquid milk business						
Organic liquid milk						
Before elimination	1,615,850	438,442	21.3%	1,267,411	388,278	23.5%
After elimination(2)	969,298	1,084,994	52.8%	798,365	857,324	51.8%
High-end non-organic liquid milk						
Before elimination	51,702	149	0.3%	—	—	0.0%
After elimination(3)	26,244	25,607	49.4%	—	—	0.0%
Subtotal of liquid milk business						
Before elimination	1,667,552	438,591	20.8%	1,267,411	388,278	23.5%
After elimination	995,542	1,110,601	52.7%	798,365	857,324	51.8%
Total	1,791,133	1,675,411	48.3%	1,623,168	1,477,543	47.7%

(1) Represents gross profit after elimination of internal profit attributable to inter-segment sales of organic raw milk. Such internal profit is calculated as the difference of (i) the inter-segment sales of organic raw milk used in our liquid milk business and (ii) the production costs for such organic raw milk calculated as the product of (a) total cost of sales of organic raw milk plus (b) the volume of organic raw milk sold to our liquid milk business divided by total sales volume of organic raw milk.

(2) Represents gross profit after adding back the internal profit attributable to inter-segment sales of organic raw milk. Such internal profit is arrived at by calculating the difference of (i) the inter-segment sales of organic raw milk used in this segment and (ii) the production costs for such organic raw milk, calculated using the formula in note (1) above.

(3) Premium non-organic raw milk after elimination is calculated using the formula in note (1) above, and the premium non-organic liquid milk after elimination is calculated using the formula in note (2) above.

Cost of sales of the Group increased from RMB1,623.2 million in 2015 to RMB1,791.1 million in 2016. Gross profit increased from RMB1,447.5 million in 2015 to RMB1,675.4 million in 2016. Gross profit margin increased from 47.7% in 2015 to 48.3% in 2016.

In 2016, cost of sales of the Group increased by 10.3% from 2015, lower than 11.8% increase of revenue, mainly attributable to the Group's effective control and reduction of production and procurement cost of the whole production chain by continuous implementation of the precision and meticulous management model. Meanwhile, further increased contribution from high profit margin business, such as organic business (in particular, the self-owned brand organic liquid milk business), to the total revenue of the Group compared with 2015 resulted in a 13.4% increase in gross profit of the Group in 2016.

Overall, though affected by intensified competition in the dairy industry and relatively higher pressure on upstream raw milk, the consolidated gross margin of the Group increased from 47.7% in 2015 to 48.3% in 2016, attributable to (1) decrease in its average unit cost as a result of enhancement of economics of scale and increase in efficiency resulting from the scale expansion of the Group; and (2) increase in the percentage of revenue from organic raw milk and organic liquid milk with higher gross margin to total revenue as for product structure.

Other Income and Gains/(Losses)

Other income and gains/(losses) of the Group decreased from a net gain of RMB47.4 million in 2015 to a net loss of RMB87.1 million in 2016, mainly attributable to the provision for impairment of trade receivables referring to the collectability of individual account receivables and aging analysis by the Group.

Selling and Distribution Expenses

Selling and distribution expenses of the Group primarily include logistics and transportation expenses, warehouse fees and relevant employees' remunerations. In 2016 and 2015, selling and distribution expenses of the Group were RMB287.9 million and RMB265.5 million, accounting for 8.3% and 8.6% of revenue, respectively.

Administrative Expenses

Administrative expenses mainly include salary and welfare, travel expenses and transportation expenses of management and administrative employees. In 2016 and 2015, administrative expenses of the Group were RMB141.7 million and RMB107.5 million, accounting for 4.1% and 3.5% of revenue, respectively. Such increase in administrative expenses as a percentage of revenue in 2016 was mainly due to increase of equity-settled share option expense compared with 2015. Excluding this, administrative expenses of the Group accounted for 2.8% and 2.6% of revenue in 2016 and 2015 respectively.

Net Gains or Losses Arising from Changes in Fair Value Less Costs to Sell of Biological Assets

Net gains or losses arising from changes in fair value less costs to sell of biological assets represents fair value changes in the dairy cows, due to the changes in physical attributes and market prices of the dairy cows and discounted future cash flow to be generated by those cows. In general, when a heifer grows into a milkable cow, its value increases, as the discounted cash flow from milkable cow is higher than the selling price of heifer. Further, when a milkable cow is ousted and sold, its value decreases.

The Group recorded net gains or losses arising from changes in fair value less costs to sell of biological assets of RMB-15.7 million and RMB52.7 million in 2016 and 2015 respectively. The changes in fair value less costs to sell of biological assets in 2016 decreased as compared to 2015 and recorded a net loss, mainly because the net losses arising from changes in fair value less costs to sell of biological assets associated with non-organic dairy cows was higher than the net gains arising from changes in fair value less costs to sell of biological assets associated with organic dairy cows.

Major Investment

During 2016, as an effort to expand its international business horizon, the Group established Food Union Shengmu Dairy Co., Ltd. (富友聯合聖牧乳品有限公司) ("**Food Union Shengmu**"), a joint-stock company with Food Union (Dairy) Hong Kong Limited ("**Food Union**"). The Group holds 20% equity interest in Food Union Shengmu. Food Union Shengmu will produce organic dairy products including high-end children dairy products, with all the organic raw milk to be purchased from the Group. Food Union and the Group invest in Food Union Shengmu and provide financing support based on the contract. During 2016, the Group invested approximately RMB75.2 million in Food Union Shengmu and provided guarantee of approximately RMB51.5 million for its bank borrowings.

Other Expenses

In 2016, the Group incurred other expenses of RMB56.2 million, mainly as Shengmu offered strong support to social public welfare during the year to contribute to the society while seeking economic and environmental efficiency.

Share of Profits and Losses of Associates

The associates mainly include (a) the companies that were jointly established by the Group and its premium distributors in its key distribution cities to distribute the liquid milk products with the Group's self-owned brand; and (b) Bayannur Shengmu High-tech Ecological Forage Co., Ltd. (巴彥淖爾市聖牧高科生態草業有限公司) and its subsidiary ("**Shengmu Forage**") in which the Group invested and held minority interests; and (c) Food Union Shengmu and Inner Mongolia Shengmu Low Temperature Dairy Product Company Limited (內蒙古聖牧低溫乳品有限公司) in which the Group invested and held minority interests and which produce dairy products with the raw milk to be purchased from the Group. The Group recorded share of losses of associates of RMB16.2 million and RMB18.0 million in 2016 and 2015 respectively.

Income Tax Credit/(Expense)

All profits of the Group was derived from its operations in the PRC. According to the Enterprise Income Tax Law of the PRC (the "**EIT Law**"), the Group's subsidiaries in the PRC are generally subject to a corporate income tax at a rate of 25%. According to the preferential provisions of the EIT Law, the Group's income arising from agricultural activities, such as dairy farming and processing of raw agricultural products, is exempted from enterprise income tax. Under the PRC tax laws and regulations, there is no statutory time limit for such tax exemption as long as the relevant PRC subsidiaries of the Group complete filings with the relevant tax authorities as required.

In accordance with "The Notice of Tax Policies Relating to the Implementation of the Western China Development Strategy" jointly issued by Ministry of Finance, General Administration of Customs and State Administration of Taxation (財政部、海關總署、國家税務總局《關於深入實施西部大開發戰略有關税收政策問題的通知》(財税[2011]58號)), the Group's taxable income arising from processing of non-raw agricultural products is subject to preferential tax rate of 15% from 2013 to 2020.

Income tax credit of the Group was RMB11.1 million in 2016 while income tax expense of the Group was RMB4.6 million in 2015, among which current income tax expenses were RMB12.5 million and RMB4.8 million respectively. Based on the percentage of the current income tax expenses of the profit before tax, the effective enterprise income tax rate of the Group was 1.3% and 0.4% for 2016 and 2015 respectively.

Profit Attributable to Owners of the Parent and Profit Attributable to Non-controlling Interests

Profit attributable to non-controlling interests mainly represents the profit entitled to the non-controlling equity interests in the Group's farms held by dairy farmers with whom the Group cooperates in relation to farm management. In 2016 and 2015, profit attributable to owners of the parent were RMB680.6 million and RMB800.7 million, and profit attributable to non-controlling interests were RMB276.2 million and RMB282.6 million, respectively.

Profit attributable to owners of the parent in 2016 decreased by RMB120.1 million compared with 2015, mainly due to the provision of RMB86.3 million for impairment of trade receivables for the year and donation of RMB56.2 million occurred by the Group for exerting great efforts in public welfare undertakings in 2016. As such, the profit attributable to owners of the parent in 2016 decreased by 15.0% compared with 2015.

ANALYSIS ON CONSOLIDATED STATEMENT OF FINANCIAL POSITION

Current Assets

As at December 31, 2016, the total current assets of the Group were RMB3,665.3 million (RMB4,010.3 million as at December 31, 2015), primarily consisting of inventories of RMB928.8 million (RMB824.5 million as at December 31, 2015), trade and bills receivables of RMB1,108.7 million (RMB915.3 million as at December 31, 2015), prepayments, deposits and other receivables of RMB393.6 million (RMB468.5 million as at December 31, 2015) and cash and bank balances available-for-sale investments and pledged deposits of RMB1,234.2 million (RMB1,802.0 million as at December 31, 2015).

Trade and bills receivables

Unit: RMB in thousands, except percentages

	As at	
	December 31, 2016	December 31, 2015
Trade and bills receivables	1,194,299	915,681
Impairment	(85,512)	(369)
Total	1,108,787	915,312

	As at			
Aging	December 31, 2016		December 31, 2015	
	Amount	Percentage	Amount	Percentage
Within 6 months	815,914	73.6%	851,948	93.1%
7 to 12 months	268,863	24.2%	60,042	6.5%
Over 1 year	24,010	2.2%	3,322	0.4%
Total	1,108,787	100.0%	915,312	100.0%

Trade and bills receivables of the Group increased substantially as compared to last year, mainly attributable to the increase in revenue from self-owned brand liquid milk products as the Group took into consideration the recovery days of the receivables from terminal supermarkets and department stores and aimed to increase and consolidate its share in organic liquid milk market.

The Group formulated its policy in respect of making provisions for asset impairment based on the practical situation of production and operation. Based on such policy, the Group determined the receivables group based on the aging as the credit risk characteristics, made provisions for bad debt of receivables and other receivables through aging analysis, and estimated the provisions for asset impairment based on recoverability of individual receivables and customer creditworthiness at the same time. In 2016, the Group made a total provision of RMB86.3 million for the impairment of receivables.

Current Liabilities

As at December 31, 2016, the total current liabilities of the Group amounted to RMB2,292.3 million (RMB2,975.6 million as at December 31, 2015), primarily consisting of trade and bills payables of RMB920.6 million (RMB1,018.1 million as at December 31, 2015), receipts in advance of RMB13.2 million (RMB17.3 million as at December 31, 2015), other payables and accruals of RMB438.5 million (RMB338.3 million as at December 31, 2015), interest-bearing bank and other borrowings of RMB918.4 million (RMB1,599.9 million as at December 31, 2015), and income tax payable of RMB1.6 million (RMB2.0 million as at December 31, 2015). Current liabilities of the Group as at December 31, 2016 decreased substantially as compared to December 31, 2015, primarily because the Group repaid short-term borrowings due with the proceeds from the issue of long-term corporate bonds and began to partially obtain financing by the way of offshore directional borrowings in 2016, optimizing the debt structure of the Group while enriching the forms of financing.

Non-Current Liabilities

As at December 31, 2016, the total non-current liabilities of the Group amounted to RMB1,859.9 million (RMB1,117.0 million as at December 31, 2015), primarily consisting of interest-bearing bank and other borrowings of RMB1,752.0 million (RMB1,117.0 million as at December 31, 2015) and long-term payables of RMB107.9 million. The substantial increase in the non-current liabilities as at December 31, 2016 as compared to December 31, 2015 is primarily due to the increase in the long-term interest-bearing bank and other borrowings resulted from the issue of RMB600 million long-term corporate bonds by the Group in 2016. Such issue of corporate bonds optimized the Group's debt structure and reduced its overall financing cost rate.

Foreign Exchange Risk

The Group's businesses are principally located in the mainland China and substantially all transactions are conducted in RMB. As at December 31, 2016, the Group did not have significant foreign currency exposure from its operations, except interest-bearing bank borrowings equivalent to approximately RMB70.8 million which were denominated in Euros, bank balances equivalent to approximately RMB11.9 million and RMB0.8 million which were denominated in Hong Kong dollars and United States dollars, respectively. In 2016, the Group did not enter into any arrangements to hedge against any fluctuation in foreign exchange.

Credit Risk

The Group only trades with recognized and creditworthy third parties. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. As the Group's trade receivables relate to a large number of diversified customers, there is no significant concentration of credit risk. Since the Group trades only with recognized and creditworthy third parties, collateral is not required.

Charge on Assets

As at December 31, 2016, the Group has pledged deposits in the amount of approximately RMB66.8 million (RMB70.3 million as at December 31, 2015) to banks in the PRC as deposits for the issuance of letters of credit and bank drafts.

Liquidity, Financial Resources and Capital Structure

In 2016, the Group financed its daily operations mainly from internally generated cash flows and bank and other borrowings. As at December 31, 2016, the Group had (a) cash and bank balances of RMB1,047.4 million (RMB1,731.8 million as at December 31, 2015), and (b) interest-bearing bank and other borrowings of RMB2,670.4 million (RMB2,716.9 million as at December 31, 2015), of which, RMB1,686.5 million were repayable within one to five years and RMB65.4 million repayable within five to eight years, while the remaining interest-bearing bank and other borrowings were repayable within one year. The gearing ratio (calculated as total debt (total interest bearing bank and other borrowings) divided by total equity) was 42.1% as at December 31, 2016 (50.6% as at December 31, 2015). Except bank and other borrowings equivalent to RMB70.8 million which are denominated in Euros and bear fixed interest rates, the Group's remaining bank and other borrowings are denominated in RMB and bear fixed interest rates. In 2016, the annual interest rate of bank and other borrowings was 1.55% to 5.87% (2015: 4.48% to 7.14%). In 2016, the Group started to partially obtain financing by the way of offshore directional borrowings, which reduced the financing cost while enriching the ways of financing.

ENVIRONMENTAL POLICIES AND PERFORMANCE

The Group's operations were in compliance in all material respects with currently applicable national and local environmental protection laws and regulations in the PRC in 2016.

CAPITAL COMMITMENTS

As at December 31, 2016, the Group's capital commitments amounted to RMB352.6 million (RMB201.2 million as at December 31, 2015), primarily relating to the expansion of liquid milk production capacity by investing and constructing new production plants and production lines for liquid milk business in 2016, in order to keep up with the rapid development of the downstream self-owned brand liquid milk business of Shengmu's desert-based grass-to-glass organic production model. The Group has sufficient internal and financial resources to fund its capital expenditures.

HUMAN RESOURCES

As at December 31, 2016, the Group had a total of 3,849 employees (3,713 employees in total as at December 31, 2015). Total staff costs for 2016 (including the emoluments of Directors and senior management of the Company) amounted to RMB280.2 million (excluding equity-settled share option expenses) (RMB258.7 million in 2015).

The Group believes that the dedicated efforts of all of its employees are the very essence of the Group's rapid development and success in the future. The Group provides management personnel and employees with on-the-job education, training and other opportunities to improve their skills and knowledge. In general, the Group determines employee compensation based on each employee's performance, qualifications, position and seniority. The Group has made contributions to the social security funds and housing reserve for its employees in accordance with the relevant national and local social welfare laws and regulations.

The Group has also approved and adopted a pre-IPO share option scheme (the "**Pre-IPO Share Option Scheme**") and a share option scheme (the "**Share Option Scheme**"). The purpose of the Pre-IPO Share Option Scheme and the Share Option Scheme is to attract, retain and motivate the Directors, senior management and employees of the Group and other participants.

CONTINGENT LIABILITIES

For the year and as at December 31, 2016, the Group provided guarantees with amounts of RMB300,000,000 (2015: RMB300,000,000) and RMB51,450,000 (2015: Nil) for the bank loans of Shengmu Forage and Food Union Shengmu, respectively.

MATERIAL ACQUISITIONS AND DISPOSALS

The Company did not make any material acquisitions and disposals of subsidiaries and associated companies in 2016.

FUTURE PLANS FOR MATERIAL INVESTMENTS OR ACQUISITION OF CAPITAL ASSETS AND EXPECTED SOURCE OF FUNDING

Save as disclosed above in connection with capital commitments under the paragraph headed "Capital Commitments" and in the prospectus under the section headed "Future Plans and Use of Proceeds", the Group does not have any plan for material investments or acquisition of capital assets as at the date of this announcement.

OUTLOOK

The Group's long-term objective is to become a leading organic dairy company in the world.

Continue to Increase the Investment of Organic Dairy Farms to Build the Most Beautiful Organic Dairy Farms

In 2017, the Group intends to continue to increase the investment of organic dairy farms to build comfortable garden-like organic dairy farms, so as to further improve the herd growing environment and staff working environment and the whole environment of the dairy farms, striking to further turn the current high standard advanced dairy farms into the world-class most beautiful dairy farms where the best living welfare is provided to the organic dairy cows in the desert, turning them into "happy cows and healthy cows".

Continue to Enhance the Processing Ability of Self-Owned Brand Liquid Milk and New Plant Will Commence Trial Production in the Second Quarter of in 2017

In order to enhance the Group's ability to produce liquid milk and meet the increasing market demand, the new production plant and production lines of liquid milk built by the Group during the year will commence trial production in the second quarter of in 2017. Three production lines of liquid milk are currently under construction and are expected to produce 320 tonnes of milk per day when completed.

Continue to Implement Industrial Technology Innovation and Develop New Grass-to-Glass Organic Liquid Milk Products under Its Self-Owned Brand

In 2017, the Group will adhere to the principle of "innovation leads to success" and implement industrial technology innovation to develop new organic liquid milk products. Based on the continuous increase in the promotion of Shengmu yogurt machine, the Group successfully launched its new desert-based grass-to-glass organic product "Shengmu Naijue" (聖牧奶爵) in early 2017. This product selects premium milk resources from Shengmu desert-based top-level organic dairy cows, and the milk resources contain natural DHA, pure and rare. "Shengmu Naijue" contains premium protein of 3.7 g/100ml and native calcium of 120 mg/100ml, approximately 30% higher than regular milk, and it contains DHA beneficial to human bodies, i.e. Omega-3. This product is produced with adoption of lactose hydrolysis technique to refine nutrition and therefore dispenses with the problem of lactose intolerance so as to be better absorbed and be suitable for more, and a wider range of people.

Continue to Proceed Marketing Channel Development and Innovation Development to Enhance Awareness of Brand

In 2017, the Group will continue to expand its "blue ocean" strategy development channel of large chain- community stores and to open 20,000 large chain-community stores on top of over the 100,000 existing large chain-community stores while consolidating and enhancing the sales volume per large chain-community store. In 2017, the Group will expand the scope of promotion and installation activities of China Shengmu yogurt machines across special channels such as hospitals, schools, and restaurants and canteens nationwide and expects to install 20,000 - 30,000 machines in the first half of 2017, the achievement of which will lead to a bigger and more effective brand effect and economic benefits for China Shengmu.

In 2017, the Group will enhance and improve its "key account (KA)" distribution channels and standardized image of large chain-community stores through integration of the VI system, and innovate its marketing channel development by taking measures such as encouraging the navy, land and air forces and cooperating with veterans so as to promote the organic, green and loving brand image of China Shengmu.

In 2017, the Group intends to invite many news media groups to host a variety of new product launches and organic promotion activities to make headlines. Meanwhile, the Group intends to plan to record its desert-based grass-to-glass organic production model details in more detail and more comprehensively in the form of a VCR documentary so as to more intuitively and conveniently present before the consumers a clean desert, a beautiful grassland, dairy farms and modern processing facilities, namely, our grass-to-glass integrated organic industrial chain covering planting, farming and processing, thereby sufficiently indicating the advantage of the grass-to- glass organic green industry of Shengmu.

REPORT OF THE DIRECTORS

The Board has the pleasure in submitting its annual report together with the audited consolidated financial statements of the Group for the year ended December 31, 2016. Save as stated otherwise in this report, the defined terms herein shall have the same meaning as in the prospectus (“the **Prospectus**”) dated June 30, 2014.

PRINCIPAL BUSINESSES

The Group’s principal businesses consist of the dairy farming business and the liquid milk business. For details of the principal subsidiaries of the Group, please refer to Note 1 to the financial statements.

The Group’s income is mainly derived from its business activities in the PRC. For operating segment information of the Group for the year ended December 31, 2016, please refer to Note 4 to the financial statements.

RESULTS

The Group’s consolidated results for the year ended December 31, 2016 are set out in the consolidated statement of profit or loss and other comprehensive income in the financial statements.

FIVE-YEAR FINANCIAL HIGHLIGHTS

A summary of the results, assets and liabilities of the Group for the last five financial years is set out in the section headed “Financial Summary” in this annual report.

PROPERTY, PLANT AND EQUIPMENT

For details of the changes in the properties, plant and equipment of the Group during the year, please refer to Note 14 to the financial statements.

DIVIDEND DISTRIBUTION

The Board does not recommend the payment of final dividend for the year ended December 31, 2016 (2015: Nil).

DISTRIBUTABLE RESERVES

The Company’s distributable reserves amounted to RMB3,014.5 million as at December 31, 2016. For details of the changes in the Company’s reserves in 2016, please refer to Note 41 to the financial statements.

SHARE CAPITAL

For details of the changes in the Company’s share capital in 2016, please refer to the consolidated statement of changes in equity in the financial statements and Note 31 to the financial statements.

EVENTS AFTER THE REPORTING PERIOD

There were no significant subsequent events for disclosure since the end of reporting period of the Group and up to the latest practicable date prior to the issue of this annual report.

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

For the year ended December 31, 2016, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's shares.

ANNUAL GENERAL MEETING AND CLOSURE OF REGISTER OF MEMBERS

The forthcoming annual general meeting of the Company will be held on June 28, 2017. For determining the entitlement to attend and vote at the annual general meeting, the register of members of the Company will be closed from June 23, 2017 to June 28, 2017, both days inclusive. In order to be eligible to attend and vote at the above meeting, unregistered holders of shares of the Company should ensure that all share transfer documents accompanied by the relevant share certificates must be lodged with the Company's branch share registrar in Hong Kong, Tricor Investor Services Limited, at Level 22, Hopewell Centre, 183 Queen's Road East, Hong Kong not later than 4:30 p.m. on June 22, 2017.

The notice of annual general meeting and related circular will be despatched to the shareholders in due course.

PRE-EMPTIVE RIGHTS

Neither the Articles of Association of the Company nor the laws of the Cayman Islands, where the Company is incorporated, contains any provisions relating to pre-emptive rights.

MAJOR CUSTOMERS AND SUPPLIERS

In 2016, the five largest customers of the Group in aggregate accounted for 49.5% of the Group's total revenue and the largest customer accounted for 23.4% of the Group's total income. In 2016, the five largest suppliers of the Group accounted for 37.5% of the Group's total amount of purchases and the largest supplier accounted for 17.7% of the Group's total amount of purchases.

In 2016, to the knowledge of the Directors, except for Shengmu Forage, an associate of the Company, none of any of shareholders or any of Directors or any of their close associates who owns more than 5% of the Company's issued share capital, had any interest in the five largest suppliers or customers of the Group.

In 2016, we did not experience any material disputes with our customers or suppliers.

DIRECTORS

For the year ended December 31, 2016, the Company's Directors were as follows:

Executive Directors

Mr. YAO Tongshan (Chairman and chief executive officer) (appointed on February 14, 2014)
Mr. WU Jianye (President) (appointed on March 26, 2014)
Ms. GAO Lingfeng (Vice President) (appointed on March 26, 2014)
Mr. CUI Ruicheng (Vice President) (appointed on March 26, 2014)

Non-executive Directors

Mr. FAN Xiang(appointed on March 26, 2014)
Mr. CUI Guiyong (appointed on March 26, 2014)
Mr. SUN Qian (appointed on March 26, 2014)
Mr. DONG Xianli (appointed on February 19, 2016)
Mr. SHAO Genhuo (appointed on September 26, 2016)
Mr. ZHANG Jiawang (appointed on September 26, 2016)
The former non-executive Director, Mr. WU Jingshui, resigned with effect from Feburary 19, 2016.

Independent Non-executive Directors

Mr. WONG Kun Kau (appointed on June 18, 2014)
Mr. LI Changqing (appointed on June 18, 2014)
Ms. GE Xiaoping (appointed on June 18, 2014)
Mr. YUAN Qing (appointed on June 18, 2014)
Mr. FU Wenge (appointed on September 26, 2016)

BIOGRAPHICAL DETAILS OF DIRECTORS AND MEMBERS OF OUR SENIOR MANAGEMENT

Biographical details of Directors and members of our senior management are set out in the section headed "Directors and Senior Management" in this annual report.

DIRECTORS' SERVICE CONTRACTS

Each of the Directors has entered into a service contract or an appointment letter with the Company for a term of three years starting from the respective appointment date and shall retire and retire by rotation at the general meeting according to the requirements of the Articles of Association of the Company. The Board may appoint any person as a Director from time to time and at any time either to fill a casual vacancy or as an addition to the Board. Any Director so appointed shall hold office only until the next general meeting of the Company and shall then be eligible for re-election. None of our Directors has entered into any service contract or appointment letter which cannot be terminated within one year without payment of compensation (other than statutory compensation) with the Company or any of its subsidiaries.

CHANGES TO INFORMATION IN RESPECT OF DIRECTORS

Mr. CUI Guiyong, a non-executive Director of the Company, has been appointed as a non-executive director of COFCO Meat Holdings Limited, a company listed on the Stock Exchange (stock code: 1610), since May 23, 2016. Mr. SUN Qian, a non-executive Director of the Company, has ceased to act as a non-executive director of Dongpeng Holdings Company Limited (東鵬控股股份有限公司), a company listed on the Stock Exchange (stock code: 3386) (delisted from the Stock Exchange at 4:00 p.m. on June 22, 2016), since June 23, 2016. Mr. WONG Kun Kau, an independent non-executive Director of the Company, has ceased to act as an independent non-executive director of Anhui Conch Cement Company Limited (安徽海螺水泥股份有限公司), a company listed on the Stock Exchange (stock code: 914), since June 2, 2016. Mr. YUAN Qing,an independent non-executive Director of the Company, has ceased to act as an independent director of Inner Mongolia M-Grass Ecology and Environment (Group) Co., Ltd. (內蒙古蒙草生態環境(集團)股份有限公司), a company listed on the Shenzhen Stock Exchange (stock code: 300355), since October 14, 2016. Mr. DONG Xianli, a non-executive Director of the Company, has been appointed as the chief financial officer of China Modern Dairy Holdings Ltd. (中國現代牧業控股有限公司) ("**Modern Dairy**"), a company listed on the Stock Exchange (stock code: 1117), since December 1, 2016. Save as disclosed herein, as at December 31, 2016, there was no change to the information required to be disclosed by the Directors pursuant to paragraphs (a) to (e) and (g) of Rule 13.51(2) of the Listing Rules where applicable.

DIRECTORS' INTERESTS IN COMPETING BUSINESS

Mr. WU Jingshui, a non-executive Director of the Company from March 26, 2014 to February 19, 2016, held the following positions in the following companies whose businesses are or may be, directly or indirectly, in competition with our business: (i) vice president of Inner Mongolia Mengniu Dairy Group Limited (內蒙古蒙牛乳業 (集團) 股份有限公司) ("**Inner Mongolia Mengniu**"), a subsidiary of China Mengniu Dairy Company Limited (中國蒙牛乳業有限公司) ("**China Mengniu**"), a company listed on the Stock Exchange (stock code: 2319); (ii) from July 24, 2013 to January 29, 2016, a non-executive director of Yashili International Holdings Limited (雅士利國際控股有限公司) ("**Yashili**"), a company listed on the Stock Exchange (stock code: 1230) and a non-wholly-owned subsidiary of China Mengniu; and (iii) from June 26, 2014 to March 22, 2016, a non-executive director in Modern Dairy.

On December 1, 2016, Mr. DONG Xianli, a non-executive Director of the Company, was appointed as the chief financial officer of Modern Dairy.

For further information on the businesses of China Mengniu and Yashili and the potential competition between those businesses with the businesses of the Group, please refer to the section headed "Relationship with Controlling Shareholders – Directors' Interests in Competing Business" in the Prospectus.

Modern Dairy is primarily engaged in (i) dairy farming business, under which it mainly produces and sells raw milk to customers; and (ii) liquid milk products business under its own brands. As the Board is independent of the board of directors of Modern Dairy, and businesses of the Group and businesses controlled by Modern Dairy are managed by independent entities under independent management and administration respectively, businesses of the Group and businesses controlled by Modern Dairy are independent of each other and are conducted separately in arm's length.

Save as disclosed above, all Directors have confirmed that for the year ended December 31, 2016 and as at the date of this report, they and their close associates have not engaged in or held any interest in any business which is or may be, directly or indirectly, in competition with our business.

INDEPENDENCE OF INDEPENDENT NON-EXECUTIVE DIRECTORS

Pursuant to the criteria sets out in Rule 3.13 of the Listing Rules, the Company considers that Mr. WONG Kun Kau, Ms. GE Xiaoping, Mr. LI Changqing, Mr. YUAN Qing and Mr. FU Wenge are independent parties and has received from them written confirmations on their independence.

NON-COMPETITION UNDERTAKING

The Company's Ultimate Controlling Shareholders (as defined in the Prospectus) and World Shining (together the "**Covenantors**") have entered into a deed of non-competition (the "**Non-competition Deed**") (as set out in the section headed "**Relationship with Controlling Shareholders**" in the Prospectus) in favor of us. Pursuant to the Non-competition Deed, the Covenantors have undertaken to us that they would not, and that their associates (except any member of our Group) would not, during the restricted period set out in the "Non-competition Deed", engage in or be interested in any business which is or may be in competition with our existing core business (the "**Restricted Business**") except for the business currently carried out by Xinjiang Shenghe Dairy Company Limited (新疆盛和乳業有限公司) ("**Non-competition Undertaking**"). All independent non-executive Directors of the Company have reviewed the matters relating to the implementation of the Non-competition Undertaking and consider that the Covenantors have complied with the terms of the Non-competition Undertaking for the year ended December 31, 2016.

For details on major retained businesses of the Ultimate Controlling Shareholders, please refer to the section headed "Relationship with Controlling Shareholders — Major Retained Businesses of Our Ultimate Controlling Shareholders" in the Prospectus.

During the period from June 4, 2015 to December 31, 2017, the Group provides financial assistance in the form of guarantees for external borrowing of Shengmu Forage, a connected person of the Company (as defined under the Listing Rules), the details of which are set out in the announcement of the Company dated June 4, 2015.

As disclosed in the section headed "Relationship with Controlling Shareholders – Our Ultimate Controlling Shareholders Acting In Concert" in the Prospectus, the Ultimate Controlling Shareholders had entered into an acting-in-concert arrangement (the "**acting-in-concert arrangement**") prior to the Listing, and as the Ultimate Controlling Shareholders, through World Shining (together, the "**Controlling Shareholders**"), were entitled to exercise more than 30% of the voting rights at general meeting of our Company as a group of shareholders, they were regarded as the controlling shareholders (as defined under the Listing Rules) of the Company. In September 2016, the acting-in-concert arrangement was terminated. For details on the termination of the acting-in-concert arrangement, please refer to the announcement of the Company dated September 23, 2016. For the avoidance of doubt, notwithstanding the termination of the acting-in-concert arrangement, the Non-competition Deed continued to be in effect for the year ended December 31, 2016.

MATERIAL ACQUISITION AND DISPOSAL OF SUBSIDIARIES AND ASSOCIATED COMPANIES

For the year ended December 31, 2016 and as at the date of this report, there was no material acquisition or disposal of subsidiaries or associated companies of the Company by the Group.

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY

So far as is known to any Director or chief executive of the Company, as at December 31, 2016, the interests or short positions of the Directors and chief executive of the Company in the Shares, underlying Shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) (the "**SFO**")) which were required to be immediately notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they were taken or deemed to have under such provisions of the SFO), or the interests or short positions which were required, pursuant to Section 352 of the SFO, to be entered in the register referred to therein, or the interests or short positions which were required, pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers as set out in Appendix 10 to the Listing Rules (the "**Model Code**"), to be immediately notified to the Company and the Stock Exchange, were as follows:

(i) Long position in the Shares or underlying Shares

Name	Capacity/Nature of interest	Number of Shares/ underlying Shares	Percentage of interest
YAO Tongshan	Beneficial Owner	412,421,900(1)	6.49%
WU Jianye	Beneficial Owner	206,066,900(2)	3.24%
GAO Lingfeng	Beneficial Owner	161,277,680(3)	2.54%
CUI Ruicheng	Beneficial Owner	85,493,500(4)	1.35%
Shao Genhuo	Interest of a controlled corporation(5)	1,301,651,000	20.48%

(1) Among the 412,421,900 Shares held by Mr. YAO Tongshan (姚同山), 70,419,200 Shares are interests in options granted pursuant to the Pre-IPO Share Option Scheme.

(2) Among the 206,066,900 Shares held by Mr. WU Jianye (武建鄴), 64,876,800 Shares are interests in options granted pursuant to the Pre-IPO Share Option Scheme.

(3) Among the 161,277,680 Shares held by Ms. GAO Lingfeng (高凌鳳), 31,992,000 Shares are interests in options granted pursuant to the Pre-IPO Share Option Scheme.

(4) Among the 85,493,500 Shares held by Mr. CUI Ruicheng (崔瑞成), 31,992,000 Shares are interests in options granted pursuant to the Pre-IPO Share Option Scheme.

(5) Mr. SHAO Genhuo (邵根夥) holds the entire equity interests of Beijing Zhi Nong Investment Co., Ltd. ("**Beijing Zhi Nong**"), which in turn holds the entire equity interests of Nong You. Therefore, Mr. Shao is deemed to be interested in the Shares held by Nong You.

(ii) Long position in the shares of associated corporation

Name	Name of associated corporation	Percentage of interest
YAO Tongshan (姚同山)	Bayannur Shengmu High-tech Ecological Forage Co., Ltd. (巴彥淖爾市聖牧高科生態草業有限公司)	1.45%
WU Jianye (武建鄴)	Bayannur Shengmu Pangu Farming Co., Ltd. (巴彥淖爾市聖牧盤古牧業有限責任公司) ("**Shengmu Pangu**")	45.00%
	Bayannur Shengmu High-tech Ecological Forage Co., Ltd. (巴彥淖爾市聖牧高科生態草業有限公司)	6.83%
GAO Lingfeng (高凌鳳)	Bayannur Shengmu High-tech Ecological Forage Co., Ltd. (巴彥淖爾市聖牧高科生態草業有限公司)	14.52%

Save as disclosed above and to the best knowledge of the Directors, as at December 31, 2016, none of the Directors or chief executive of the Company had any interest or short position in the shares or underlying shares or debentures of the Company or any of its associated corporations which were required to be immediately notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they were taken or deemed to have under such provisions of the SFO) or which were required, pursuant to Section 352 of the SFO, to be entered in the register referred to therein, or which were required to be notified to the Company and the Stock Exchange pursuant to the Model Code.

INTERESTS OF THE SUBSTANTIAL SHAREHOLDERS

So far as is known to any Director or chief executive of the Company, as at December 31, 2016, the following persons (other than the Directors and the chief executive of the Company) had an interest or short position in the Shares or the underlying Shares as recorded in the register required to be kept by the Company pursuant to Section 336 of the SFO or which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO, or were, directly or indirectly, interested or deemed to be interested in 5% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any member of the Group:

Name	Capacity/Nature of interest	Number of Shares/ underlying Shares	Percentage of interest
Greenbelt Global Limited	Beneficial Owner	395,235,200(L)	6.22%(L)
		395,235,200(S)	6.22%(S)
Baring Private Equity Asia GP V Limited	Interest of a controlled corporation	395,235,200(L)	6.22%(L)
		395,235,200(S)	6.22%(S)
Baring Private Equity Asia GP V LP	Interest of a controlled corporation	395,235,200(L)	6.22%(L)
		395,235,200(S)	6.22%(S)
The Baring Asia Private Equity Fund V LP	Interest of a controlled corporation	395,235,200(L)	6.22%(L)
		395,235,200(S)	6.22%(S)
Salata Jean	Interest of a controlled corporation	395,235,200(L)	6.22%(L)
		395,235,200(S)	6.22%(S)
Sequoia Capital 2010 CGF Holdco, Ltd.	Beneficial Owner	378,320,000(L)	5.95%(L)
		378,320,000(S)	5.95%(S)
SC China Growth 2010 Management, L.P.	Interest of a controlled corporation	378,320,000(L)	5.95%(L)
		378,320,000(S)	5.95%(S)
SC China Holding Limited	Interest of a controlled corporation	378,320,000(L)	5.95%(L)
		378,320,000(S)	5.95%(S)
Sequoia Capital China Advisors Limited	Interest of a controlled corporation	378,320,000(L)	5.95%(L)
		378,320,000(S)	5.95%(S)
Sequoia Capital China Growth 2010, L.P.	Interest of a controlled corporation	378,320,000(L)	5.95%(L)
		378,320,000(S)	5.95%(S)
SNP China Enterprises Limited	Interest of a controlled corporation	378,320,000(L)	5.95%(L)
		378,320,000(S)	5.95%(S)
SHEN Nanpeng (沈南鵬)	Interest of a controlled corporation	378,320,000(L)	5.95%(L)
		378,320,000(S)	5.95%(S)
The Goldman Sachs Group, Inc.	Beneficial Owner	407,008,300(L)	6.41%(L)
		406,264,300(S)	6.39%(S)
Nong You Co., Ltd.	Beneficial Owner	1,301,651,000	20.48%
Beijing Zhi Nong Investment Co., Ltd.	Interest of a controlled corporation	1,301,651,000	20.48%
Shao Genhuo	Interest of a controlled corporation	1,301,651,000	20.48%
Inner Mongolia Yili Industrial Group Co., Ltd.	Interest of a controlled corporation	2,351,128,000	37.00%

INTERESTS OF THE SUBSTANTIAL SHAREHOLDERS OF ANY MEMBER OF THE GROUP (OTHER THAN THE COMPANY)

Name	Name of member company	Percentage of interest
Inner Mongolia University Aodu Assets Management Limited (內蒙古大學奧都資產經營有限責任公司)	Inner Mongolia IMU-Shengmu High-tech Dairy Co., Ltd. (內蒙古內大聖牧高科牧業有限公司)	30.00%
CHEN Qingjun (陳慶軍)	Bayannur Shengmu Hateng Farming Co., Ltd. (巴彥淖爾市聖牧哈騰牧業有限公司)	35.00%
LI Yongqiang (李永強)	Bayannur Shengmu Taohai Farming Co., Ltd. (巴彥淖爾市聖牧套海牧業有限公司)	45.00%
DING Gaohuai (丁高懷)	Bayannur Shengmu Liuhe Farming Co., Ltd. (巴彥淖爾市聖牧六和牧業有限公司)	35.00%
WANG Qiang (王強)	Alxa Shengmu Wuxing Farming Co., Ltd. (阿拉善盟聖牧五星牧業有限公司)	35.00%
LI Ruijun (李瑞軍)	Bayannur Shengmu Qixing Farming Co., Ltd. (巴彥淖爾市聖牧七星牧業有限公司)	35.00%
YUAN Lun (院輪)	Bayannur Shengmu Beidou Farming Co., Ltd. (巴彥淖爾市聖牧北斗牧業有限公司)	35.00%
WANG Lixin (汪立新)	Bayannur Shengmu Xinhe Farming Co., Ltd. (巴彥淖爾市聖牧新禾牧業有限公司)	35.00%
CHANG Zhiba (常志拔)	Bayannur Shengmu Zhenghe Farming Co., Ltd. (巴彥淖爾市聖牧正和牧業有限公司)	15.48%
HOU Liubin (侯留斌)	Bayannur Shengmu Weiye Farming Co., Ltd. (巴彥淖爾市聖牧偉業牧業有限公司)	35.00%
GUO Yongfeng (郭永豐)	Alxa Shengmu Zhaofeng Farming Co., Ltd. (阿拉善盟聖牧兆豐牧業有限公司)	35.00%
REN Junming (任俊明)	Bayannur Shengmu Sanli Farming Co., Ltd. (巴彥淖爾市聖牧三利牧業有限公司)	35.00%
YU Gong (于工)	Bayannur Shengmu Shajin Farming Co., Ltd. (巴彥淖爾市聖牧沙金牧業有限公司)	35.00%

Save as set out above, our Directors are not aware of any person (not being a Director or chief executive of our Company) who, as at December 31, 2016, was interested, directly or indirectly, in 10% or more of the nominal amount of any class of share capital carrying rights to vote in all circumstances at general meetings of any member of our Group (other than our Company) or any options in respect of such capital.

PRE-IPO SHARE OPTION SCHEME AND SHARE OPTION SCHEME

Pre-IPO Share Option Scheme

The Company has approved and adopted the Pre-IPO Share Option Scheme pursuant to the resolutions of the Shareholders passed on April 30, 2014. The purpose of the Pre-IPO Share Option Scheme is to attract, retain and motivate the Directors, as well as the senior management of the Group and Shengmu Forage, to provide a means of compensation through the grant of options under the Pre-IPO Share Option Scheme for their contribution to the growth and profits of the Group, and to allow them to participate in the future growth and profitability of the Group. Participants of the Pre-IPO Share Option Scheme include (a) the executive Directors, (b) senior management of the Group, (c) management of the subsidiaries of the Company, and (d) management of Shengmu Forage.

The Pre-IPO Share Option Scheme provides that, within two (2) years (being the period from May 4, 2015 to May 4, 2017) after the Vesting Date, a grantee shall not sell, offer to sell, contract or agree to sell, mortgage, charge, pledge, hypothecate, lend, grant or sell any option, warrants, contract or right to purchase, grant or purchase any option, warrant, contract or right to sell, or otherwise transfer or dispose of or create an encumbrance over, or agree to transfer or dispose of or create an encumbrance over (either directly or indirectly, conditionally or unconditionally) any Shares which have been issued to him/her pursuant to his/her exercise of any option granted to and vested on him/her under the Pre-IPO Share Option Scheme.

According to the Pre-IPO Share Option Scheme, options granted (and vested on the Vesting Date) must be exercised by the relevant grantee within six (6) months after the Vesting Date. Options not exercised within such six (6) months shall lapse immediately afterwards. Save for the options which have been granted before the Listing Date, no further options will be granted under the Pre-IPO Share Option Scheme on or after the Listing Date.

As the options to subscribe for 488,484,000 Shares were fully vested to 181 grantees on the Vesting Date (i.e. May 4, 2015), they will lapse if not being exercised on or before November 4, 2015.

Pursuant to a resolution approved by the Shareholders at the extraordinary general meeting on November 3, 2015, the Pre-IPO Share Option Scheme was amended as follows:

(1) All the Shares issued pursuant to the exercise of options during the Amended Exercise Period (as defined hereunder) would not be subject to any restriction applicable during the Lock-up Period (being the period from May 4, 2015 to May 4, 2017) provided under the Pre-IPO Share Option Scheme. Grantees are entitled to sell or otherwise dispose of any interest in the Shares after they exercise the options during the Amended Exercise Period (as defined hereunder).

(2) The exercise period provided under the Pre-IPO Share Option Scheme (from May 4, 2015 to November 4, 2015) was varied to the ("**Amended Exercise Period**") in the following manner:

Amended Exercise Period	Maximum percentage of options exercisable during the respective Amended Exercise Period
From May 4, 2016 to May 4, 2017	50% of the options vested
From November 4, 2016 to May 4, 2017	50% of the options vested

If the grantee ceases employment with the Group or Shengmu Forage before May 4, 2016, 100% of the options held by him/her shall lapse immediately, and if the grantee ceases employment with the Group or Shengmu Forage on or after May 4, 2016 but before November 4, 2016, 50% of the options held by him/her shall lapse immediately.

Apart from the above amendments, the other terms of the Pre-IPO Share Option Scheme remain the same. The Pre-IPO Share Option Scheme was conditionally approved and adopted pursuant to shareholders' resolutions passed on April 30, 2014. On the same date, all options under the Pre-IPO Share Option Scheme were granted to the respective grantees. The Pre-IPO Share Option Scheme will remain in force for a period of four years commencing on the date on which an option is granted pursuant to the scheme, and will accordingly expire on April 30, 2018.

The table below sets out the particulars of changes of options granted under the Pre-IPO Share Option Scheme from January 1, 2016 to December 31, 2016:

	Number of options [1]						
Name or category of participant	As at January 1, 2016	Exercised during the period	Lapsed/ Cancelled during the period	As at December 31, 2016	Date of grant of options	Exercise period of options (both dates inclusive)	Exercise price of options (HK$)
Directors of the Company							
YAO Tongshan	70,419,200	Nil	Nil	70,419,200	April 30, 2014	(1) May 4, 2016–May 4, 2017: 50%; (2) November 4, 2016 – May 4, 2017: 50% [2]	HK$1.56
WU Jianye	64,876,800	Nil	Nil	64,876,800	April 30, 2014	(1) May 4, 2016–May 4, 2017: 50%; (2) November 4, 2016 – May 4, 2017: 50% [2]	HK$1.56
GAO Lingfeng	31,992,000	Nil	Nil	31,992,000	April 30, 2014	(1) May 4, 2016–May 4, 2017: 50%; (2) November 4, 2016 – May 4, 2017: 50% [2]	HK$1.56
CUI Ruicheng	31,992,000	Nil	Nil	31,992,000	April 30, 2014	(1) May 4, 2016–May 4, 2017: 50%; (2) November 4, 2016 – May 4, 2017: 50% [2]	HK$1.56
Directors of subsidiaries of the Company not mentioned above	122,868,600	Nil	11,160,000 [3]	111,708,600	April 30, 2014	(1) May 4, 2016–May 4, 2017: 50%; (2) November 4, 2016 – May 4, 2017: 50% [2]	HK$1.56
Other grantees who are employees of the Group	123,481,000	Nil	29,502,600 [3]	93,978,400	April 30, 2014	(1) May 4, 2016–May 4, 2017: 50%; (2) November 4, 2016 – May 4, 2017: 50% [2]	HK$1.56
Other 6 grantees who are employees of Shengmu Forage	3,868,800	Nil	Nil	3,868,800	April 30, 2014	(1) May 4, 2016–May 4, 2017: 50%; (2) November 4, 2016 – May 4, 2017: 50% [2]	HK$1.56
Total:	449,498,400 options eligible to subscribe for 449,498,400 shares of the Company	Nil	Total of 40,662,600 options (with rights to subscribe for 40,662,600 shares of the Company) have lapsed [3]	408,835,800 options eligible to subscribe for 408,835,800 shares of the Company			

Note:

(1) Prior to the Listing Date, options to subscribe for an aggregate of 504,480,000 Shares have been conditionally granted to a total of 189 grantees under the Pre-IPO Share Option Scheme by the Company. As of the date of this report, there were 45 grantees who have left employment with the Group and 95,644,200 options they held to subscribe for 95,644,200 Shares had lapsed. As at the date of this report, a total of 144 grantees held a total of 408,835,800 options granted under the Pre-IPO Share Option Scheme to subscribe for 408,835,800 shares representing (i) approximately 6.43% of the Company's issued share capital as at the date of this report (excluding all Shares which may be allotted and issued upon the exercise of any options granted under the Pre-IPO Share Option Scheme or to be granted under the Share Option Scheme); and (ii) approximately 6.04% of the Company's issued share capital as of the date of this report, (assuming that all options currently in force which have been granted and vested under the Pre-IPO Share Option Scheme are exercised, but without taking into account any Shares which may be allotted and issued upon the exercise of any options which may be granted under the Share Option Scheme). Save for the options which have been granted before the Listing Date, no further options will be granted under the Pre-IPO Share Option Scheme on or after the Listing Date. The subscription price per share of each option granted under the Pre-IPO Share Option Scheme is HK$1.56.

(2) The Board of the Company has passed board resolutions confirming that the vesting conditions have been satisfied, hence 488,484,000 options out of all subsisting options granted under the Pre-IPO Share Option Scheme were fully vested to relevant grantees on May 4, 2015 (being the first business day after the expiration of Waiting Period on April 30, 2015), exercisable from April 30, 2015 to November 4, 2015. According to an ordinary resolution approved by the Shareholders at the extraordinary general meeting on November 3, 2015, the exercise period of options under the Pre-IPO Share Option Scheme was amend as follows: grantees are entitled to exercise 50% of their vested options from May 4, 2016 to May 4, 2017 and 50% from November 4, 2016 to May 4, 2017 respectively. All the Shares issued pursuant to the exercise of options during the exercise period would not be subject to any restriction currently applicable during the Lock-up Period. Grantees are entitled to sell or otherwise dispose of any interest in the Shares after they exercise the options during the exercise period.

(3) A total of 40,662,600 options to subscribe for a total of 40,662,600 Shares had lapsed as certain grantees ceased to be employees of the Group.

A detailed summary of the terms (including the terms of the scheme and conditions) of the Pre-IPO Share Option Scheme and list of grantees has been set out in the section headed "Appendix IV – Statutory and General Information – D. Pre-IPO Share Option Scheme" in the Prospectus and the announcement of the Company dated October 2, 2015. Details of the impact of options granted under the Pre-IPO Share Option Scheme on the financial statements are set out in Note 34 to the consolidated financial statements.

Share Option Scheme

On June 18, 2014, the Company adopted the Share Option Scheme which is subject to the provisions under Chapter 17 of the Listing Rules. The purpose of the Share Option Scheme is to attract, retain and motivate employees, Directors and other participants, and to provide a means of compensation through the grant of options for their contribution to the growth and profits of the Group, and to allow them to participate in the future growth and profitability of the Group. The participants of the Share Option Scheme are any executive, non-executive or independent non-executive Directors or any employees (whether full-time or part-time) of our Company, or any of its subsidiaries or associated companies or any other person whom the Board considers, in its sole discretion, has contributed or will contribute to our Group. The basis of eligibility of any of the class of the participants to the grant of any options under the Share Option Scheme shall be determined by the Board from time to time on the basis of their contribution to the development and growth of our Group and any invested entity.

The Shares which may be issued upon exercise of all options to be granted under the Share Option Scheme and other share option schemes of the Company (and to which the provisions of the Listing Rules are applicable) shall not exceed 10% of the aggregate of the Shares of the Company in issue on the Listing Date, being a total of 635,440,000 Shares, which also represents 10% of the issued share capital of the Company as at the date of this annual report.

The total number of Shares issued and to be issued upon exercise of the options granted to each eligible participant under the Share Option Scheme (including exercised, cancelled and outstanding options) in any 12-month period shall not exceed 1% of the Shares in issue. Any further grant of options to an eligible participant under the Share Option Scheme which would result in the Shares issued and to be issued upon exercise of all options granted and to be granted to such participant (including exercised, cancelled and outstanding options) in the 12-month period up to and including the date of such further grant exceeding the abovesaid limit shall be subject to our Shareholders' approval in general meeting with such participant and his associates (as defined under the Listing Rules) abstaining from voting.

The amount of HK$1.00 is payable as consideration for each grant of options under the Share Option Scheme, upon acceptance of such grant. The subscription price in respect of Shares upon exercise of options under the Share Option Scheme shall be such price as determined by the Board in its absolute discretion at the time of the grant of the relevant option (and shall be stated in the letter containing the offer of the grant of the option), but in any case the subscription price shall not be less than the higher of (a) the closing price of the Shares as stated in the daily quotation sheet of the Stock Exchange on the date of grant, which must be a business day, (b) the average closing price of the Shares as stated in the daily quotation sheets of the Stock Exchange for the five (5) business days immediately preceding the date of grant, and (c) the nominal value of a Share.

An option granted under the Share Option Scheme may be exercised in accordance with the terms of the Share Option Scheme at any time during the period to be determined by our Board at its absolute discretion and notified by our Board to each grantee as being the period during which an option may be exercised and in any event, such period shall not be longer than 10 years from the date upon which any particular option is granted in accordance with the Share Option Scheme.

No option has been granted under the Share Option Scheme since the adoption date of the Share Option Scheme and up to the latest practicable date prior to the publication of this annual report. A summary of the terms of the Share Option Scheme has been set out in the section headed "Appendix IV – Statutory and General Information – E. Share Option Scheme" in the Prospectus.

The Share Option Scheme was approved by shareholders' resolutions of the Company passed on June 18, 2014, and will remain in force for a period of 10 years following such date.

USE OF NET PROCEEDS FROM THE GLOBAL OFFERING

The net proceeds from the Global Offering of the Company were approximately RMB801.2 million. The relevant net proceeds are intended to be or have been used in accordance with the proposed usages as set out in the section headed "Future Plans and Use of Proceeds" in the Prospectus of the Company dated June 30, 2014.

As at December 31, 2016, the net proceeds were applied as follows:

	Funds utilized as at December 31, 2016 RMB'000
Constructing six additional organic dairy farms	182,525
Acquiring dairy cows domestically and from overseas	145,644
Sales and marketing activities and expansion of distribution network	40,102
Expanding the Group's liquid milk production capacity	120,306
Repayment of loans	120,306
Additional working capital and general corporate purposes	80,204
Total:	689,087

CONTRACT OF SIGNIFICANCE WITH DIRECTORS AND CONTROLLING SHAREHOLDERS

Save as the related party disclosures set out in Note 37 to the financial statements and as disclosed in the section headed "Connected Persons and Continuing Connected Transactions" below, no contract of significance in relation to the Group's business to which the Company or any of its subsidiaries was a party and in which a Director of the Company or a controlling shareholder of the Company had a material interest, whether directly or indirectly, subsisted for the year ended December 31, 2016.

CONNECTED PERSONS AND CONTINUING CONNECTED TRANSACTIONS

Connected Persons

*Shengmu Forage and Alxa Forage ("**Shengmu Forage**")*

During the period from January 1, 2016 up to September 23, 2016, some of the former ultimate controlling shareholders and their family members (namely Mr. Yao Tongshan, Ms. Gao Lingfeng, Mr. Wu Jianye, Mr. Wang Fuzhu, Ms. Shi Jianhong, Ms. Yang Yaping, Mr. Wang Zhenxi and Ms. Qin Yuan) held more than 30% equity interest in Shengmu Forage. Accordingly, Shengmu Forage was a connected person (as defined under the Listing Rules) of the Company during such period of time, and since Alxa Forage is a wholly-owned subsidiary of Shengmu Forage, therefore, it was also a connected person (as defined under the Listing Rules) of the Company during such period of time. On September 23, 2016, the former ultimate controlling shareholders of the Company (namely, Mr. Yao Tongshan, Mr. Wang Fuzhu, Ms. Shi Jianhong, Mr. Wang Zhenxi, Ms. Yang Yaping, Ms. Yang Yali, Mr. Lu Shunyi, Ms. Guo Yunfeng, Mr. Yun Jindong, Ms. Gao Lingfeng, Mr. Zhang Junke, Mr. Wang Zhen, Mr. Cui Ruicheng and Mr. Wu Jianye) entered into a written termination agreement to terminate the acting-in-concert relationship among them. Thereafter, Shengmu Forage has ceased to be an associate of any connected person under the Listing Rules and hence was no longer a connected person of the Company. Besides, Alxa Forage, a company wholly owned by Shengmu Forage, has also ceased to be a connected person of the Company accordingly.

Shengmu Xiwang

During the period from January 1, 2016 up to March 2, 2016, Shengmu Xiwang was a 65% owned subsidiary of the Group and was held as to 17.5% by Mr. Wang zhen, one of the former ultimate controlling shareholders. Accordingly, Shengmu Xiwang was a connected person (as defined under the Listing Rules) of the Company during such period of time. On March 2, 2016, Mr. Wangzhen, one of the former ultimate controlling shareholders of the Company (i.e. a former connected person of the Company), ceased to hold any share of Shengmu Xiwang. As a result, Shengmu Xiwang has then ceased to be a connected person of the Company.

Continuing Connected Transactions

The Company's continuing connected transactions during the year of 2016 are as follows:

1. On June 25, 2014, Shengmu Forage and Inner Mongolia Shengmu High-tech Farming Co., Ltd. (內蒙古聖牧高科牧業有限公司) ("**Shengmu Holding**") entered into a framework agreement in relation to the purchase of forage by the Group from Shengmu Forage and its subsidiaries (including Alxa Shengmu High-tech Ecological Forage Co., Ltd. (阿拉善盟聖牧高科生態草業有限公司) ("**Alxa Forage**") ("**Forage Supply Framework Agreement**"), details of which are set out in the section headed "Continuing Connected Transactions" in the Prospectus. Pursuant to the agreement, Shengmu Forage and its subsidiaries (including Alxa Forage) shall sell all the forage produced by it to us on an exclusive basis for a term from January 1, 2014 to December 31, 2016. The total annual amount of purchases made by the Group from Shengmu Forage and Alxa Forage under the Forage Supply Framework Agreement will not exceed RMB392.0 million, RMB630.0 million and RMB911.0 million for each of the years ended December 31, 2014, 2015 and 2016. During the period from January 1, 2016 to September 23, 2016, total purchase made by the Group from Shengmu Forage was RMB 187.9 million. Reasons for and benefits of

the transactions under the Forage Supply Framework Agreement are: Shengmu Forage and Alxa Forage grow organic forage without using any synthetic pesticides or synthetic fertilizers. All of the growing fields developed by Shengmu Forage and Alxa Forage meet the E.U. standards set by ECOCERT S.A. and are certified organic under the PRC standards by the COFCC. We believe these crops provide organic, nutritious feeds necessary for our dairy cows, allowing them to produce organic and nutritious milk. In addition, farms of Shengmu Forage and Alxa Forage in the Ulan Buh Desert are in the proximity of our organic dairy farms. As such, it is commercially beneficial to the Group to continue to purchase forage from Shengmu Forage and Alxa Forage in view of their stable and reliable supply of good quality forage and the proximity of its forage farms to our dairy farms. The term of the Forage Supply Framework Agreement expired on December 31, 2016.

2. On June 25, 2014, Shengmu Pangu, Shengmu Xiwang and Shengmu Holding entered into a framework agreement in relation to the purchase of organic raw milk by the Group (excluding Shengmu Pangu and Shengmu Xiwang) from Shengmu Pangu and Shengmu Xiwang ("**Milk Supply Framework Agreement**"), details of which are set out in the section headed "Continuing Connected Transactions" in the Prospectus. Pursuant to the agreement, organic raw milk of Shengmu Pangu and Shengmu Xiwang were subject to our centralized sales management. Both of them must sell their organic raw milk to us on a priority basis to meet our requirement. Excessive organic raw milk could be sold to third parties as permitted and managed by Shengmu Holding. The term of the agreement was from January 1, 2014 to December 31, 2016. The total annual amount of purchases made by the Group (excluding Shengmu Pangu and Shengmu Xiwang) from Shengmu Pangu and Shengmu Xiwang under the Milk Supply Framework Agreement could not exceed RMB160.0 million, RMB250.0 million and RMB400.0 million for each of the years ended December 31, 2014, 2015 and 2016. For the year ended December 31, 2016, total purchase of raw fresh milk made by the Group from Shengmu Pangu was RMB202.9 million. During the period from January 1, 2016 to March 2, 2016, total purchase of raw fresh milk made by the Group from Shengmu Xiwang was RMB7.5 million. Reasons for and benefits of the transactions under the Milk Supply Framework Agreement were: we manage our sales of raw milk under a centralized system and Shengmu Dairy serves as the processing center of raw milk for all our subsidiaries. As subsidiaries of the Group, Shengmu Pangu and Shengmu Xiwang are also subject to such centralized sales system. The term of the Milk Supply Framework Agreement expired on December 31, 2016.

3. On June 25, 2014, Shengmu Pangu, Shengmu Xiwang and Shengmu Holding entered into a framework agreement in relation to the purchase of cows by the Group (excluding Shengmu Pangu and Shengmu Xiwang) from Shengmu Pangu and Shengmu Xiwang ("**Framework Agreement for Sale and Purchase of Cows**"), details of which are set out in the section headed "Continuing Connected Transactions" in the Prospectus. The term of the agreement was from January 1, 2014 to December 31, 2016. Under the Framework Agreement for Sale and Purchase of Cows, (I) the total annual amount of purchases of cows made by the Group (excluding Shengmu Pangu and Shengmu Xiwang) from Shengmu Pangu and Shengmu Xiwang will not exceed RMB33.0 million, RMB62.0 million and RMB61.0 million, and (II) the total sales of cows made by the Group (excluding Shengmu Pangu and Shengmu Xiwang) to Shengmu Pangu and Shengmu Xiwang could not exceed RMB65.0 million, RMB55.0 million and RMB75.0 million, for each of the years ended December 31, 2014, 2015 and 2016. Under the Framework Agreement for Sale and Purchase of Cows above, for the year ended December 31, 2016, total purchase of cows made by the Group (excluding Shengmu Pangu) was RMB21.9 million and total revenue was RMB41.8 million. During the period from January 1, 2016 to March 2, 2016, the Group (excluding Shengmu Xiwang) didn't purchase from nor sell to Shengmu Xiwang any cow. Reasons for and benefits of the transactions under the Framework Agreement for Sale and Purchase of Cows were: we manage our dairy farming on a centralized basis. As subsidiaries of the Group, Shengmu Pangu and Shengmu Xiwang are also subject to such centralized management. The term of the Framework Agreement for Sale and Purchase of Cows expired on December 31, 2016.

4. On June 25, 2014, Shengmu Pangu, Shengmu Xiwang and Shengmu Holding entered into a framework agreement for a term from January 1, 2014 to December 31, 2016 in relation to the provision of financial assistance by the Group (excluding Shengmu Pangu and Shengmu Xiwang) to Shengmu Pangu and Shengmu Xiwang ("**Financial Assistance Framework Agreement**"), details of which are set out in the section headed "Continuing Connected Transactions" in the Prospectus. Pursuant to such agreement, the Group would provide financial assistances (in the form of guarantees) to Shengmu Pangu and Shengmu Xiwang on normal commercial terms. The term of the agreement was from January 1, 2014 to December 31, 2016. The maximum daily balance of financial assistance to be provided by the Group (excluding Shengmu Pangu and Shengmu Xiwang) to Shengmu Pangu and Shengmu Xiwang could not exceed RMB60.0 million, RMB100.0 million and RMB120.0 million for each of the years ended December 31, 2014, 2015 and 2016. For the year ended December 31, 2016, the maximum daily balance of financial assistance provided by the Group to Shengmu Pangu was RMB32.0 million. During the period from January 1, 2016 to March 2, 2016, the maximum daily balance of financial assistance provided by the Group to Shengmu Xiwang was RMB15.0 million. Reasons for and benefits of the transactions under the Financial Assistance Framework Agreement were: it would be difficult for our subsidiaries established for a short time, including Shengmu Pangu and Shengmu Xiwang, to obtain commercial loans and borrowings without guarantees of our other earlier established subsidiaries. Even if they could obtain such loans and borrowings on their own, they would incur higher finance costs on commercial loans and borrowings without guarantees given by our other earlier established subsidiaries. As such, it is commercially beneficial to the Group to continue to provide financial assistances to Shengmu Pangu and Shengmu Xiwang, which will also lower our overall finance costs. The term of the Financial Assistance Framework Agreement expired on December 31, 2016.

5. On June 4, 2015, the Company and Shengmu Forage entered into a financial assistance framework agreement, pursuant to which the Group will provide financial assistance (in the form of guarantees) for the external borrowings of Shengmu Forage. The maximum daily balance of financial assistance (in the form of guarantees) to be provided by the Group to Shengmu Forage may not exceed RMB300.0 million for each of the years ended December 31, 2015, 2016 and 2017. The maximum daily balance of financial assistance for the period ended September 23, 2016 was RMB300.0 million. Reasons for and benefits of the transactions under the financial assistance framework agreement are: provision of guarantees for the external borrowings of Shengmu Forage enables Shengmu Forage to implement its expansion plans, which is beneficial to the development of the Group. Besides, the risks arising from the provision of financial assistance are controllable.

6. On November 22, 2016, Shengmu Pangu and Shengmu Holding entered into a framework agreement in relation to the purchase of organic raw milk by the Group (excluding Shengmu Pangu) from Shengmu Pangu (the "**New Milk Supply Framework Agreement**"). As at the date of this agreement, Shengmu Pangu was a 55% indirectly owned subsidiary of the Company and the remaining 45% equity interest in Shengmu Pangu is owned by Mr. WU Jianye, an executive Director. As a result, Shengmu Pangu is a connected person of the Company as defined under the Listing Rules. Pursuant to the Agreement, the organic raw milk of Shengmu Pangu is subject to our centralised sales. Shengmu Pangu shall sell all of its organic raw milk to us on a priority basis to satisfy our demand. Excessive organic raw milk can be sold to third parties as permitted and managed by Shengmu Holding. The term of the Agreement is from January 1, 2017 to December 31, 2019. For each of the years ended December 31, 2017, 2018 and 2019, under the Milk Supply Framework Agreement, (I) the total annual amount of purchases made by the Group (excluding Shengmu Pangu) from Shengmu Pangu may not exceed RMB333.1 million, RMB421.5 million and RMB454.2 million, respectively. Reasons for and benefits of the transactions under the Milk Supply Framework Agreement are that we manage our sales of raw milk under a centralised system. As a subsidiary of the Group, Shengmu Pangu is also subject to such centralised sales system. Details of the New Milk Supply Framework Agreement are set out in the announcement of the Company dated November 22, 2016 with respect to continuing connected transactions of the Company.

7. On November 22, 2016, Shengmu Pangu and Shengmu Holding entered into a framework agreement in relation to the purchase of cows by the Group (excluding Shengmu Pangu) from Shengmu Pangu (the "**New Framework Agreement for Sale and Purchase of Cows**"). As at the date of this agreement, Shengmu Pangu was a 55% indirectly owned subsidiary of the Company and the remaining 45% equity interest in Shengmu Pangu is owned by Mr. WU Jianye, an executive Director. As a result, Shengmu Pangu is a connected person of the Company as defined under the Listing Rules. Pursuant to the New Framework Agreement for Sale and Purchase of Cows, the parties thereto will sell and purchase cows from the other, such that the calves and heifers of the parties will be raised on a centralised basis and separately from milkable cows. The term of the agreement is from January 1, 2017 to December 31, 2019. For each of the years ended December 31, 2017, 2018 and 2019, under the Framework Agreement for Sale and Purchase of Cows, (I) the total annual amount of purchases of cows made by the Group (excluding Shengmu Pangu) from Shengmu Pangu may not exceed RMB95.9 million, RMB 94.1 million and RMB16.0 million, respectively; and (II) the total revenue of sales of cows made by the Group (excluding Shengmu Pangu) to Shengmu Pangu may not exceed RMB94.3 million, RMB67.2 million and RMB34.5 million, respectively. Reasons and benefits of the transactions under the Framework Agreement for Sale and Purchase of Cows are that the Group manages the dairy farming business on a centralised basis. The majority of the calves and heifers are raised by Shengmu Farming, another subsidiary of the Company, separately from milkable cows on other farms. Shengmu Farming further sells pregnant heifers to the other farms of the Group to replenish their herds. As a subsidiary of the Group, Shengmu Pangu is also subject to such centralised management. Details of the New Framework Agreement for Sale and Purchase of Cows are set out in the announcement of the Company dated November 22, 2016 with respect to continuing connected transactions of the Company.

8. On November 22, 2016, Shengmu Holding and Shengmu Pangu entered into a framework agreement in relation to the provision of financial assistance (in the form of guarantees) by the Group (excluding Shengmu Pangu) for the commercial loans and borrowings of Shengmu Pangu on normal commercial terms, based on the requests of Shengmu Pangu from time to time (the "**New Financial Assistance Agreement**"). As at the date of this agreement, Shengmu Pangu was a 55% indirectly owned subsidiary of the Company and the remaining 45% equity interest in Shengmu Pangu is owned by Mr. WU Jianye, an executive Director. As a result, Shengmu Pangu is a connected person of the Company as defined under the Listing Rules. The term of the New Financial Assistance Agreement is from January 1, 2017 to December 31, 2019. Under the New Financial Assistance Agreement, the maximum daily balance of financial assistance to be provided by the Group (excluding Shengmu Pangu) to Shengmu Pangu may not exceed RMB60.0 million for each of the years ended December 31, 2017, 2018 and 2019 respectively. Reasons and benefits of the transactions under the New Financial Assistance Agreement are that Shengmu Pangu, as a relatively newly established subsidiary of the Group, has been obtaining commercial loans and borrowings with the guarantees provided by the other more established subsidiaries of the Group, such as Shengmu Holding and Shengmu Farming. Without such guarantees, it would incur higher finance costs to obtain such commercial loans and borrowings. As such, it is commercially beneficial to the Group to continue to provide financial assistances to Shengmu Pangu, which will also lower the overall finance costs of the Group. Details of the New Financial Assistance Agreement are set out in the announcement of the Company dated November 22, 2016 with respect to continuing connected transactions of the Company.

9. On November 22, 2016, Shengmu Holding and Inner Mongolia Sijichun Co. Ltd. (內蒙古四季春飼料有限公司) ("**Sijichun**") entered into a framework agreement in relation to purchase of feed by the Group from Sijichun (the "**Feed Supply Framework Agreement**"). As Sijichun is an indirectly wholly-owned subsidiary of Beijing Dabeinong Technology Group Co., Ltd. ("**Dabeinong Group**") in which, a non-executive Director of the Company, Mr. SHAO Genhuo holds more than 30% equity interest, the transactions under the Feed Supply Framework Agreement constitute continuing connected transactions of the Company. The term of the Feed Supply Framework Agreement is from January 1, 2017 to December 31, 2019. Under the Feed Supply Framework Agreement, the total annual purchase amount by the Group from Sijichun under the Feed Supply Framework Agreement shall not exceed RMB31.8 million, RMB30.4 million and RMB30.5 million for each of the years ended December 31, 2017, 2018 and 2019, respectively. Reasons and benefits of the transactions under the Feed Supply Framework Agreement are that Sijichun grows high quality feed and it is commercially beneficial to the Group to purchase feed from Sijichun in view of its stable and reliable supply of good quality feed. Details of the Feed Supply Framework Agreement are set out in the announcement of the Company dated November 22, 2016 with respect to continuing connected transactions of the Company.

The Directors (including the independent non-executive Directors) are of the view that the continuing connected transactions referred to above are entered into during the ordinary course of the Group's business on normal or better commercial terms and under agreements of such transactions, the terms of which are fair and reasonable and in the interests of the Shareholders of listed companies as a whole. The Company's auditor has confirmed that: (i) nothing has come to their attention that causes them to believe that the disclosed continuing connected transactions have not been approved by the Company's board of directors; (ii) nothing has come to their attention that causes them to believe that the transactions were not, in all material respects, in accordance with the pricing policies of the Group; (iii) nothing has come to their attention that causes them to believe that the transactions were not entered into, in all material respects, in accordance with the relevant agreements governing such transactions; and (iv) with respect to the aggregate amount of each of the continuing connected transactions set out above, nothing has come to their attention that causes them to believe that the disclosed continuing connected transactions have exceeded the maximum annual cap as set by the Company.

RELATED PARTY TRANSACTIONS

Details of the Group's related party transactions are set out in Note 37 to the financial statements. The related party transactions mainly comprise: (1) sale of products to certain entities which have been accounted for as associates of the Company as the Group holds interests in such entities. None of the connected person of the Company holds interests in or position with such entities, and such entities are not considered connected person under the Listing Rules; (2) purchase of forage from Shengmu Forage in accordance with the Forage Supply Framework Agreement; (3) purchase of feed from Sijichun in accordance with the Feed Supply Framework Agreement; and (4) payment of emoluments to key management of the Group. The arrangement whereby Shengmu Forage provided biowaste (i.e. cow dung) cleaning services to our organic dairy farms for free in return for our supply of such unprocessed biowaste from our organic dairy farms to Shengmu Forage for free, is an exempt continuing connected transaction, details of which has been set out in the section headed "Continuing Connected Transaction" in the Prospectus of the Company. All the requirements under Chapter 14A of the Listing Rules have been complied with for the year ended December 31, 2016.

EMPLOYEES

As at December 31, 2016, the Group had a total of 3,849 employees (3,713 employees in total as at December 31, 2015). Total staff costs for 2016 (including the emoluments of Directors and senior management of the Company) amounted to RMB280.2 million (excluding equity-settled share option expenses) (RMB258.7 million in 2015).

The Group believes that the dedicated efforts of all of its employees are the very essence of the Group's rapid development and success in the future. The Group provides management personnel and employees with on-the-job education, training and other opportunities to improve their skills and knowledge. In general, the Group determines employee compensation based on each employee's performance, qualifications, position and seniority. The Group has made contributions to the social security funds and housing reserve for its employees in accordance with the relevant national and local social welfare laws and regulations.

The Group has also approved and adopted a pre-IPO share option scheme (the "**Pre-IPO Share Option Scheme**") and a share option scheme (the "**Share Option Scheme**"). The purpose of the Pre-IPO Share Option Scheme and the Share Option Scheme is to attract, retain and motivate the Directors, senior management and employees of the Group and other participants.

RETIREMENT BENEFIT PLANS

The Group has participated in a number of fixed contribution retirement plans for eligible employees within the Group in accordance with applicable laws and regulations.

REMUNERATION POLICY FOR DIRECTORS AND SENIOR MANAGEMENT

The remunerations of Directors and senior management are determined based on their working experience, industry expertise, educational background and skills as well as the Group's performance and operating results and with reference to the remuneration policies of other companies in the industry and prevailing market rates. Directors and employees also participate in performance incentive arrangements relating to the performance of the Group and individuals.

For the year of 2016, no emoluments were paid by the Group to any Director or any of the five highest paid individuals of the Company as an inducement to join or upon joining the Group or as compensation for loss of office. None of the directors has waived any emoluments for the year ended December 31, 2016.

For details of remuneration paid to the Directors and the five highest paid individuals which are required to be disclosed pursuant to Appendix 16 of the Listing Rules, please refer to Notes 9 and 10 to the financial statements.

SUFFICIENT PUBLIC FLOAT

Based on the public information available to the Company and so far as all Directors are aware, the Company had maintained the public float as required by the Listing Rules throughout the period up to the latest practicable date prior to the publication of this annual report.

AUDITORS

Ernst & Young has audited the financial statements for the year ended December 31, 2016. A resolution for the reappointment of Ernst & Young as auditors of the Company will be proposed at the forthcoming annual general meeting.

By Order of the Board of
China Shengmu Organic Milk Limited
Yao Tongshan
Chairman

Hong Kong, March 20, 2017

DIRECTORS AND SENIOR MANAGEMENT

EXECUTIVE DIRECTORS

Mr. **YAO Tongshan (姚同山)**, aged 60, is the founder of our Group, chairman of the Board, chief executive officer and executive Director of the Company. He is also the chairman of the nomination committee of the Company. He is primarily responsible for our Company's strategic planning and long term business planning, overall business, market development and operation management, annual budgets, business plan, and other significant matters arising from ordinary business operation. Mr. YAO was appointed to our Board in February 2014. For positions with other members of the Group, Mr. YAO is also the director of Shengmu Holding, Inner Mongolia IMU-Shengmu High-tech Dairy Co., Ltd. (內蒙古內大聖牧高科牧業有限公司) ("**IMU-Shengmu Dairy**"), Inner Mongolia Shengmu Holding Co. Ltd. (內蒙古聖牧控股有限公司) ("**Shengmu Farming**"), Inner Mongolia Shengmu High-tech Dairy Co., Ltd. (內蒙古聖牧高科奶業有限公司) ("**Shengmu Dairy**"), Shining Investment Industry Limited ("**Shining Investment**"), China Mengniu Investment Company Limited (中國蒙牛投資有限公司) ("**Mengniu Investment**"), Saint Investment HK Limited ("**Saint Investment**"), Flourish Treasure Holdings Limited ("**Flourish Treasure**"), Horizon King Investments Limited ("**Horizon King**"), Fortune Globe Limited ("**Fortune Globe**"), Saint Investment (Cayman) Limited ("**Saint Investment (Cayman)**"), Credence Global Investments Limited ("**Credence Global**") and Elite Noble Investment Limited ("**Elite Noble**"). He has over 15 years of experience in the dairy industry, with extensive industry and management experiences. In March 2014, Mr. YAO was honored as one of the top 10 economic figures in Inner Mongolia (內蒙古經濟年度十大人物) of 2013 for his contribution to the development of local economy jointly by Inner Mongolia Daily (內蒙古日報社), Inner Mongolia Federation of Industry and Commerce (General Chamber of Commerce) (內蒙古自治區工商聯(總商會)) and Inner Mongolia Association of Entrepreneurs (內蒙古企業家聯合會).

In December 2016, Mr. YAO was honored as one of the 50 business leaders influencing the Inner Mongolia economy in the 50 Business Leaders Influencing the Inner Mongolia Economy (影響內蒙古經濟的50位商界領袖) campaign held by Inner Mongolia Financial Network (內蒙古金融網) jointly with such institutions as Inner Mongolia Association of Financiers and Entrepreneurs (內蒙古金融家及企業家聯合會).

Mr. YAO was the chief financial officer and executive director of China Mengniu Dairy Company Limited (中國蒙牛乳業有限公司) which is listed on the Stock Exchange (stock code:2319) from July 2008 to March 2010. Mr. YAO served as the chief financial officer, financial vice president and director of Inner Mongolia Mengniu a subsidiary of China Mengniu Dairy Company Limited, which is principally engaged in manufacturing of liquid milk, ice cream and other dairy products, between October 2001 and January 2010. Mr. YAO gained relevant finance and investment experience by serving as project manager (primarily responsible for identifying appropriate investment opportunities) of Inner Mongolia Investment Consultancy Company (內蒙古投資諮詢公司) (a subsidiary of China Construction Bank which is principally engaged in investment business) between July 1988 and January 1991; and as head of International credit department, manager of the credit department of China Construction Bank (Inner Mongolia branch) between January 1991 and July 1999. Mr. YAO was also the general manager (mainly responsible for providing finance and accounting advice) of Inner Mongolia Jingtong Investment Consultancy Company (內蒙古景通投資顧問公司) (principally engaged in providing finance advisory) from September 1999 to September 2001.

Mr. YAO graduated from Inner Mongolia University of Technology (內蒙古工業大學) (formerly known as Inner Mongolia Engineering College (內蒙古工學院)) with a bachelor's degree in power engineering in August 1982 and Tianjin University (天津大學) with a master's degree in engineering in June 1988. Mr. YAO was awarded the qualification as a senior economist (高級經濟師) by People's Construction Bank of China (formerly known as China People's Construction Bank) in December 1995.

Save as disclosed above, Mr. YAO did not hold directorships in any public listed companies in the last three years.

Mr. **WU Jianye (武建鄴)**, aged 43, is the president and executive Director of the Company. He is primarily responsible for the management and operation of our Group such as the strategic management and implementing the key performance indicator of Shengmu Farming and Shengmu Dairy. Mr. WU was appointed to our Board on March 26, 2014. For position with other members of the Group, Mr. WU is also the director of Shengmu Holding, IMU-Shengmu Dairy and Shengmu Pangu. He has over 12 years of management experience in various different industries. Mr. WU joined our Group in September 2010 as an assistant to chief executive officer and was designated as the president of Shengmu Holding in August 2013.

Prior to joining our Group in September 2010, he was the chairman and president (mainly responsible for operational management) of Inner Mongolia Pangu Group Co., Ltd. (內蒙古盤古集團有限責任公司) (principally engaged in agricultural business) between May 2003 and August 2010. Mr. WU was the general manager (mainly responsible for overall management and sales) of Inner Mongolia Pangu Cashmere Co., Ltd (內蒙古盤古羊絨製品有限公司) (principally engaged in manufacture of cashmere) between January 2000 and May 2003.

Mr. WU graduated from the University of Inner Mongolia (內蒙古大學) in July 1995 and was awarded a college graduate certificate (專科) majoring in Chinese language and further obtained the bachelor's degree from University of Inner Mongolia (內蒙古大學) in January 2007 majoring in law (distance learning). Mr. WU also received his executive master of business administration in July 2009 from Tsinghua University in the PRC.

Save as disclosed above, Mr. WU did not hold directorships in any public listed companies in the last three years.

Ms. **GAO Lingfeng (高凌鳳)**, aged 46, is the vice president and executive Director of the Company. She is primarily responsible for setting up and implementing key performance indicators for various business units, production chain's quality management and organic certification management. In addition, Ms. GAO is primarily responsible for the evaluation, improvement and monitoring of our quality control system, and oversees the Group's overall administrative operation and the coordination between various business departments, and is also principally responsible for overseeing the management of Shengmu Farming. Ms. GAO was appointed to our Board on March 26, 2014. For position with other members of the Group, Ms. GAO is also the director of Shengmu Holding, IMU-Shengmu Dairy, Shengmu Agriculture and Shengmu Farming. She has over 17 years of experience in the dairy industry and 18 years of management experience in production and product quality.

Ms. GAO joined our Group since its establishment in October 2009 as vice president of Shengmu Holding. Prior to joining our Group, Ms. GAO has held various management positions with Inner Mongolia Mengniu, including head of quality control department between October 1999 and April 2009.

Ms. GAO received her master of business administration from Inner Mongolia University of Technology (內蒙古工業大學) (formerly known as Inner Mongolia Engineering College (內蒙古工學院)) in January 2011.

Save as disclosed above, Ms. GAO did not hold directorships in any public listed companies in the last three years.

Mr. **CUI Ruicheng (崔瑞成)**, aged 34, is the vice president, chief financial officer and executive Director of the Company. He is primarily responsible for the financial management of the Group. Mr. CUI was appointed to our Board on March 26, 2014. For position with other members of the Group, Mr. CUI is also the director of Shengmu Holding. He has over 12 years of experience in the dairy industry and financial management.

Mr. CUI joined our Group since its establishment in October 2009. He has been appointed as a Joint Company Secretary of the Company since December 4, 2015. He has served as the vice president (finance) and chief financial officer of Shengmu Holding since January 2014. Prior to joining our Group, Mr. CUI held various financial and accounting positions with Inner Mongolia Mengniu, including accountant and listing administrator between July 2003 and August 2006, and was the finance department head with Inner Mongolia Mengniu Shengwu Zhineng Company Limited (內蒙古蒙牛生物質能有限公司) between August 2006 and September 2009.

Mr. CUI passed the accounting final exams (self-learning) with Inner Mongolia University of Finance and Economics (內蒙古財經大學) (formerly known as Inner Mongolia Finance and Economics College (內蒙古財經學院)) and was awarded a college graduate certificate (專科) in December 2005 and obtained the bachelor's degree from China University of Geosciences (中國地質大學) in July 2009 majoring in business administration (on-line study). Mr. CUI is a qualified accountant in the PRC since May 2006.

Save as disclosed above, Mr. CUI did not hold directorships in any public listed companies in the last three years.

NON-EXECUTIVE DIRECTORS

Mr. **DONG Xianli (董先理)**, aged 52, is a non-executive Director of the Company. He was appointed to our Board on February 19, 2016.

Mr. DONG is currently the chief financial officer of China Modern Dairy Holdings Ltd. (stock code: 1117). Mr. DONG was an assistant vice president of Inner Mongolia Mengniu, a subsidiary of China Mengniu Dairy Company Limited, a company listed on the main board of the Stock Exchange (stock code: 2319) before December 1, 2016. Mr. DONG is primarily responsible for investment management, property management, risk control and internal audits of Inner Mongolia Mengniu. Mr. DONG joined Inner Mongolia Mengniu in January 2004 and has held various positions such as investment controller and financing controller since then. Mr. DONG has extensive experience in auditing, finance and investment management.

Mr. DONG received his bachelor's degree from Beijing Forestry University (北京林業大學) (formerly known as Beijing Forestry College (北京林學院)) in July 1985, majoring in soil and water conservation and his master of project management from Inner Mongolia University of Technology (內蒙古工業大學) in January 2010, Mr. DONG has obtained qualifications as a Certified Public Accountant and a Certified Asset Appraiser in the People's Republic of China.

Save as disclosed above, Mr. DONG did not hold directorships in any public listed companies in the last three years.

Mr. **FAN Xiang (范翔)**, aged 40, is a non-executive Director of the Company. He was appointed to our Board on March 26, 2014. For position with other members of the Group, Mr. FAN is also the director of Shengmu Holding since December 2013. In addition to his role with our Company, Mr. FAN is currently the chairman and general manager of Goldman Sachs Broad Street (Beijing) Equity Investment Management Co., Ltd. (北京高盛寬街博華股權投資管理有限公司), a wholly-owned subsidiary of The Goldman Sachs Group, Inc. (高盛集團有限公司) (collectively "**Goldman Sachs**") since January 2013. Prior to the relocation to Beijing in January 2013, Mr. FAN was with the Hong Kong principal investment area and the New York investment banking division of Goldman Sachs as managing director and executive director from August 2007 to December 2012. Mr. FAN was with KKR Asia Limited as manager from March 2006 to July 2007.

Mr. FAN graduated with a bachelor's degree of arts from Yale University in the United States in May 1999 and received his master of business administration from the Wharton School, University of Pennsylvania in the United States in May 2004.

Save as disclosed above, Mr. FAN did not hold directorships in any public listed companies in the last three years.

Mr. **CUI Guiyong (崔桂勇)**, aged 54, is a non-executive Director of the Company. He was appointed to our Board on March 26, 2014. He is also a member of the audit committee. For position with other members of the Group, Mr. CUI is also the director of Shengmu Holding since December 2013. In addition to his role with our Company, Mr. CUI is currently the managing director of Baring Private Equity Asia Limited since January 2012. Mr. CUI served as a managing director at HOPU Investment Management Co. Ltd. since May 2008 and a partner in October 2009. Prior to joining HOPU Investment Management Co., Ltd., Mr. CUI was an investment banker for 14 years, during which he served as the managing director of Morgan Stanley Asia Limited between April 2007 and April 2008, managing director of GIBA-Resources and Energy of HSBC Markets (Asia) Limited between March 2004 and April 2007, head of Investment Banking Division of ICEA Capital Limited from June 2002 to August 2003 and assumed various positions in N M Rothschild & Sons (Hong Kong) Limited from September 1994 to June 2002, including the position of the chief representative of China in its Beijing Office before he left the company in 2002.

Mr. CUI obtained his Doctor of Philosophy degree from the University of Oxford in the United Kingdom in May 1995, and Bachelor of Engineering and Master of Engineering degrees from the University of Science and Technology of Beijing (北京科技大學) in April 1982 and June 1987, respectively.

Mr. CUI has served as a non-executive director of COFCO Meat Holdings Limited which is listed on the Stock Exchange (stock code: 1610), since May 2016. He has served as a non-executive director of AAG Energy Holdings Limited which is listed on the Stock Exchange (stock code: 2686), since January 2015.

Save as disclosed above, Mr. CUI did not hold directorships in any public listed companies in the last three years.

Mr. **SUN Qian (孫謙)**, aged 43, is a non-executive Director of the Company. He was appointed to our Board on March 26, 2014 and he is a member of the remuneration committee. Mr. SUN currently is a partner of Sequoia Capital China.

Mr. SUN received a bachelor' s degree in applied mathematics from Harvard University in the United States in June 1997, and master of business administration from Harvard University and a juris doctor degree from Harvard Law School in the United States both in June 2003.

Mr. SUN was a director of Bona Film Group Limited (principally engaged in film distribution business), a company listed on NASDAQ, from 2007 to 2011 and a director of 500.com Limited (principally engaged in online sports lottery services) since October 2013. Mr. SUN has been a non-executive director in Dongpeng Holdings Company Limited, a company listed on the Stock Exchange (stock code: 3386)(delisted from the Stock Exchange at four p.m. on June 22, 2016), from December 2013 to June 2016.

Save as disclosed above, Mr. SUN did not hold directorships in any public listed companies in the last three years.

Mr. **SHAO Genhuo (邵根夥)**, aged 51, is a non-executive Director of the Company. He was appointed to our Board on September 26, 2016.

Mr. SHAO Genhuo is currently the chairman of the board of directors and president of Dabeinong Group, a company listed on the Small and Medium Enterprise Board of the Shenzhen Stock Exchange (stock code: 2385). Mr. SHAO is primary responsible for the strategic planning and overall management of DBN Group. Mr. SHAO founded DBN Group in October 1994 and served as its chairman and general manager since then.

Mr. SHAO received his bachelor's degree from Zhejiang University (浙江大學) (formerly known as Zhejiang Agricultural University (浙江農業大學)) in 1986. Mr. SHAO received his master's and doctoral degree from China Agricultural University (中國農業大學) (formerly known as Beijing Agricultural University (北京農業大學)) in 1988 and 1991, respectively.

Save as disclosed above, Mr. SHAO did not hold directorships in any public listed companies in the last three years.

Mr. **ZHANG Jiawang (張家旺)**, aged 38, is a non-executive Director of the Company. He was appointed to our Board on September 26, 2016.

Mr. ZHANG Jiawang is currently a vice president and manager of strategy and development of DBN Group. Mr. ZHANG joined DBN Group in August 2001 and has held various positions, including outreach director, development and investment manager and president's assistant since then.

Mr. ZHANG received his bachelor's degree from Inner Mongolia Agricultural University (內蒙古農業大學) in July 2001, majoring in horticulture and his executive master of business administration from People's University of China (中國人民大學) in January 2010.

Save as disclosed above, Mr. ZHANG did not hold directorships in any public listed companies in the last three years.

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. **WONG Kun Kau (黃灌球)**, aged 56, is an independent non-executive Director of the Company. He was appointed to our Board on June 18, 2014. He is a chairman of the remuneration committee and a member of the nomination committee. Mr. WONG has more than 24 years of experience in investment banking and corporate finance. He is currently the founder and managing partner of Bull Capital Partners Ltd. ("**Bull Capital**"), a fund management company specializing in direct investment in the greater China region.

Mr. WONG received his bachelor's degree in social science from The University of Hong Kong in November 1982.

Mr. WONG was an independent non-executive director of Sun. King Power Electronics Group Limited, a company listed on the Stock Exchange (stock code: 580) (principally engaged in trading and manufacturing of power electronic components) from May 2010 to June 2015. He is also the independent non-executive director of West China Cement Limited (principally engaged in manufacture and sale of cement and cement products) since July 2010, Anhui Conch Cement Company Limited ("**Anhui Conch**") (principally engaged in manufacture and sales of clinker and cement products) from May 2012 to June 2016, Lifestyle Properties Development Limited (principally engaged in property development and property investment) since August 2013, all of which are listed on the Stock Exchange (stock code: 2233, stock code: 914 and stock code: 2183, respectively) and an independent non-executive director of REF Holdings Limited (principally engaged in financial printing services) (stock code: 8177), since September 2015; Anhui Conch is additionally listed on The Shanghai Stock Exchange (stock code: 600585).

Save as disclosed above, Mr. WONG did not hold directorships in any public listed companies in the last three years.

Mr. **LI Changqing (李長青)**, aged 60, is an independent non-executive Director of the Company. He was appointed to our Board on June 18, 2014. He is a member of the audit committee and remuneration committee.

Mr. LI is currently a professor and tutor of doctoral students and has been appointed as the director of the academic committee of Inner Mongolia University of Technology (內蒙古工業大學), since 2010. Mr. LI started his career with Inner Mongolia University of Technology (內蒙古工業大學) in 1982, and has held various positions including serving as the director of business management department, deputy director of management engineering department, dean of school of international business school and founding dean of the college of management between 1996 and 2010. Mr. LI also served as a vice chairman to the Inner Mongolia Academy of Management (內蒙古管理學會) since 2006 and a director to the Inner Mongolia Management Modernization Research Center (內蒙古管理現代化研究中心) since 2007, respectively.

Mr. LI is widely recognized for his research and has received numerous awards in recognition of his exemplary work including the title of National outstanding teacher (全國優秀教師稱號) awarded in September 2014, Inner Mongolia outstanding talent award (內蒙古自治區傑出人才獎) by Inner Mongolia Autonomous Region Government in September 2012 and the first-class award of Inner Mongolia science and technology progress (內蒙古自治區科學技術進步一等獎) by Inner Mongolia Autonomous Region Government in January 2009, Wuyi-Worker Medal of the Autonomous Region (全區五一勞動獎章) by Inner Mongolia Autonomous Region General Worker Union (內蒙古自治區總工會) in April 2012 and received special allowance from the State Council in March 2009 in recognition of his outstanding contribution in the education sector.

Mr. LI graduated with a bachelor's degree in engineering from Inner Mongolia University of Technology (內蒙古工業大學) (formerly known as Inner Mongolia Engineering College (內蒙古工學院)) in January 1982, received a master's degree of engineering from Tianjin University (天津大學) in April 1995, and received his doctorate in management science from Huazhong University of Science and Technology (華中科技大學) in the PRC in June 2005.

Save as disclosed above, Mr. LI did not hold directorships in any public listed companies in the last three years.

Ms. **GE Xiaoping (葛曉萍)**, aged 53, is an independent non-executive Director of the Company. She was appointed to our Board on June 18, 2014. She is the chairman of the audit committee. Ms. GE has over 32 years of experience in auditing and accounting, she is a certified public accountant in PRC and certified public valuer in the PRC.

Ms. GE is currently a partner and branch chief representative (Xiamen branch) for BDO China Shu Lun Pan Certified Public Accountants LLP ("**BDO**") (立信會計師事務所(特殊普通合夥)) since March 2010. Ms. GE was the accounting lecturer for the People's Liberation Army Necessities and Finance College (中國人民解放軍軍需財經高等專科學校) between June 1989 and January 1997, and she held various positions (including accountant) with Hubei Electronic Engines Factory (湖北電機廠) (principally engaged in manufacture of electronic engines) between December 1980 and June 1989.

Ms. GE received numerous awards and appointments in recognition of her exemplary work including: a member of the eleventh and twelfth Xiamen Chinese People's Political Consultative Conference (廈門市政協第十一屆、十二屆委員) (with the appointment term from 2007 to 2016), Outstanding Member of the People's Political Consultative Conference (2010-2011) (2010-2011年度優秀政協委員) and the vice president of the Certified Public Accountant Association (Xiamen branch) since October 2013.

Ms. GE graduated from Zhongnan University of Economics and Law (中南財經政法大學) (formerly known as Zhongnan University of Economics (中南財經大學)) in the PRC majoring in financial accounting in July 1995.

Ms. GE was an independent director of Tsann Keun China Enterprise Co., Ltd. (廈門燦坤實業股份有限公司), a company listed on the Shenzhen Stock Exchange (stock code: 200512), between May 2008 and May 2014.

Save as disclosed above, Ms. GE did not hold directorships in any public listed companies in the last three years.

Mr. **YUAN Qing (袁清)**, aged 59, is an independent non-executive Director of the Company. He was appointed to our Board on June 18, 2014. He is a member of the nomination committee. Mr. YUAN has over 28 years of experience in academic research, on the subject of grassland resources.

Mr. YUAN has been engaged in research work with the Institute of Grassland Research Chinese Academy of Agricultural Sciences (中國農業科學院草原研究所) since 1986. Mr. YUAN was the vice president of the China Grassland Society of Grassland Resources and Professional Committee (中國草學會草地資源與利用專業委員會) from September 2007 to October 2013, the head of resources and environmental research office in the Institute of Grassland Research of Chinese Academy of Agricultural Sciences (中國農業科學院草原研究所資源與環境研究室) from 2002 to 2005 and currently a member of the academic committee of the Institute of Grassland Research of Chinese Academy of Agricultural Sciences (中國農業科學院草原研究所學術委員會). Mr. YUAN served as the standing director and deputy general-secretary of China branch of the Association of Remote Sensing Applications, Environmental Remote Sensing (中國遙感應用協會環境遙感分會) from December 2006 to August 2013, and is currently the vice president of it.

Mr. YUAN is widely recognized for his research work, and was recognized as the Young Expert with Outstanding Contribution (中青年有突出貢獻專家) by the PRC's Ministry of Agriculture (中華人民共和國農業部) in December 2001. Mr. YUAN was awarded the special allowance (特殊津貼) from the State Council in April 1999.

Mr. YUAN received his master's degree in agriculture from the Chinese Academy of Agricultural Sciences (中國農業科學院) in the PRC in November 1986.

Mr. YUAN is an independent director in Inner Mongolia M-Grass Ecology and Environment (Group) Co., Ltd. (內蒙古蒙草生態環境（集團）股份有限公司) (principally engaged in construction of garden landscape), a company listed on the Shenzhen Stock Exchange (stock code: 300355) from August 2010 to October 2016.

Save as disclosed above, Mr. YUAN did not hold directorships in any public listed companies in the last three years.

Mr. **FU Wenge (付文革)**, aged 50, is an independent non-executive Director of the Company. He was appointed to our Board on September 26, 2016.

Mr. FU Wenge is currently a professor and doctoral supervisor at the Economic Management School of China Agricultural University (中國農業大學) (formerly known as Beijing Agricultural University (北京農業大學)). Mr. FU has been working in Agricultural University since July 1997 and held various positions including associate professor and the director of MBA education center.

Mr. FU worked in Kaifeng Education College (開封師範高等專科學校), now known as Henan University (河南大學), as a lecturer from July 1986 to September 1994. Mr. FU received his associate degree in English from Kaifeng Education College in June 1986 and master's degree in economics from Henan University in June 1997. Mr. FU received his doctor's degree in economics in Renmin University of China in June 2004.

Save as disclosed above, Mr. FU did not hold directorships in any public listed companies in the last three years.

SENIOR MANAGEMENT

Mr. **YAO Tongshan (姚同山)**, aged 60, is the founder of our Group, chairman, chief executive officer and executive Director of our Company. His biographical details are set out under the section "Executive Directors" above.

Mr. **WU Jianye (武建鄴)**, aged 43, is the president and executive Director of our Company. His biographical details are set out under the section "Executive Directors" above.

Ms. **GAO Lingfeng (高凌鳳)**, aged 46, is a vice president and executive Director of our Company. Her biographical details are set out under the section "Executive Directors" above.

Mr. **CUI Ruicheng (崔瑞成)**, aged 34, is the vice-president, chief financial officer, executive Director and Joint Company Secretary of our Company. His biographical details are set out under the section "Executive Directors" above.

Mr. **AU Wai Keung (區偉強)**, aged 45, is a Joint Company Secretary of our Company. Mr. AU was appointed on March 27, 2014. Mr. AU has more than 18 years of experience in the area of accounting. Currently, Mr. AU is a director of Arion & Associated Limited (亞利安會計事務所有限公司), a corporate secretarial and accounting services provider in Hong Kong. He is now also the company secretary of Honworld Group Limited (老恒和釀造有限公司) (stock code: 2226), China Digital Video Holdings Limited (stock code: 8280), and SDM Group Holdings Limited (stock code: 8363). Mr. AU obtained a bachelor's degree in social sciences from the Chinese University of Hong Kong in December 1993 and a master's degree in business administration from the City University of Hong Kong in November 1999. He is a fellow member of the Hong Kong Institute of Certified Public Accountants and a member of the Institute of Chartered Accountants in England and Wales.

For details of interest (as defined in Part XV of the Securities and Futures Ordinance) in the shares of the Company by our Directors, please refer to the section headed "Report of the Directors – Directors' and chief executive's interests and short positions in shares, underlying shares and debentures of the Company" in this annual report.

Save as disclosed above, no further information of our Directors or senior management is required to be disclosed pursuant to Rules 13.51(2)(h) to (v) under the Listing Rules.

CORPORATE GOVERNANCE PRACTICES

The Company ensures that the Company and its subsidiaries are committed to achieving and maintaining high standards of corporate governance. The Board understands the influence and importance of high standards of corporate governance on the value of the Company, and that good corporate governance is in the interest of the Group and shareholders on the whole.

We have adopted, applied and complied with the code provisions contained in the Code on Corporate Governance and Corporate Governance Report (the "**Code**") as set out in Appendix 14 to the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (the "**Listing Rules**") (as amended from time to time) for the year ended December 31, 2016, except for provision A2.1 of the Corporate Governance Code as disclosed below.

Pursuant to provision A2.1 of the Corporate Governance Code, the roles of chairman and chief executive officer should be separate and should not be performed by the same individual. However, the Company does not have a separate chairman and chief executive officer and Mr. YAO Tongshan currently performs these two roles. The Board believes that vesting the roles of both chairman and chief executive officer in the same person has the benefit of ensuring the consistent leadership within the Group and enables more effective and efficient overall strategic planning and implementation for the Group. The Board considers that the balance of power and authority for the present arrangement will not be impaired and this structure will enable the Company to make and implement decisions promptly and effectively. The Board will continue to review and consider splitting the roles of chairman of the Board and chief executive officer of the Company at a time when it is appropriate and suitable by taking into account the circumstances of the Group as a whole.

BOARD OF DIRECTORS

The Board is the decision-making body of the Company, and is responsible for formulating overall strategies and policies of the Group and approving its implementation plans to ensure that the Group achieves its goal swiftly. For the year ended December 31, 2016, the responsibilities performed by the Board include: formulation of strategies of the Company; formulation of development goals, guidelines and policies and implementation plans of the Company; control of and assessment on the fulfillment of the Company's financial and operating goals; review and approval of annual financial budgets, final accounts plans, profit distribution plans and compensation plans of the Company; establishment of effective internal control systems for risks assessment; and review and approval of the Company's material contracts and transactions, information disclosure, connected transactions and other matters required to be handled by the Board.

Moreover, the functions of Corporate Governance of the Broad include: formulation and review of corporate governance policies and practices of the Company; review and monitor of the training and continuous professional development of the Directors and senior management; review and monitor of the Company's policies and practices on compliance with legal and regulatory requirements; formulation, review and monitoring of the code of conducts for staff and the Directors; and review of the Company's compliance with other provisions contained in the Listing Rules from time to time and disclosure in the Corporate Governance Report.

Delegation by the Board

To assist the Board in execution of its duties and facilitate effective management, certain functions of the Board have been delegated by the Board to several committees under the Board (including the Audit Committee, Remuneration Committee and Nomination Committee) and senior management. All Board committees perform respective functions and duties within their terms of reference (which are available for inspection by the public on the websites of the Company and the Stock Exchange).

With the leadership of the chief executive officer, the senior management is delegated by the Board with authorities and duties on the daily operation and management of the Group. The delegated functions and work progress will be reviewed regularly. Approval from the Board shall be obtained by the Company before entering into of any material transactions.

Composition of the Board

For the year ended December 31, 2016, the Board was comprised of fifteen Directors, including four executive Directors (Mr. YAO Tongshan, Mr. WU Jianye, Ms. GAO Lingfeng and Mr. CUI Ruicheng); six non-executive Directors (Mr. DONG Xianli, Mr. FAN Xiang, Mr. CUI Guiyong, Mr. SUN Qian, Mr. SHAO Genhuo and Mr. ZHANG Jiawang); and five independent non-executive Directors (Mr. WONG Kun Kau, Mr. LI Changqing, Ms. GE Xiaoping, Mr. YUAN Qing and Mr. FU Wenge). The Chairman of the Board of the Company is Mr. YAO Tongshan. Each of Mr. SHAO Genhuo and Mr. ZHANG Jiawang was appointed as a non-executive Director of the Company on September 26, 2016. Mr. FU Wenge was appointed as an independent non-executive Director of the Company on September 26, 2016. Mr. WU Jingshui resigned as a non-executive Director of the Company on February 19, 2016, and Mr. DONG Xianli was appointed as a non-executive Director of the Company on February 19, 2016.

Biographical details of the existing Directors are set out in the section headed "Directors and Senior Management" in this annual report.

Permitted Indemnity Provision

As at the date of this report, the Company has maintained adequate liability insurances cover in respect of potential legal actions against its Directors.

Appointment, Re-election and Dismissal of Directors

Each of the Directors (including independent non-executive Directors) has signed a service agreement or an appointment letter with the Company for a term of three years. The Directors shall be subject to retirement from office by rotation or re-election at the forthcoming annual general meeting of the Company pursuant to Article 16 of the Articles of Association of the Company.

Pursuant to Article 16.2 of the Articles, any Director appointed by the Board to fill a casual vacancy or as an addition to the existing Directors shall hold office only until the next following general meeting of the Company and shall then be eligible for the re-election. Pursuant to Article 16.3 of the Articles, any Director appointed by ordinary resolution to fill a casual vacancy or as an addition to the existing Directors shall hold office only until the next following general meeting of the Company and shall then be eligible for re-election.

According to Article 16.18 of the Articles, at every annual general meeting of the Company, one-third of the Directors for the time being (or, if their number is not three or a multiple of three, then the number nearest to, but not less than, one-third) shall retire from office by rotation provided that every Director (including those appointed for a specific term) shall be subject to retirement by rotation at least once every three years. Any Director appointed pursuant to Article 16.2 or Article 16.3 of the Articles shall not be taken into account in determining which Directors are to retire by rotation. A retiring Director shall retain office until the close of the meeting at which he retires and shall be eligible for re-election. The Company at any annual general meeting at which any Directors retire may fill the vacated office by electing a like number of persons to be Directors.

Board Diversity Policy

The Board implements a policy of diversified composition of the Board. For the purpose of sustained and balanced development, the Company recognises that the Board diversity is critical for facilitating its strategic goals and maintaining its sustainable development. All appointments to the Board are in the principle of talents priority plus benefits of the diversified Board composition taken into account. The selection of Board members is initially based on multiple factors from the point of the Board diversity, including but not limited to, gender, age, cultural and educational background, professional experience, skills, knowledge and terms of service. Then, we will make decisions according to our specific requirements for talents at different stages of business development and strategic planning.

Independent Non-executive Directors

The Company has complied with the requirement of appointing adequate number of independent non-executive Directors under Rule 3.10 of the Listing Rules. Ms. GE Xiaoping, one of the independent non-executive Directors of the Company has an experience of over 32 years in the auditing and accounting and is a PRC certified accountant.

The Company has received the letter of confirmation issued by each of the independent non-executive Directors as to his/her independence pursuant to Rule 3.13 of the Listing Rules and considers that all the independent non-executive Directors are independent.

Board Meeting

The Board convenes a meeting on a regular basis and at least four meetings each year. In 2016, the Board held six meetings at which the operating results, investment issues, etc. of the Company were considered and discussed.

Attendance record is as below:

Members	Meetings attended/ meetings held since respective appointment date	Attendance
Executive Directors		
Mr. YAO Tongshan	6/6	100%
Mr. WU Jianye	6/6	100%
Ms. GAO Lingfeng	6/6	100%
Mr. CUI Ruicheng	6/6	100%
Non-executive Directors		
Mr. DONG Xianli	6/6	100%
Mr. FAN Xiang	6/6	100%
Mr. CUI Guiyong	5/6	83%
Mr. SUN Qian	6/6	100%
Mr. SHAO Genhuo	2/3	66%
Mr. ZHANG Jiawang	3/3	100%
Mr. WU Jingshui [Note1]	1/1	100%
Independent non-executive Directors		
Mr. WONG Kun Kau	6/6	100%
Mr. LI Changqing	6/6	100%
Ms. GE Xiaoping	6/6	100%
Mr. YUAN Qing	6/6	100%
Mr. FU Wenge	3/3	100%

Notes:

(1) Mr. WU Jingshui resigned as a non-executive Director with effect from February 19, 2016. He attended the relerant Board meetings convened before his resignation.

DIRECTOR TRAINING

The Company provides an introduction and related documents necessary for all new Directors upon joining the Board to ensure a broad understanding of the Company's business and operation model as well as the laws, regulations and various rules pertaining to the Company.

The Company encourages and supports all the Directors (i.e. Mr. YAO Tongshan, Mr. WU Jianye, Ms. GAO Lingfeng, Mr. CUI Ruicheng, Mr. DONG Xianli, Mr. FAN Xiang, Mr. CUI Guiyong, Mr. SUN Qian, Mr. SHAO Genhuo, Mr. ZHANG Jiawang, Mr. WONG Kun Kau, Mr. LI Changqing, Ms. GE Xiaoping, Mr. YUAN Qing and Mr. FU Wenge) to receive training and encourages their continuous professional development, so as to develop and keep abreast of their knowledge and skills better and serve the Company more efficiently. The Company offers training opportunities for all the Directors from time to time. During the year, the legal advisors of the Company have provided training on among others, directors' duties, inside information provisions, the Takeovers Code, market misconduct and continuing duties under the Companies Ordinance and the Listing Rules for all Directors.

BOARD COMMITTEES

The Company has three Board committees, namely the Remuneration Committee, the Nomination Committee and the Audit Committee. Each committee performs its work in accordance with the terms of reference approved by the Board.

REMUNERATION COMMITTEE

The Company established the Remuneration Committee on June 18, 2014 in compliance with the Corporate Governance Code set out in Appendix 14 to the Listing Rules. The Remuneration Committee was established with written terms of reference in compliance with the Corporate Governance Code. The primary functions of the Remuneration Committee include determining the policies in relation to human resources management, reviewing the Company's remuneration policies and determining remuneration packages for the Directors and senior management members. As at December 31, 2016, the Remuneration Committee comprised two independent non-executive Directors (Mr. WONG Kun Kau and Mr. LI Changqing) and one non-executive Director (Mr. SUN Qian) and was chaired by Mr. WONG Kun Kau.

According to the terms of reference of the Remuneration Committee of the Company, the Remuneration Committee convenes at least one meeting in each year. In 2016, the Remuneration Committee convened a total of two meetings, whereby the overall remuneration policy and structure for Company's Directors and senior management members and proposals on the establishment of standard and transparent procedures for the formulation of remuneration policies were reviewed.

NOMINATION COMMITTEE

The Company established the Nomination Committee on June 18, 2014 in compliance with the Corporate Governance Code set out in Appendix 14 to the Listing Rules. The Nomination Committee was established with written terms of reference in compliance with the Corporate Governance Code. The primary duties of the Nomination Committee are to make recommendations to the Board regarding candidates to fill vacancies on the Board. As at December 31, 2016, the Nomination Committee comprised two independent non-executive Directors (Mr. YUAN Qing and Mr. WONG Kun Kau) and one executive Director (Mr. YAO Tongshan) and was chaired by Mr. YAO Tongshan.

The Nomination Committee recommends potential candidates to appointments on the Board based on merits of such candidates, having regard for the benefits of diversity of the members of the Board and the necessity of ensuring a balanced composition of expertise appropriate for the businesses of the Group. The selection of potential candidates is based on a range of diverse factors, including but not limited to gender, age, cultural and educational background, experience (professional or otherwise), skills, knowledge, and leadership qualities, and ultimately, the contribution that such candidates will be able to bring to the Board, to complement the abilities of existing Directors.

According to the terms of reference of the Nomination Committee of the Company, the Nomination Committee convenes at least one meeting in each year. In 2016, the Nomination Committee convened a total of two meetings, whereby the members discussed the structure and composition of the Board of the Company, advised on the proposed changes to the Board for the purpose of the Company's corporate strategies and assessed the independence of independent non-executive Directors.

AUDIT COMMITTEE

The Company established the Audit Committee on June 18, 2014 in compliance with the Corporate Governance Code set out in Appendix 14 to the Listing Rules. The Audit Committee was established with written terms of reference in compliance with the Corporate Governance Code. The primary duties of the Audit Committee are to review and supervise the financial reporting process and internal control system of the Group. The Company modified the terms of reference of the Audit Committee on January 1, 2016. As at December 31, 2016, the Audit Committee comprised two independent non-executive Directors (Ms. GE Xiaoping and Mr. LI Changqing) and one non-executive Director (Mr. CUI Guiyong) and was chaired by Ms. GE Xiaoping.

The Audit Committee has reviewed the accounting standards and practices adopted by the Group and discussed with the management on the internal control and financial reporting matters, including the review of the annual results for 2016.

According to the terms of reference of the Audit Committee of the Company, the Audit Committee convenes at least two meetings in each year. In 2016, the Audit Committee convened a total of two meetings, whereby the members discussed various matters, including the 2015 annual results and 2016 interim results of the Company and its subsidiaries.

The attendance record of Directors at meetings of the Audit Committee, the Remuneration Committee and the Nomination Committee is as follows:

	Number of attendances/meetings		
Directors	Remuneration Committee	Nomination Committee	Audit Committee
YAO Tongshan		2/2	
GE Xiaoping			2/2
WONG Kun Kau	2/2	2/2	
LI Changqing	2/2		2/2
YUAN Qing		2/2	
CUI Guiyong			2/2
SUN Qian	2/2		

GENERAL MEETINGS

For the year ended December 31, 2016, the attendance record of each Director at General Meetings is as follows:

Directors	Number of attendances/ meetings Annual General Meeting
YAO Tongshan	1/1
WU Jianye	1/1
GAO Lingfeng	1/1
CUI Ruicheng	1/1
DONG Xianli	0/1
FAN Xiang	1/1
CUI Guiyong	0/1
SUN Qian	1/1
SHAO Genhuo	N/A
ZHANG Jiawang	N/A
WONG Kun Kau	0/1
LI Changqing	0/1
GE Xiaoping	1/1
YUAN Qing	0/1
FU Wenge	N/A

MODEL CODE FOR DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted a code of conduct regarding securities transactions on terms no less exacting than the required standard of dealings set out in the Model Code for Securities Transactions by Directors of Listed Issuers (the "**Model Code**") as set out in Appendix 10 to the Listing Rules. Having made specific queries to the Directors, all Directors have confirmed that they have complied with the required standards as set out in the Model Code for the year ended December 31, 2016.

DIRECTORS' RESPONSIBILITY FOR FINANCIAL REPORTING IN RESPECT OF THE FINANCIAL STATEMENTS

The Directors acknowledge their responsibility for preparing the Group's accounts and other financial disclosures required under the Listing Rules, meanwhile, the senior management should provide relevant and sufficient information and explanation to the Board to enable it to make informed assessment of the financial and other decisions.

The Directors are not aware of any material uncertainties relating to events or conditions that may cast significant doubt upon the Company's ability to continue as a going concern.

The statement of the auditors of the Company in respect of their reporting responsibilities on the Company's financial statements for the year ended December 31, 2016 is set out in the "Independent Auditor's Report" contained in this annual report.

RISK MANAGEMENT AND INTERNAL CONTROL

Our Group has complied and implemented relevant necessary risk management and internal control in accordance with the Corporate Governance Code and Corporate Governance Report (the "**Code**") as set out in Appendix 14 to the Listing Rules during the year.

The Board acknowledges its responsibility to maintain sound and effective risk management and internal control systems of the Company, which are designed to provide reasonable but not absolute assurance against material misstatement or loss, and to manage rather than eliminate risks of failure to achieve business objectives.

The Board is also responsible for monitoring our risk management and internal control systems of the Group and reviewing the effectiveness of such systems.

The internal control management center of the Group is established to act as the management institution of risk management and internal control, responsible for the evaluation of the establishment, optimization and implementation of internal control system throughout the industrial chain of the Group as to whether the internal control system of the Group is reasonably designed, free from risk and implemented effectively, as well as providing management support for the improvement and refinement of such defects and risks identified, if any, in the progress of evaluation. Meanwhile, the internal control management center is also responsible for diagnosing material risk control matters in each segment throughout the industrial chain of the Group, analyzing, assessing and selecting risk management object for review so as to provide solutions to risk control and related requirements, and tracking the progress and result of risk control for acceptance for the purpose of effective risk management and control.

During the year, each operating and management department of the Group continued to work in system improvement and process optimization to realize the management goal in a more effective and consistent way.

The Group conducts risk management and internal control in different aspects in line with different level of corporate governance, and aims to provide necessary adjustment, restriction, assessment and control measures for the economics, efficiency and effectiveness of the implementation of the Group's operational goals, to keep the assets of the Group safe and intact and to ensure the correctness and reasonableness of accounting data, the compliance with relevant laws, regulations and rules, and such that all operational procedures are free from fraud or error, as it is reasonably able. All employees are committed to continually enhancing the risk management and internal control systems of the Company, linking such systems to our corporate strategies as well as integrating such systems into our day-to-day operation.

With respect to the dissemination of inside information, the Group acknowledges its responsibilities under the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong), the Listing Rules and the overriding principle (that inside information should be announced as soon as possible when it is the subject of a decision). The Group has implemented and disclosed its policy on fair disclosure by pursuing broad, non-exclusive distribution of information to the public through channels such as financial reporting, public announcements and its website. Unauthorised use of confidential or inside information is strictly prohibited by the internal policies of the Group, and the Group has also established and implemented procedures for responding to external enquiries about the Group's affairs.

The Group maintains an internal audit function. Internal audit reports are presented to and reviewed by the audit committee, who reports the findings to the Board. Based on the assessment by the Audit Committee, senior management members and the internal audit department, we did not identify any material internal control flaw or deficit, nor was any major issue raised for improvement, as at December 31, 2016.

COMPANY SECRETARIES

Mr. CUI Ruicheng (崔瑞成), one of our joint company secretaries, is a full-time employee of the Company. Mr. CUI does not possess the qualification as stipulated in Rule 3.28 of the Listing Rules. We have appointed and engaged Mr. AU Wai Keung (區偉強), who possesses the qualification required under Rule 3.28, to act as another joint company secretary. Mr. CUI Ruicheng, the executive director and chief financial officer of the Company, is the usual contact person to liaise with Mr. AU.

Mr. AU and Mr. CUI cooperate with each other to jointly discharge the duties and responsibilities of company secretaries. Meanwhile, Mr. CUI joins relevant training and familiarizes himself with the Listing Rules and the duties required for a company secretary of a company listed on the Stock Exchange.

In 2016, Mr. CUI and Mr. AU, who are the Company's joint company secretaries, confirmed that they had complied with the relevant professional training requirements under Rule 3.29 of the Listing Rules by taking at least 15 hours of relevant professional training.

EXTERNAL AUDITOR AND ITS EMOLUMENTS

The Group's external auditor is Ernst & Young. For the year ended December 31, 2016, the emoluments paid or payable for the audit and non-audit services provided by Ernst & Young was as follows:

	Amount (RMB)
Audit Services	2,700,000
Non-audit Services	250,000
Total	2,950,000

COMMUNICATION WITH SHAREHOLDERS AND INVESTORS/INVESTOR RELATIONS

We adopt active policies to welcome shareholders and investors to put forward valuable advice and suggestions. We assign dedicated staff members to maintain investor relations and regularly or occasionally communicate or coordinate with institutional investors, with an aim to enhance communication and mutual understanding in a timely manner. We will also update the investor relations website in a timely manner, so as to ensure that the shareholders and investors can have timely access to and understand the Company's latest data, information and reports.

PROCEDURES FOR PUTTING FORWARD PROPOSALS AT GENERAL MEETINGS

Shareholders can also send enquiries and proposals to be put forward at general meetings for shareholders' consideration to the Board or senior management by email at zgsm@smorganic.cn or by mail to the principal place of business of the Company in Hong Kong at Room 606-607, 6/F, China Merchants Building, 152-155 Connaught Road Central, Hong Kong Special Administrative Region.

PROCEDURES FOR THE CONVENING OF EXTRAORDINARY GENERAL MEETINGS BY SHAREHOLDERS

Pursuant to the provisions set out in the Articles of Association, the Board may, whenever it thinks fit, convene an extraordinary general meeting. General meetings shall also be convened on the written requisition of any two or more members of the Company deposited at the principal office of the Company in Hong Kong specifying the objects of the meeting and signed by the requisitionists, provided that such requisitionists held as at the date of deposit of the requisition not less than one-tenth of the paid up capital of the Company which carries the right of voting at general meetings of the Company.

CONSTITUTIONAL DOCUMENTS

For the year ended December 31, 2016, there was no change in or amendment to the Company's constitutional documents.

1. Materiality Analysis of Environmental, Social and Governance Issues

Since its inception, China Shengmu Organic Milk Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") have always adhered to the principle of "green industry creates value, contributes to society and benefits the nation and its people". It is committed to optimising the environmental and social impact as an enterprise, and achieving comprehensive, coordinated and sustainable development of society. By benchmarking against the "Environmental, Social and Governance Reporting Guide" released by the Stock Exchange, combined with its business model and internal/external communication, the Group has identified material environmental, social and governance issues that are based on two dimensions, influence on stakeholders and influence on strategic operations.

The Group generates revenue and conducts business in the PRC, hence the Environmental, Social and Governance Report contains information and data of the Group that originates in the PRC.

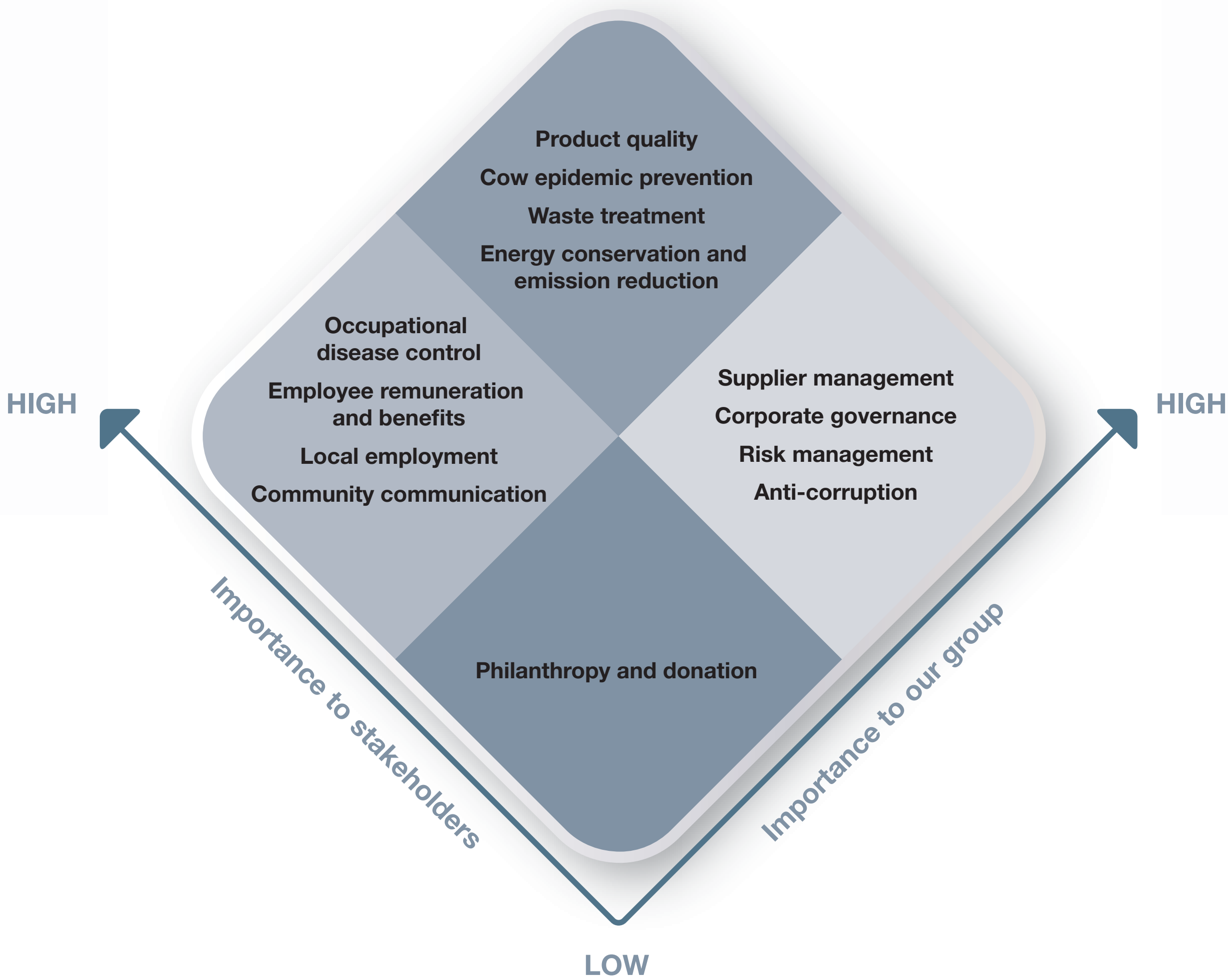

Figure: Material Issues Matrix of China Shengmu Organic Milk Limited

2. Establishment of an Organic Dairy Chain

The Group adheres to develop the vertically integrated production chain covering planting and farming through laying out an organic environment, monitoring the growing of organic forage, establishing self-owned dairy farms, implementing organic dairy farming and producing organic liquid milk products. China Shengmu has turned the Ulan Buh Desert into the largest dairy farming base in the Inner Mongolia Autonomous Region – the world's first circular organic industry chain in a desert area. The Group adheres to the combination model of planting and farming, being "to plant forage with farming and to breed cows with forage". On one hand, the dairy cow dung in the organic farm can be used as fertilizer to form an organic ecological circle. On the other hand, the strong and long-time sunshine in the desert helps forage grow and enables dairy cows to transform plant protein to animal protein so as to increase the calcium content in the milk to further improve the quality of milk.

An Organic Environment Rooted in a Pure Pollution-Free Hinterland

The Group has its production base located in the Ulan Buh Desert, Inner Mongolia. Being the eighth largest desert in the PRC, neither industrial nor chemical pollution has contaminated this region as there are no industrial parks within hundreds of kilometres. A natural virus isolation zone is formed by hot sands under direct sunlight, which provides an excellent environment for grass planting given the virtual absence of pollution, bacteria, viruses and pests.

Organic Planting to Build an Oasis in the Desert

Our strategic partner, Shengmu Forage, has nearly 200,000 mu of organic grassland in the hinterland of Ulan Buh Desert, where forage grass for dairy cows, such as alfalfa and maize, are planted. In the organic grassland, no chemical fertilisers or pesticides are used, and organic manure enhances soil fertility, thus a sustainable supply of high-quality coarse fodder is provided to the Group.

Organic Breeding to Enhance National Animal Husbandry Industry

The Group has cultivated 23 organic dairy farms in the hinterland of the deserts accommodating a total of nearly 95,000 organic dairy cows. Most farms have 3,500 to 4,500 dairy cows with an average of 60 to 80 square meters per cow. Favorable welfare benefits are provided to dairy cows, namely specialized nutritionists, a sophisticated healthcare system and an exclusive environmental system.

Organic Production process to Produce Trustworthy Milk Products

All of the Group's raw milk for its liquid milk products are supplied by its exclusive organic dairy farms. With the most advanced A3 production equipment imported from Swedish Tetra Pak, our organic milk is produced in strict accordance with the PRC organic standards (GB/T19630-2011) and the E.U. organic standards. No preservatives, artificial colorants or artificial flavors are used in the production process.

Traceability of Organic Milk to Let Consumers Enjoy Our Milk Safely

All of Shengmu's organic milk products are marked with an organic barcode certified by the Certification and Accreditation Administration of China. Thus, each carton is traceable to the source of production. At the website of Chinese Food and Agricultural Product Certification System (http://food.cnca.cn), customers can find information such as the name of the organic product, certification number, certified enterprise, etc., by inputting the organic barcode from each carton.

3. Sustainable Operation

The Group upholds the concept of sustainable operation and cultivates ecological dairy farms. It promotes the sustainable development of the industry chain for dairy products by pursuing cyclical development – from forage grass planting and dairy cow breeding to liquid milk production.

As at December 31, 2016, the Company was the largest organic dairy company in the PRC in terms of the annual number of organic dairy cows and organic raw milk output. It is the only vertically integrated grass-to-glass organic dairy company in the PRC that meets the E.U. organic standards and the only sizeable dairy company in the PRC to operate the "desert-based grass-to-glass organic production model" . In 2016, our Group was awarded the "2016 Public Thumb Award" by China Children and Women Industry Expo, the "Technical Progress Second Prize", the 2016 "Excellent New Product Award" by the China Dairy Industry Association and Gold Medal jointly by the China Green Food Development Center and the NürnbergMesse Group for the fifth time.

As at the end of 2016, the Company owned 23 organic dairy farms with nearly 95,000 organic dairy cows, producing about 1,200 tons of organic milk daily. It also operated 12 non-organic dairy farms with nearly 35,000 high-yield non-organic dairy cows, producing about 500 tons of non-organic milk daily.

Sustainable Breeding of Dairy Cows for High Quality Milk

With continuing improvement of quality control systems and strict implementation of quality control regulations, the Group ensures the high quality of each drop of milk. With regard to the quality management of organic milk, the Group has established strict organic management regulations, covering the environment, planting, breeding, production and other aspects. Every single production link in the whole dairy industry chain meets the organic quality standards and guarantees the high quality and safety of organic liquid milk products. With regard to non-organic milk management, the Company feeds the non-organic dairy cows with the same kind of forage and fine fodder for organic dairy cows purchased from third-party suppliers and ensures the quality of non-organic products by using the same high-standard equipment and management procedures as organic products.

During the reporting year, the Company has complied with all relevant laws and regulations that have a significant impact on the Company relating to health and safety, advertising, other matters relating to product responsibility.

Quality Control for Fodder

Premium fodder is the first step in producing high-quality milk. In order to ensure fodder safety and nutritional balance for each dairy cow, the Company strictly controls fodder quality. The Company has imposed very stringent inspections on incoming fodder, and has planted forage grass in the Ulan Buh Desert to maintain high quality from the source.

- *Inspection and Warehouse Management for Outsourcing Fodder*

  The Group requires outsourcing fodder must be strictly inspected. Sample fodder is numbered and then sent to a laboratory for physical and chemical testing. No fodder is allowed to enter our dairy farms until it passes proper testing. Even fodder has been sent to the warehouse, it still needs to pass random checks to prevent fraud. For fodder management, one material in two warehouses and first-in first-out mechanisms are implemented to ensure that fodder and forage are renewed timely and are not mildewed.

- *Organic Forage Grass Planting*

  The Group has chosen to plant forage grass in the Ulan Buh Desert where there is no chemical industry. The unique weather conditions of the desert form a favorable environment for cultivating forage grass given the virtual absence of pollution, bacteria, viruses and pests. In this manner the quality of organic forage grass is controlled from the source.

  Following the philosophy that "all staff participate in the organic management", Shengmu Forage has entered into the Organic Management Agreement with its staff to divide responsible areas of organic management and carry out non-scheduled internal checks so as to ensure the precise and effective implementation of the organic management. In order to achieve its precise and refined management objectives, Shengmu Forage sowed seeds in its sprinkler irrigation fields with comprehensive adoption of a GPS system, thereby enhancing its precise sowing standard in its drip irrigation fields, and installed scribers to enhance planting uniformity and adopt rational close planting, while continuing to use green organic cow dung to thicken the humus layer of soil, so as to improve the fertility of original organic planting fields to make them more suitable for the growth of natural plants, which ensured the improvement of production volume and quality of forage planting.

- *Formulation for Dairy Fodder*

  The Group has introduced an internationally advanced fodder management system and equipment with independent research and development of scientific fodder formulation and management to ensure the healthy development of each dairy cow.

  Relying on the total mixed ration (TMR) technology, and conditional information on targeted cows, such as production phase, milk yield, milk fat content, protein, foetal age, parity, body weight, body fat, climate etc., together with the TMR watch system (TMRWATH), and the employment of NDR near infrared spectrum instruments, the Group has realised refined and preuse feeding by reasonably matching its self-developed fodder formulae. Errors in fodder mixing and feeding have been minimised within 3%.

Creating a Safe and Comfortable Environment

The Group pays attention to the health and comfort of its cows and strives to create a safe and comfortable environment for them. In accordance with the principle of "prevention firsts and prevention is superior to treatment", the Group has established a feasible bio-security system. *China Shengmu Epidemic Prevention for Herds & Occupational Disease Prevention and Management System* was established to regulate procedures including disinfection, vaccination, quarantine and harmless disposal of cows that have died from diseases.

Table: Requirements of epidemic prevention for herds & occupational disease prevention and management procedures in the Company

Disinfection	Daily disinfection for dairy cottages, barns, maternity wards and farm roads
Vaccination	Foot and mouth disease vaccine: regularly vaccination three times a year
	Brucellosis vaccine (A19): first vaccination for 6-month old cows and additional vaccination for 12-month old cows on the 15th of each month
	IBR vaccine and BVDV vaccine: vaccination in April and October each year
Quarantine	Quarantine covers brucellosis disease and tuberculosis twice a year (in May and November) for the diseases: culling and harmless disposal of all positive cows
Harmless disposal	An agreement signed with a local harmless disposal company in Bayannur for treatment of cows that have died from disease
	An agreement signed with a local disposal company in Hohhot for in-time leave and standardised disposal of cows that have died from disease

The Company carries out humanized breeding for dairy cows. Each cow is provided with living space of 60 to 80 square meters. In summer, fans and water curtains are installed in barns for cooling and dry yellow sands are used as beds, which are cleaned and replaced twice a day. In winter, pad insulation of more than 10 cm thick is provided for calves, which are also fed in small groups to meet their social needs. A variety of living conditions are provided to improve the living comfort of dairy cows.

The Company continues to increase the investment of organic dairy farms to build comfortable garden-like organic dairy farms, so as to further improve the herd growing environment and staff working environment and the whole environment of the dairy farms, striking to further turn the current high standard advanced dairy farms into the world-class most beautiful dairy farms where the best living welfare is provided to the organic dairy cows in the desert, turning them into "happy cows and healthy cows".

Production of High-quality Milk

In the Group, the entire process is controllable from the source of milking to the production of milk products, which ensures there are no loopholes in the production process. As such, the quality of the milk products are strictly controlled and the milk products are of premium quality.

Scientific milking: With the high-efficiency rotary milking equipment introduced from GEA Group and high-end configuration facilitating scientific milking, such as DAIRY PLAN milking management software and IQ cup groups, the milking data and information of each cow is under information regulation and control. Based on the milk yield of each dairy cow, differentiation management is carried out for cows to the extent that each cow's milking time is controlled within 4 minutes. All milking equipment is provided with high-end quick cooling systems to ensure that milk is cooled to below 4℃ as soon as possible. After milking, an automatic CIP system is used to clean the milking equipment with acid and alkali solutions for sanitary purposes. Milk containers in warehouses and milk tanks in vehicles made of food-grade stainless steel conforming to national standards are used for storage and transportation. It takes less than two hours from milking to processing.

Additives-free milk: All raw milk for the Group's production of liquid milk products is supplied by exclusive organic dairy farms. No preservatives, artificial colorants or artificial flavors are used in the whole production process. A database covering organic fields, organic cows, organic liquid milk, internal inspectors and other information and management systems have been established for real-time tracing, monitoring and verification in the whole dairy industry chain. This ensures that every link in the "desert-based grass-to-glass organic production model" conforms to the organic standards and that the our organic products are in good quality, safe, reliable and worthy of the name.

Expansion of Sales Channels and Improvement of Customer Service

With diversified dairy products and increasing competition in the PRC, the Group has pioneered organic liquid milk products in the PRC. With effective market promotion, it is recognised and praised by the mass consumers. In order to introduce more consumers to organic milk, the Group has actively broadened its sales channels, enhanced the quality of customer service, and established a good market reputation.

Expansion of Sales Channels

With the Group's increasing market coverage, its liquid milk products are currently available in more than 400 domestic cities and even in Tibet, Xinjiang, Hainan and other border areas. Based on its current sales network covering first and second tier cities and major third and fourth tier cities, the Group continued to expand its market network to third and fourth tier cities. In order to stay close to the consumers, the Group adheres to the "blue ocean" strategy. Since the large chain-community stores were first built in 2015, Shengmu's products in the PRC have become available in a total of more than 100,000 reputable large chain-community store. At the same time, we also work with large-scale e-commerce platforms to actively promote online sales, achieving simultaneous online and offline development.

Improvement of Customer Service

Customer trust is the driving force for the Group. We have always focused on improving our customer service system and providing a good purchasing experience by carrying out satisfaction surveys and trying to understand customers' needs, developing the *Management System for Terminal Market Complaints* and running a 400-hotline for customer complaints, suggestions and other information. We also organize field visits to allow customers to experience the quality assurance of our organic milk. In addition, more people are introduced to our organic milk at free tastings in our stores.

Regulation of Supply Chain Management and Promotion of Suppliers' Development

The Group is committed to establishing a stable cooperative relationship with suppliers. With its own technical advantages and industry experience, it also works to help suppliers to enhance technology and capacity to obtain organic certification through cooperation. By doing so, the Group promotes the sustainable development of the organic milk industry chain.

Procurement Management

The Group has formulated the *Supplier Management Procedure* for effective and standardised management of newly developed suppliers and qualified suppliers. In selection of suppliers, the Group requires the suppliers to provide three certificates and their business license, production license, quality management system certification, environmental management system certification, fire acceptance certificate, G.B. and E.U. organic standard certificates and other qualifications. Requirements for compliance, anti-corruption, environment and safety are also included in the procurement standards. Suppliers who have been approved and have started supplying the Group are assessed every three months. The supplier's qualifications, quality level, price concessions, delivery capacity and cooperation services are rated and a preliminary assessment of the supplier is then issued. Suppliers are required to make improvements if there is any insufficiency. For suppliers who are recognized as A-level suppliers in the quarterly assessment, there will be discretionary increase in purchase volume and they will receive purchase priority under the same condition.

Supplier Development

As a leading organic milk supplier in the PRC, the Group has accumulated extensive experience in terms of forage grass planting, use of organic fertilisers and organic dairy breeding. The Group has shared and exchanged the concept of organic management with suppliers, provided professional training, and assisted them to achieve organic certification.

4. Concerned about Impacts on the Environment

The Group is fully aware of the complementary relationship between production operations and environmental protection. In the pursuit of development, it is concerned about the impacts on the environment imposed by production and operations, it also actively protects and improves the natural environment.

During the reporting year, the Group has complied with all relevant environmental laws and regulations that have a significant impact on the Croup.

Ulan Buh Desert Transformation: "A Cup of Organic Milk, a Piece of Green Desert"

Ulan Buh Desert is the eighth largest desert in the PRC formed by repeated diversion of the Yellow River. There is a fertile riverbed under the desert and the Yellow River also provides adequate water resources. However, soil erosion has led to land desertification in this area. Water and wind erosion degrades land and reduces production fertility, which seriously affects human life and living.

With its foothold in the Ulan Buh Desert, the Group works together with Shengmu Forage to build organic grasslands and change the desert. The Group is following Mr. Qian Xuesen's theory of "sand-to-grass industry" to turn barren land into an oasis to grow economic crops through transformation of the desert environment. In addition to economic benefits, this achieves sustainable green development. Shengmu Forage and the Group have successfully transformed the hinterland of Ulan Buh Desert covering an area of nearly 200,000 mu with tens of millions of sand fixation trees planted, changing a barren desert into a fertile oasis, contributing to desert control in the PRC. Sandstorms affecting surrounding urban residents have been greatly reduced. As to vegetation selection, the combination of xerophytic trees, sandy shrubs, perennial grasses and annual grasses fully utilize the advantages of wind prevention and sand fixation provided by herbaceous plants. At the same time, dwarf shrub grasslands combined with perennial grasses have been cultivated to eliminate the source of large sandstorms. In order to block sand blown by the wind, a sheltesbelt mainly composed of holly, red willow, caragana, haloxylon, hedysarum scoparium and other low sand shrubs has been established around the newly developed land. Xinjiang poplar, populous, elaeagnus, elm, locust and other fast-growing trees have been planted for auxiliary purposes. These measures not only prevent further desertification of the land, but also protect the artificial grasslands and form a three-dimensional ecosystem involving trees, shrubs and grasses in the desert.

Figure: Comparison of the desert before and after the transformation

Under difficult natural conditions, our Group's desertification control measures have made remarkable progress. Till now, tens of millions of trees have been planted and more than 200,000 mu of grassland has been opened up, significantly increasing the green area in the hinterland of Ulan Buh Desert. Furthermore, local annual precipitation has increased, urban air quality has improved significantly, and remarkable achievements have been made in desert control. The Group's organic sand-grass planting model has created a number of desert oases and contributed to the harmonious coexistence of man and nature.

Figure: Transformed dairy farm in the desert

Reducing Discharge of Pollutants

The Company implements pollutants emission control to minimise the adverse impacts of pollutants in production processes to meet ecofriendly requirements. Appropriate measures are taken to reduce emissions and pollution.

Fecal Harmless Treatment

The Group is aware that the cow manure is both a pollutant and a valuable resource. The Standard for Returning Solid and Liquid Fertilizer to the Farmland is formulated based on the national standard, management measures and assessment mechanisms for cow manure are implemented to monitor the fecal harmless treatment so as to promote an ecological benign cycle. Economic benefits are maximized while ecofriendly requirements are met.

The Group's equipment and facilities for the treatment of faeces and sewage mainly include solid-liquid separators, solid-liquid separation tanks, manure storage tanks, sedimentation tanks and oxidation ponds. The dairy farms adopt the unmanned automatic scraper manure cleaning system for automated manure cleaning, and the manure produced by dairy cows is stored in the storage tanks in our dairy farms and then sent to solid-liquid separators for treatment. The treated part of the solid fertilizer is further ripened and then treated as a fertilizer, which is applied to the planting ground according to plan. The treated liquid fertilizer is processed and fermented in the fermentation tank, and it becomes liquid fertilizer after reaching the standard and is stored in the fertilizer storage tanks, which will be extracted and introduced to the planting ground by irrigation machines as per the plan and the proportion. The wastewater produced by the milking hall is discharged into a Level-III sedimentation tank, and the supernatant water in the third sedimentation tank after Level-III sedimentation is supplied to the milking hall for washing. The remaining water will pass into the oxidation pond through a pipeline and be used for surrounding silage irrigation after aerobic processing, flocculation sedimentation and disinfection.

The treated solid fecal waste from non-organic dairy farms is supplied to local fodder suppliers. The treated solid fecal waste from organic dairy farms is cleaned and collected by Shengmu Forage, and then stored in organic fertilizer processing plants in the vicinity of the dairy farms, for use after composting as an organic fertilizer. This treatment of fecal waste provides premium and cheap organic fertilizer, realizes the reuse of biological resources and increases silage production, in order to achieve a win-win balance between faecal matter treatment and fertiliser collection. At the same time, organic cow manure is very beneficial to organic improvement of sandy soil, and plays a very important role in the transformation of desert farmland.

The cow manure reduction facilities include 9 organic manure fields, 7 new loose manure temporary pools, 40 oxidation ponds and 17 solid-liquid separation facilities. The cow manure reduction facilities in non-organic husbandry are similar to their organic counterparts.

Exhaust Gas Treatment

The Group regulates boiler exhaust gas and controls the emission of gas pollutants in accordance with regulatory standards. In 2016, the Group transformed the previous single-base wet-type desulphurisation dust remover into a double-base wet-type desulphurisation dust remover with handling capacity of 90,000 m^3/h. A 45-meter chimney was also added. Emission indicators show the Group is on top of the national environmental protection standards.

Wastewater Treatment

The Group has built a 3,000-ton wastewater plant which was put into operation in September 2013. The Group's dairy production wastewater meets Standard B specified in the *Standards for Sewage Discharged into Urban Sewers* (CJ343-2010) after being treated by the wastewater plant, and is then discharged into a sewage treatment plant in Dengkou County. The sludge is delivered to the landfill in the Dengkou County by the Environmental Protection Bureau for centralized waste treatment.

Compliance with relevant laws and regulations

The Group strictly complies with relevant national environmental laws and regulations in the course of its operations, including the Regulations on the Prevention and Control of Pollution Caused by Large-scale Breeding of Livestock and Poultry (《畜禽規模養殖污染防治條例》), the Environmental Protection Law of the PRC (《中華人民共和國環境保護法》) and the Law of the PRC on Prevention and Control of Water Pollution (《中華人民共和國水污染防治法》). The Group has adopted different measures to reduce its discharge of pollutants and enhance the utilisation of resources. The measures are implemented and reviewed on an ongoing basis.

Enhancing Utilisation of Resources

To better control energy indexes and improve resource utilisation, the Company has developed the Energy Management System based on the production process and actual energy consumption for production to establish and improve the energy management system.

Energy Conservation

The Group has developed a comprehensive energy control plan to develop energy consumption targets for its departments, and manage and urge them to implement energy conservation initiatives. The implementation is tracked monthly for the purpose of effective monitoring and control of energy utilization and management.

Table: Achievements made with energy conservation measures in 2016

Measures	Achievements
Solar energy utilization project	Through the combination of prominent local solar energy resources and new energy sources such as air energy, energy consumption is reduced. Annual electricity consumption reduced by 3 million kwh.
Air energy technology	Air energy technology has been gradually put into the production, for example, the current solar plus air energy for water heating saves about 90% of energy compared with the previous electricity heating.
Application of traction chaff cutters	Fuel consumption savings of about 4 L/ton, annual total savings of about 200,000L and cost decrease about RMB1 million.

Conservation of Water Resources

Water consumption in the production process mainly comes from milking hall. The Company has developed the *Management System for Milking Hall Water Consumption* to regulate inspections and assessment methods. It has also implemented fixed-amount water consumption and fixed-amount discharges as well as a variety of water-conserving measures.

Table: Achievements made with water-conserving measures in 2016

Measures	Achievements
Water circulation	The dairy company set up a whole-plant circulating water station with two 100-ton cooling water tanks, four 200-ton closed cooling towers, two 100-ton chilled water tanks, and four 120-ton chilled water units for recycling and reuse of cooling water and chilled water to improve the concentration of recycled water and reduce the amount of water discharge and water supplementation.
Water recycling	Equipment washing water, clear water, concentrated acid, and concentrated alkaline water are directly recycled by the cleaning station to reduce fresh water consumption.
Reuse of wastewater	Part of the treated production wastewater is used for greening and road cleaning to improve the water recycling rate.
Water-conservation management	Water meters are mounted to water systems for elimination of water leakages during use. Water consumption targets are provided for production areas and incentive measures are implemented to raise employee awareness of water conservation in production areas.
Water-conserving approach in milking operation	Based on the position of the turntable, wash the turntable milking system timely and intermittently to reduce long-stream washing, saving about 20 tons/day.

5. Caring for Our Employees' Development

The Group strictly follows the Labour Law, Labour Contract Law, Law on the Protection of Rights and Interests of Women and relevant laws and regulations, to eliminate child and forced labour in any form. It adheres to an open, fair, and equal employment policy to realise equal pay for equal work as well as gender equality.

The Company believes that employees are valuable assets of the Group and thus are key to its development. Through a series of policies, the Group provides employees with fair and competitive job opportunities, a comprehensive training system and a diverse career promotion platform, creating an atmosphere of humanistic care with an eye to employees' health and safety.

Strengthening Recruitment Management

The Company strictly regulates the recruitment of new employees, and has formulated the *Rules on Recruitment Management.* It adheres to the principles of fair competition, merit-based selection, unified management and combining internal selection with external recruitment. It also forbids all departments from individual recruitment or employing relatives to work directly in units or departments under their own leadership.

The Group has attached great importance to in-depth collaboration with colleges and universities since the very beginning of its founding. So far the Group has established partnerships with nine colleges and universities. In addition, the Group has provided many internships in various fields for college students, while sending the Group's employees back to the universities and colleges they graduated from to attract more talents for the Group. From 2014 to 2016, campus recruitment has increased year by year, promoting employment of local graduates, as well as stable and sustainable development of the Group.

The Group releases weekly recruitment newsletter and uses mobile platforms such as WeChat to release recruitment information. Furthermore, the Group interviews non-local applicants on mobile terminals at their convenience. The Group has also set up a *Talent Scout Award* to incentivize people recommend candidates for hard-to-staff positions. A series of measures have been taken to attract talents to facilitate the growth of the Group.

Comprehensive Training System

Career training is an important approach to enhancing employees' abilities. The Group carries out a post-based general training system to ensure every employee receives high-quality training through its comprehensive training guarantee system. The Group makes and carries out its annual training plan, and has developed various training channels including sharing sessions, study tours and open lectures, forming a phased training system that takes a step-by-step approach from orientation and pre-job training to on-the-job training with an internal part-time lecturer system and a "mentoring" system in place, together with actively introducing external resources such as technical support from suppliers and technical services from professional agencies, to fulfil employees' special training needs.

In 2016, the Group increased its investment in employee training by providing a series of systematic, multilevel, and comprehensive training courses targeting different business needs and work responsibilities.

Case Study: Overseas Training

The Group sends production engineers and outstanding employees overseas to study advanced production processes and obtain breeding experience every year. Senior management and personnel in key positions also participate in overseas exchange program to have a better understanding of the current status of the industry and development trend, observe advanced international management experience and techniques, widen their horizons and improve their skills and management abilities.

Case Study: The Group Held Anti-corruption-themed Activity Series

The Group attaches great importance to anti-corruption, and actively holds anti-corruption law education activities to strengthen the awareness on integrity, self-discipline and legal concepts among the Group's party leaders, and require them to strictly follow all regulations and laws. The Group has set up special mailboxes and telephone hotlines to file internal complaints on fraud, illegal activities and corrupt practices. The Group has also established a punishment and prevention system, emphasizing on education, policies and supervision, to ensure the healthy development of the Group.

In 2016, the Group held a series of activities with an anti-corrpution theme for personnel on key positions and managers, which included watching the film *Late Autumn*, anti-corruption lectures by the local Crime Prevention Department of Procuratorate, and visits to the Hohhot No.1 Prison's law education base.

Promoting Career Growth

The Group provides both career growth pathways and awards for talented employees. The career growth pathways include the management pathway and tech pathway, in which management personnel are promoted through open competition, while the occupational ranks and salary scale of tech personnel in charge of equipment and laboratory, etc., would be determined according to their theoretical knowledge and practical skills. The above pathways plus three promotion incentive mechanisms, a talent reward mechanism and talent honours constitute the Group's incentive system for honouring and promoting outstanding talents.

Table: The Group's Talent Incentive Mechanism

	Dairy Companies	Husbandry Companies
Promotion Incentive Mechanism	Each manager trains a deputy as a reserve, establishing a talent echelon.	Formulates layers of posts for professionals, and promotes on the basis of one's professionalism.
Talent Reward Mechanism	Mainly includes: certificate holders in key process posts, multi-tasker award, mentor award, and part-time lecturer award.	For the promoted professionals, incentives are given to their immediate superiors.
Talent Honours	In 2016, a total of 84 people were honoured with RMB70,900 prizes, including the General Manager's Special Award, Outstanding Manager Award (for department heads, managers and squad leaders), Outstanding Employee Award, Guardian of Quality Award, Innovative Star, Sales Star, Outstanding Operational Team Award, and Best Partnership Award.	There are two reward mechanisms with RMB500 for outstanding employees and RMB5,000-10,000 for bench-marking pastures given through payrolls respectively.

Ensuring Employee Health and Safety

Ensuring employee physical and mental health and work safety is one of the important components of the Group's Caring for Our Employees' Development concept, as well as creating a favorable working atmosphere. In 2016, the Group strengthened its care for employees' health by taking measures to reduce and prevent occupational diseases.

The Group's care for employees' health and safety mainly concerns the employee health management system that includes a health check for new employees, training for production safety and occupational health management, and medical stations for employees. The Group has also formulated relatively complete measures for both prevention and treatment of occupational diseases and creating a safe working environment by drawing up regulations for employee safety and protection that includes mandatory work clothes at the husbandry production areas, regular sanitation checks in working and breeding areas, timely cleaning and regular disinfection of cowsheds, additional inspections of production segments by managers every day, and careful handling of work-related injury incidents according to related laws and regulations. Other than that, the Group carries out strict registration and disinfection protocols for outsiders entering into pastures, and forbids any such contact during the disease prevention period from every November to March to ensure the production safety.

Figure: Signing the Safety Responsibility Agreement

Figure: Occupational Health and Safety Training

Figure: Fire Drills

Figure: Safety Knowledge Contest

Focus on Humanisic Care

Creating a work atmosphere with humanistic care for employees is one of the objectives that the Group has long lived out. The Group arranged appropriate working hours for all employees and ensured their right on leaves and vacations according to related regulation. The Group has not only implemented tailor-made measures for different employee groups, but also prioritized employees' work-life balance by holding speech, cooking, karaoke and chess contests as well as other art and sports activities to enrich their spare time.

The Group tailor-makes care services for different employee groups respectively. For instance, the Group pays great attention to caring for female employees. Apart from formulating specific rules on maternity leave, pregnancy examination leave and paternity leave, the Group gives holiday benefits to female employees on Women's Day, organises various forms of special training for female employees, operates Mommy Houses, provides fruit for pregnant female employees in office areas, and extends the breast feeding period for breast-feeding female employees.

The Group also cares for employees in need. The management team organises special taskforces to convey greetings to these employees during holidays, as well as to further understand their specific needs. As a result, the team works with local labor unions to apply for compensation and student financial aid for these employees, and does its best to solve their immediate problems. Also, the Group calls appeals other employees to donate to employees that suffering from serious family misfortunes.

6. Caring for Our Community

Besides creating economic benefits and improving the environment, the Group also actively contributes to society by strongly supporting social welfare activities, benefiting the public with organic milk, and organising and participating in social welfare activities to help those in need. In 2016, the Group donated milk with a total amount of RMB56.23 million to communities and the military, thus sending its best regards for their health.

Organic Milk in an Open Pasture

To promote the organic concept and promote the industrial green and ecofriendly philosophy and further help people understand the green, organic and sustainable production model, the Group has held a two-month special mega-event "Shengmu Desert Organic Journey" every summer since 2012. It receives customers from across the country to visit the Uulan Buh Desert Manufacturing Base to experience the whole production process of the organic milk production chain. By the end of 2016, a total of 5,900 people have been received.

The "Shengmu Desert Organic Journey" includes various contents such as a tour of the Uulan Buh Desert scenic area, a welcome banquet, a tour of the production chain and a campfire party. The Group provides considerate and detailed arrangement for visitors, such as narration, accommodations and performances. Visitors to the Group's organic grass base, organic dairy farms and organic factories not only experience the beauty of the prairie and the desert, but also further understand the Group's ecological development path of feeding the desert, with social benefits coming first and economic benefits second.

Figure: Shengmu Organic Grass Base

Figure: Shengmu Grass Irrigation Equipment

Figure: Shengmu Dairy Cows in the Desert

Figure: The “Shengmu Desert Organic Journey” Activity

Figure: The “Shengmu Desert Organic Journey” Activity

Figure: The “Shengmu Desert Organic Journey” Activity

Every Drop of Organic Milk for the Benefit of the People

As part of living up to its corporate social responsibility, the Group organizes visit lonely elders in seniors’ centres and the mentally and physically disabled. In addition, we donate to the Hope Primary School and primary schools of peasant workers’ children, encourage cleaner teams as well as to charities and social welfare activities to contribute to society. We also benefit the public by actively carrying out social welfare activities and creating economic benefits at the same time.

- *Organic Milk for Poor Villages to Improve Community Health*

  On November 7, 2016, the Group donated 15,500 boxes of organic milk to the local villagers of three poor villages in Handan City – Qianyang Village of Xifuji Township in Daming County, Jingke Village of Feixiang County and Qiandamo Village of Wei County

- *Organic Milk for Public Interest Agencies and Charities*

  On November 8, 2016, the Group donated 8,000 boxes of organic milk to the Shijiazhuang Charity Federation and the Bureau of Civil Affairs of Chang’An District. On November 25, Shengmu donated organic milk with net worth of RMB120,000 to Qingyuan Love Union and Qingyuan Love Association, which participated in the four-day, five-night rescue of a five-year-old boy who had fallen into a well on the morning of November 6

- *Organic Milk to the Angels on the Road – Sanitation Workers*

  On November 8, 2016, the Group donated 6,000 boxes of organic milk to more than 3,000 sanitation workers of Xingtai City Management Bureau's Sanitation Office

- *Organic Milk for Lonely Seniors*

  On November 26, 2016, the Group donated organic milk with net worth of RMB150,000 to lonely seniors and people with financial difficulties at Xingtai Zhongdajie Office

  This "Shengmu Desert Organic Journey" has won support from all sectors of society, especially receiving assistance from local dealers and other related corporations and enterprises. Not only did the tour allow the people in Hebei Province to get to know about Shengmu and its social welfare program, but also let the beneficiaries get a touch of warmth from the Group.

Volunteer Work: A Win-win Situation for Both Communities and the Group

Besides organising various public welfare activities, public-spirited employees in the Group have established a youth volunteer team providing voluntary services to various public activities. The volunteers from the Group not only demonstrate a high level of professionalism on their positions during work, but also influence colleagues around them with their voluntary work. They contribute time and effort to local communities and people in need to help them and pass on their love with their voluntary work.

- *Providing Services for Contestants*

  On October 16, 2016, volunteers from the Group gathered together in the Uulan Buh Desert to provide voluntary services for the national fishing competition "Yunado" Cup. They distributed supplies to contestants and maintained order in the competition

- *Donating Blood*

  On November 9, 2016, the employees of the Group responded enthusiastically to the Group's voluntary blood donation drive, with 25 of them donating blood

- *Helping Poor Children*

  On November 25, 2016, volunteers from the Group participated in the public activity "Connecting Our Hands and Hearts Together for Happy Growth", which aims to care for left-behind children in Xihuan Community of Ba Town. They gave padded coats, milk, backpacks and corn with net worth of RMB6,500 to these poor children for a warmer winter and happier growth

Response to the Call for "Double supports"

In response to the General secretary's call for double support, the Group, together with many corporations and civil organizations and agencies including religious groups, spontaneously organised a large team to support the military, which has extended their best regards to hundreds of troops across the country from the navy, army and air force by sending the best of China Shengmu's gross-to-glass organic liquid milk products to these soldiers protecting our country. Such good deeds have aroused strong social sympathies and created a new wave of social organizations to express patriotism spontaneously.

INDEPENDENT AUDITOR'S REPORT

EY 安永

To the shareholders of China Shengmu Organic Milk Limited
(Incorporated in the Cayman Islands as an exempted company with limited liability)

Opinion

We have audited the consolidated financial statements of China Shengmu Organic Milk Limited (the "**Company**") and its subsidiaries (the"**Group**") set out on pages 82 to 157, which comprise the consolidated statement of financial position as at December 31, 2016, and the consolidated statement of profit or loss and other comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at December 31, 2016, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("**IFRSs**") issued by the International Accounting Standards Board ("**IASB**") and have been properly prepared in compliance with the disclosure requirements of Hong Kong Companies Ordinance.

Basis for opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing ("**HKSAs**") issued by the Hong Kong Institute of Certified Public Accountants ("**HKICPA**"). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Group in accordance with the HKICPA's *Code of Ethics for Professional Accountants* (the "**Code**"), and we have fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Key audit matter	How our audit addressed the key audit matter
Valuation of dairy cows	
Biological assets of the Group, which represent dairy cows and are measured at fair value less cost to sell, amounted to RMB3,884,257,000 as of December 31, 2016. Dairy cows of the Group include milkable cows, heifers and calves, which are raised for the purpose of producing raw milk. The fair value of biological assets as assessed by management is hence significant to the Company's consolidated financial statements since (i) the carrying values of such biological assets accounted for approximately 37% of the total assets of the Group; and (ii) significant estimates were involved in management's fair value assessment. Management has engaged an external valuation expert to assist in the valuation of the biological assets as at December 31, 2016. The accounting policies and disclosures for biological assets are included in notes 2.4, 3 and 19 to the consolidated financial statements.	We assessed the objectivity, independence and competence of the external valuation expert employed by the Company and also evaluated the accuracy of the data provided by management to the external valuation expert, which are used as inputs for the valuation. We evaluated the management's underlying bases and assumptions. In particular, we assessed the assumptions applied to which the outcome of the valuation is most sensitive, including the estimated local market selling price of the relevant dairy cows, feed costs per kilogram of raw milk production, daily milk yield at each lactation cycle and local future market prices for raw milk.
Recoverability of trade receivables	
The Group has a significant trade receivable balance of RMB1,108,787,000 as at December 31, 2016. The aging profile of such receivables has deteriorated since December 31, 2015 and the determination of the recoverability and impairment allowance of these trade receivables involves significant judgement and estimation by management. Hence, the assessment of the recoverability and impairment allowance against the trade receivables is significant to the financial statements. The details of trade receivables and the related impairment allowance are disclosed in notes 2.4, 3 and 25 to the consolidated financial statements	Our audit procedures included: understanding and testing the Group's internal control process in the assessment and estimation of trade receivable impairment. We assessed the bases and assumptions adopted by management in estimating the impairment allowance. We evaluated the adequacy of impairment allowance made by management after taking into account the subsequent settlement from customers, aging profile, financial conditions of customers and their respective credit history.

Other information included in the Annual Report

The directors of the Company are responsible for the other information. The other information comprises the information included in the Annual Report, other than the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the directors for the consolidated financial statements

The directors of the Company are responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with IFRSs issued by the IASB and the disclosure requirements of the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the directors of the Company are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors of the Company either intend to liquidate the Group or to cease operations or have no realistic alternative but to do so.

The directors of the Company are assisted by the Audit Committee in discharging their responsibilities for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Our report is made solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with HKSAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.

- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Audit Committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Mr. TONG KA YAN, AUGUSTINE.

Ernst & Young
Certified Public Accountants

Hong Kong
March 20, 2017

CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

Year ended December 31, 2016

	Notes	2016	2015
		RMB'000	RMB'000
REVENUE	5	3,466,544	3,100,711
Cost of sales		(1,791,133)	(1,623,168)
Gross profit		1,675,411	1,477,543
Gain/(loss) arising from changes in fair value less costs to sell of biological assets	19	(15,729)	52,722
Other income and gains/(losses)	5	(87,146)	47,424
Selling and distribution expenses		(287,949)	(265,468)
Administrative expenses		(141,714)	(107,470)
Other expenses	7	(56,233)	—
Finance costs	8	(124,667)	(99,147)
Share of profits and losses of associates		(16,242)	(18,041)
Gain on disposal of a subsidiary		—	265
PROFIT BEFORE TAX	6	945,731	1,087,828
Income tax credit/(expense)	11	11,077	(4,606)
PROFIT FOR THE YEAR		956,808	1,083,222
OTHER COMPREHENSIVE INCOME			
Exchange differences on translation of foreign operations		12,158	1,893
Net other comprehensive income to be reclassified to profit or loss in subsequent periods		12,158	1,893
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		968,966	1,085,115
Profit attributable to:			
Owners of the parent		680,615	800,652
Non-controlling interests		276,193	282,570
		956,808	1,083,222
Total comprehensive income attributable to:			
Owners of the parent		692,773	802,545
Non-controlling interests		276,193	282,570
		968,966	1,085,115
EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT	13		
Basic		RMB0.107	RMB0.126
Diluted		RMB0.106	RMB0.124

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

December 31, 2016

	Notes	December 31, 2016	December 31, 2015
		RMB'000	RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment	14	2,710,368	2,093,230
Prepaid land lease payments	15	37,566	5,066
Other intangible assets	16	14,847	15,518
Investments in associates	17	112,658	32,055
Available-for-sale investments	18	1,427	1,404
Biological assets	19	3,884,257	3,285,436
Prepayments for property, plant and equipment and biological assets	21	11,963	15,690
Long term receivables	22	19,684	—
Deferred tax assets	20	24,634	1,076
Other non-current assets	23	16,565	—
Total non-current assets		6,833,969	5,449,475
CURRENT ASSETS			
Inventories	24	928,816	824,514
Trade and bills receivables	25	1,108,787	915,312
Prepayments, deposits and other receivables	21	393,550	468,456
Pledged deposits	26	66,791	70,277
Available-for-sale investments	18	120,000	—
Cash and bank balances	26	1,047,382	1,731,759
Total current assets		3,665,326	4,010,318
CURRENT LIABILITIES			
Trade and bills payables	27	920,631	1,018,126
Receipts in advance		13,152	17,320
Other payables and accruals	28	438,550	338,293
Interest-bearing bank and other borrowings	29	918,404	1,599,855
Income tax payable		1,581	1,974
Total current liabilities		2,292,318	2,975,568
NET CURRENT ASSETS		1,373,008	1,034,750
TOTAL ASSETS LESS CURRENT LIABILITIES		8,206,977	6,484,225

	Notes	December 31, 2016	December 31, 2015
		RMB'000	RMB'000
NON-CURRENT LIABILITIES			
Interest-bearing bank and other borrowings	29	1,751,950	1,117,000
Long term payables	30	107,900	—
Total non-current liabilities		1,859,850	1,117,000
Net assets		6,347,127	5,367,225
EQUITY			
Equity attributable to owners of the parent			
Share capital	31	50	50
Reserves	32	5,338,989	4,551,605
		5,339,039	4,551,655
Non-controlling interests		1,008,088	815,570
Total equity		6,347,127	5,367,225

YAO Tongshan
Director

CUI Ruicheng
Director

	Attributable to owners of the parent									
	Share capital RMB'000	Share premium account RMB'000	Contributed surplus RMB'000	Share option reserve RMB'000	Reserve funds RMB'000	Exchange fluctuation reserve RMB'000	Retained profits RMB'000	Total RMB'000	Non-controlling interests RMB'000	Total equity RMB'000
At January 1, 2015	50	1,757,767	373,656	23,396	186,771	2,779	1,377,479	3,721,898	533,201	4,255,099
Profit for the year	—	—	—	—	—	—	800,652	800,652	282,570	1,083,222
Other comprehensive income for the year:										
Exchange differences related to foreign operations	—	—	—	—	—	1,893	—	1,893	—	1,893
Total comprehensive income for the year	—	—	—	—	—	1,893	800,652	802,545	282,570	1,085,115
Equity-settled share option arrangements	—	—	—	27,011	—	—	—	27,011	—	27,011
Acquisition of non-controlling interests	—	—	201	—	—	—	—	201	(201)	—
Transfer from retained profits	—	—	—	—	116,605	—	(116,605)	—	—	—
At December 31, 2015	50	1,757,767#	373,857#	50,407#	303,376#	4,672#	2,061,526#	4,551,655	815,570	5,367,225
At January 1, 2016	50	1,757,767	373,857	50,407	303,376	4,672	2,061,526	4,551,655	815,570	5,367,225
Profit for the year	—	—	—	—	—	—	680,615	680,615	276,193	956,808
Other comprehensive income for the year:										
Exchange differences on translation of foreign operations	—	—	—	—	—	12,158	—	12,158	—	12,158
Total comprehensive income for the year	—	—	—	—	—	12,158	680,615	692,773	276,193	968,966
Equity-settled share option arrangements	—	—	—	45,151	—	—	—	45,151	—	45,151
Capital injection by non-controlling shareholders	—	—	—	—	—	—	—	—	12,205	12,205
Acquisition of non-controlling interests	—	—	49,460	—	—	—	—	49,460	(95,880)	(46,420)
Transfer from retained profits	—	—	—	—	109,361	—	(109,361)	—	—	—
At December 31, 2016	50	1,757,767#	423,317#	95,558 #	412,737#	16,830#	2,632,780#	5,339,039	1,008,088	6,347,127

These reserve accounts comprise the consolidated reserves of RMB5,338,989,000 (2015: RMB4,551,605,000) in the consolidated statement of financial position.

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended December 31, 2016

	Notes	2016	2015
		RMB'000	RMB'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit before tax		945,731	1,087,828
Adjustments for:			
Loss/(gain) arising from changes in fair value less costs to sell of biological assets	19	15,729	(52,722)
Interest income	5	(3,953)	(12,234)
Finance costs	8	124,667	99,147
Share of profits and losses of associates		16,242	18,041
Gain on disposal of a subsidiary		—	(265)
Depreciation	14	146,783	105,046
Amortisation of prepaid land lease payments	15	266	186
Amortisation of other intangible assets	16	1,434	1,454
Loss on disposal of items of property, plant and equipment	5	14,677	141
Equity-settled share option expenses	34	45,151	27,011
Foreign exchange differences, net		3,678	(543)
		1,310,405	1,273,090
Increase in inventories		(104,301)	(123,331)
Increase in trade and bills receivables		(193,475)	(517,769)
Decrease/(increase) in prepayments, deposits and other receivables		55,879	(267,846)
Decrease/(increase) in pledged deposits		3,486	(53,846)
Increase/(decrease) in trade and bills payables		(97,495)	594,162
Decrease in receipts in advance		(4,168)	(15,120)
Increase/(decrease) in other payables and accruals		(28,095)	38,916
Cash generated from operations		942,236	928,256
Interest received		12,864	5,368
Income taxes paid		(12,875)	(5,097)
Net cash flows from operating activities		942,225	928,527

	Notes	2016	2015
		RMB'000	RMB'000
Net cash flows from operating activities		942,225	928,527
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of items of property, plant and equipment		(598,218)	(506,525)
Additions to prepaid land lease payments	15	(33,911)	—
Additions to other intangible assets	16	(763)	(1,003)
Purchases of biological assets		(6,456)	(107,007)
Payments for breeding calves and heifers		(711,707)	(636,841)
Proceeds from disposal of biological assets		118,234	222,436
Proceeds from disposal of items of property, plant and equipment		6,256	269
Purchases of time deposits with original maturity of more than three months		(115,000)	(320,260)
Proceeds from disposal of time deposits with original maturity of more than three months		320,260	—
Acquisition of available-for-sale investments		(120,000)	(424)
Acquisition of associates		(92,663)	(21,670)
Net cash flows used in investing activities		(1,233,968)	(1,371,025)
CASH FLOWS FROM FINANCING ACTIVITIES			
Share issue expenses		—	(1,620)
Capital injection by non-controlling shareholders		12,205	—
Acquisition of non-controlling interests		(46,420)	(4,675)
New bank loans		1,039,189	1,587,948
Issuance of corporate bonds		600,000	1,000,000
Issuance of short-term notes		—	100,000
Corporate bonds issue expenses		(4,200)	(7,400)
Repayment of bank loans		(1,580,237)	(1,447,711)
Repayment of short-term notes		(100,000)	—
Interest paid		(112,035)	(107,791)
Net cash flows from/(used in) financing activities		(191,498)	1,118,751
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS		(483,241)	676,253
Cash and cash equivalents at beginning of year		1,411,499	734,703
Effect of foreign exchange rate changes, net		4,124	543
CASH AND CASH EQUIVALENTS AT END OF YEAR	26	932,382	1,411,499
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS			
Cash and bank balances	26	1,047,382	1,731,759
Time deposits with original maturity more than three months		(115,000)	(320,260)
CASH AND CASH EQUIVALENTS AT END OF YEAR	26	932,382	1,411,499

1. CORPORATE AND GROUP INFORMATION

The Company is an exempted company incorporated in the Cayman Islands with limited liability. The registered office address of the Company is P.O. Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands.

The Company is an investment holding company. During the year, the Company's subsidiaries were primarily engaged in the production and distribution of raw milk and dairy products in the People's Republic of China (the "**PRC**").

Information about subsidiaries

Particulars of the Company's principal subsidiaries are as follows:

Name	Place of incorporation/ registration and business	Registered share capital	Percentage of equity attributable to the Company		Principal activities
			Direct	Indirect	
內蒙古聖牧高科牧業有限公司 Inner Mongolia Shengmu High-tech Farming Co., Ltd.# (note (i))	PRC/ Mainland China	RMB 888,700,000	—	100	Production and distribution of raw milk
內蒙古圣牧控股有限公司 Inner Mongolia Shengmu Holding Co., Ltd.# (note (i))	PRC/ Mainland China	RMB 280,000,000	—	100	Production and distribution of raw milk
內蒙古聖牧高科奶業有限公司 Inner MongoliaShengmu High-tech Dairy Co., Ltd.#	PRC/ Mainland China	RMB 300,000,000	—	100	Production and distribution of dairy products
巴彥淖爾市聖牧盤古牧業有限責任公司 Bayannur Shengmu Pangu Farming Co., Ltd. ("**Shengmu Pangu**")#	PRC/ Mainland China	RMB 80,000,000	—	55	Production and distribution of raw milk

The English names of these companies represent the best effort made by management of the Company to directly translate their Chinese names as these companies did not register any official English names.

Note:

(i) The entity was registered as a foreign investment enterprise under PRC law.

The above table lists the subsidiaries of the Company which, in the opinion of the directors, principally affected the results for the year or formed a substantial portion of the net assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

2.1 BASIS OF PREPARATION

The financial statements have been prepared in accordance with International Financial Reporting Standards ("**IFRSs**") (which include all International Financial Report Standards, International Accounting standards ("**IASs**") and Interpretations) issued by the International Accounting Standards Board ("**IASB**"), and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for certain biological assets and agricultural produce which have been measured at fair value less costs to sell. These financial statements are presented in Renminbi ("**RMB**") and all values are rounded to the nearest thousand except when otherwise indicated.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended December 31, 2016. A subsidiary is an entity (including a structured entity), directly or indirectly, controlled by the Company. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee (i.e., existing rights that give the Group the current ability to direct the relevant activities of the investee).

When the Company has, directly or indirectly, less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

(a) the contractual arrangement with the other vote holders of the investee;

(b) rights arising from other contractual arrangements; and

(c) the Group's voting rights and potential voting rights.

The financial statements of the subsidiaries are prepared for the same reporting period as the Company, using consistent accounting policies. The results of subsidiaries are consolidated from the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases.

Profit or loss and each component of other comprehensive income are attributed to the owners of the parent of the Group and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

The Group reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control as defined in IFRS 10. A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction.

If the Group loses control over a subsidiary, it derecognises (i) the assets (including goodwill) and liabilities of the subsidiary, (ii) the carrying amount of any non-controlling interest and (iii) the cumulative translation differences recorded in equity; and recognises (i) the fair value of the consideration received, (ii) the fair value of any investment retained and (iii) any resulting surplus or deficit in profit or loss. The Group's share of components previously recognised in other comprehensive income is reclassified to profit or loss or retained profits, as appropriate, on the same basis as would be required if the Group had directly disposed of the related assets or liabilities.

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES

The Group has adopted the following new and revised IFRSs for the first time for the current year's financial statements.

Amendments to IFRS 10, IFRS 12 and IAS 28	*Investment Entities: Applying the Consolidation Exception*
Amendments to IFRS 11	*Accounting for Acquisitions of Interests in Joint Operations*
IFRS 14	*Regulatory Deferral Accounts*
Amendments to IAS 1	*Disclosure Initiative*
Amendments to IAS 16 and IAS 38	*Clarification of Acceptable Methods of Depreciation and Amortisation*
Amendments to IAS 27	*Equity Method in Separate Financial Statements*
Annual Improvements 2012-2014 Cycle	*Amendments to a number of IFRSs*

Except for the amendments to IFRS 10, IFRS 12 and IAS 28,amendments to IFRS 11,IFRS 14, amendments to IAS 27, and certain amendments included in the Annual Improvements 2012-2014 Cycle, which are not relevant to the preparation of the Group's financial statements, the nature and the impact of the amendments are described below:

(a) Amendments to IAS 1 include narrow-focus improvements in respect of the presentation and disclosure in financial statements. The amendments clarify:

   (i) the materiality requirements in IAS 1;

   (ii) that specific line items in the statement of profit or loss and the statement of financial position may be disaggregated;

   (iii) that entities have flexibility as to the order in which they present the notes to financial statements; and

   (iv) that the share of other comprehensive income of associates and joint ventures accounted for using the equity method must be presented in aggregate as a single line item, and classified between those items that will or will not be subsequently reclassified to profit or loss.

   Furthermore, the amendments clarify the requirements that apply when additional subtotals are presented in the statement of financial position and the statement of profit or loss. The amendments have had no significant impact on the Group's financial statements.

(b) Amendments to IAS 16 and IAS 38 clarify the principle in IAS 16 and IAS 38 that revenue reflects a pattern of economic benefits that are generated from operating a business (of which the asset is part) rather than the economic benefits that are consumed through the use of the asset. As a result, a revenue-based method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortise intangible assets. The amendments are applied prospectively. The amendments have had no impact on the financial position or performance of the Group as the Group has not used a revenue-based method for the calculation of depreciation of its non-current assets.

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES (continued)

(c) Annual Improvements to IFRSs 2012-2014 Cycle issued in September 2014 sets out amendments to a number of IFRSs. Details of the amendments are as follows:

- IFRS 5 Non-current Assets Held for Sale and Discontinued Operations: Clarifies that changes to a plan of sale or a plan of distribution to owners should not be considered to be a new plan of disposal, rather it is a continuation of the original plan. Accordingly, there is no change in the application of the requirements in IFRS 5. The amendments also clarify that changing the disposal method does not change the date of classification of the non-current assets or disposal group held for sale. The amendments are applied prospectively. The amendments have had no impact on the Group as the Group did not have any change in the plan of sale or disposal method in respect of the disposal group held for sale during the year.

The adoption of the above revised standards and interpretation has had no significant financial effect on these financial statements.

2.3 ISSUED BUT NOT YET EFFECTIVE INTERNATIONAL FINANCIAL REPORTING STANDARDS

The Group has not applied the following new and revised IFRSs, that have been issued but are not yet effective, in these financial statements.

Amendments to IFRS 2	*Classification and Measurement of Share-based Payment Transactions*[2]
Amendments to IFRS 4	*Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts*[2]
IFRS 9	*Financial Instruments*[2]
Amendments to IFRS 10 and IAS 28	*Sale or Contribution of Assets between an Investor and* its Associate or Joint Venture[4]
IFRS 15	*Revenue from Contracts with Customers*[2]
Amendments to IFRS 15	*Clarifications to IFRS 15 Revenue from Contracts with Customers*[2]
IFRS 16	*Leases*[3]
Amendments to IAS 7	*Disclosure Initiative*[1]
Amendments to IAS 12	*Recognition of Deferred Tax Assets for Unrealised Losses*[1]
Amendments to IAS 40	*Transfers of Investment Property*[2]
IFRIC 22	*Foreign Currency Transactions and Advance Consideration*
Amendments to IFRS 12 Included in Annual Improvements 2014-2016 Cycle	*Disclosure of Interests in Other Entities*[1]
Amendments to IFRS 1 Included in Annual Improvements 2014-2016 Cycle	*First-time Adoption of International Financial Reporting Standards*[2]
Amendments to IAS 28 included in Annual Improvements 2014-2016 Cycle	*Investments in Associates and Joint Ventures*[2]

1 Effective for annual periods beginning on or after January 1, 2017
2 Effective for annual periods beginning on or after January 1, 2018
3 Effective for annual periods beginning on or after January 1, 2019
4 No mandatory effective date yet determined but available for adoption

The Group is in the process of making an assessment of the impact of these new and revised IFRSs upon initial application but is not yet in a position to state whether these new and revised IFRSs would have a significant impact on the Group's results of operations and financial position.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments in associates and joint ventures

An associate is an entity in which the Group has a long term interest of generally not less than 20% of the equity voting rights and over which it is in a position to exercise significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

A joint venture is a type of joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the joint venture. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

The Groups' investments in associates and joint ventures are stated in the consolidated statement of financial position at the Groups' share of net assets under the equity method of accounting, less any impairment losses.

Adjustments are made to bring into line any dissimilar accounting policies that may exist.

The Groups' share of the post-acquisition results and other comprehensive income of associates and joint ventures is included in the consolidated statement of profit or loss and other comprehensive income, respectively. In addition, when there has been a change recognised directly in the equity of the associate or joint venture, the Group recognises its share of any changes, when applicable, in the consolidated statement of changes in equity. Unrealised gains and losses resulting from transactions between the Group and its associates or joint ventures are eliminated to the extent of the Groups' investments in the associates or joint ventures, except where unrealised losses provide evidence of an impairment of the asset transferred. Goodwill arising from the acquisition of associates or joint ventures is included as part of the Groups' investments in associates or joint ventures.

If an investment in an associate becomes an investment in a joint venture or vice versa, the retained interest is not remeasured. Instead, the investment continues to be accounted for under the equity method. In all other cases, upon loss of significant influence over the associate or joint control over the joint venture, the Group measures and recognises any retained investment at its fair value. Any difference between the carrying amount of the associate or joint venture upon loss of significant influence or joint control and the fair value of the retained investment and proceeds from disposal is recognised in profit or loss.

When an investment in an associate or a joint venture is classified as held for sale, it is accounted for in accordance with IFRS 5 Non-current Assets Held for Sale and Discontinued Operations.

Interests in joint operations

A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

The Group recognises in relation to its interest in a joint operation:

- its assets, including its share of any assets held jointly;
- its liabilities, including its share of any liabilities incurred jointly;
- its revenue from the sale of its share of the output arising from the joint operation;
- its share of the revenue from the sale of the output by the joint operation; and
- its expenses, including its share of any expenses incurred jointly.

The assets, liabilities, revenues and expenses relating to the Group's interest in a joint operation are accounted for in accordance with the IFRSs applicable to the particular assets, liabilities, revenues and expenses.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Business combinations and goodwill

Business combinations are accounted for using the acquisition method. The consideration transferred is measured at the acquisition date fair value which is the sum of the acquisition date fair values of assets transferred by the Group, liabilities assumed by the Group to the former owners of the acquiree and the equity interests issued by the Group in exchange for control of the acquiree. For each business combination, the Group elects whether to measure the non-controlling interests in the acquiree that are present ownership interests and entitle their holders to a proportionate share of net assets in the event of liquidation at fair value or at the proportionate share of the acquiree's identifiable net assets. All other components of non-controlling interests are measured at fair value. Acquisition-related costs are expensed as incurred.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts of the acquiree.

If the business combination is achieved in stages, the previously held equity interest is remeasured at its acquisition date fair value and any resulting gain or loss is recognised in profit or loss.

Any contingent consideration to be transferred by the acquirer is recognised at fair value at the acquisition date. Contingent consideration classified as an asset or liability is measured at fair value with changes in fair value recognised in profit or loss. Contingent consideration that is classified as equity is not remeasured and subsequent settlement is accounted for within equity.

Goodwill is initially measured at cost, being the excess of the aggregate of the consideration transferred, the amount recognised for non-controlling interests and any fair value of the Group's previously held equity interests in the acquiree over the identifiable net assets acquired and liabilities assumed. If the sum of this consideration and other items is lower than the fair value of the net assets acquired, the difference is, after reassessment, recognised in profit or loss as a gain on bargain purchase.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is tested for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. The Group performs its annual impairment test of goodwill as at December 31. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units) to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised. An impairment loss recognised for goodwill is not reversed in a subsequent period.

Where goodwill has been allocated to a cash-generating unit (or group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on the disposal. Goodwill disposed of in these circumstances is measured based on the relative value of the operation disposed of and the portion of the cash-generating unit retained.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair value measurement

The Group measures its biological assets and agricultural produce at fair value less costs to sell at the end of each reporting period. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either in the principal market for the asset or liability, or in the absence of a principal market, in the most advantageous market for the asset or liability. The principal or the most advantageous market must be accessible by the Group. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

Level 1 – based on quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2 – based on valuation techniques for which the lowest level input that is significant to the fair value measurement is observable, either directly or indirectly

Level 3 – based on valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by reassessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment of non-financial assets

Where an indication of impairment exists, or when annual impairment testing for an asset is required (other than inventories, construction contract assets, financial assets, investment properties and non-current assets/a disposal group classified as held for sale), the assets' recoverable amount is estimated. An assets' recoverable amount is the higher of the asset's or cash-generating unit's value in use and its fair value less costs of disposal, and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is charged to profit or loss in the period in which it arises in those expense categories consistent with the function of the impaired asset.

An assessment is made at the end of each reporting period as to whether there is an indication that previously recognised impairment losses may no longer exist or may have decreased. If such an indication exists, the recoverable amount is estimated. A previously recognised impairment loss of an asset other than goodwill is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, but not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation) had no impairment loss been recognised for the asset in prior years. A reversal of such an impairment loss is credited to profit or loss in the period in which it arises, unless the asset is carried at a revalued amount, in which case the reversal of the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

Related parties

A party is considered to be related to the Group if:

(a) the party is a person or a close member of that person's family and that person

- (i) has control or joint control over the Group;
- (ii) has significant influence over the Group; or
- (iii) is a member of the key management personnel of the Group or of a parent of the Group;

or

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Related parties (continued)

(b) the party is an entity where any of the following conditions applies:

(i) the entity and the Group are members of the same group;

(ii) one entity is an associate or joint venture of the other entity (or of a parent, subsidiary or fellow subsidiary of the other entity);

(iii) the entity and the Group are joint ventures of the same third party;

(iv) one entity is a joint venture of a third entity and the other entity is an associate of the third entity;

(v) the entity is a post-employment benefit plan for the benefit of employees of either the Group or an entity related to the Group;

(vi) the entity is controlled or jointly controlled by a person identified in (a);

(vii) a person identified in (a) (i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity); and

(viii) the entity, or any member of a group of which it is a part, provides key management personnel services to the Group or to the parent of the Group.

Property, plant and equipment and depreciation

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and any impairment losses. When an item of property, plant and equipment is classified as held for sale or when it is part of a disposal group classified as held for sale, it is not depreciated and is accounted for in accordance with IFRS 5, as further explained in the accounting policy for "Non-current assets and disposal groups held for sale". The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the statement of profit or loss in the period in which it is incurred. In situations where the recognition criteria are satisfied, the expenditure for a major inspection is capitalised in the carrying amount of the asset as a replacement. Where significant parts of property, plant and equipment are required to be replaced at intervals, the Group recognises such parts as individual assets with specific useful lives and depreciates them accordingly.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property, plant and equipment and depreciation (continued)

Depreciation is calculated on the straight-line basis to write off the cost of each item of property, plant and equipment to its residual value over its estimated useful life. The principal annual rates used for this purpose are as follows:

	Useful lives	Residual values
Buildings	20 years	5%
Machinery and equipment	5-10 years	5%
Office and other equipment	5 years	5%
Motor vehicles	5 years	5%

Where parts of an item of property, plant and equipment have different useful lives, the cost of that item is allocated on a reasonable basis among the parts and each part is depreciated separately. Residual values, useful lives and the depreciation method are reviewed, and adjusted if appropriate, at least at each financial year end.

An item of property, plant and equipment including any significant part initially recognised is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss on disposal or retirement recognised in profit or loss in the year the asset is derecognised is the difference between the net sales proceeds and the carrying amount of the relevant asset.

Construction in progress represents a building under construction, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction and capitalised borrowing costs on related borrowed funds during the period of construction. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

Biological assets

Biological assets comprise dairy cows, including milkable cows, heifers and calves which are raised by the Group for the purposes of producing raw milk.

Biological assets are measured on initial recognition and at the end of the reporting period at their fair value less costs to sell, with any resultant gain or loss recognised in profit or loss for the year in which it arises. Costs to sell are the incremental costs directly attributable to the disposal of an asset, mainly transportation costs and excluding finance costs and income taxes. The fair value of biological assets is determined based on its present location and condition and is determined independently by professional valuers.

The feeding costs and other related costs including the depreciation charge, utility costs and consumables incurred for the raising of heifers and calves are capitalised, until such time as the heifers and calves begin to produce milk.

Agricultural produce

Agricultural produce represents raw milk. Upon harvest, agricultural produce is recognised at its fair value less costs to sell, which is determined based on market prices in the local area. The costs to sell are the incremental costs directly attributable to the sales of the agricultural produce, mainly transportation costs, excluding finance costs and income tax.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Non-current assets and disposal groups held for sale

Non-current assets and disposal groups are classified as held for sale if their carrying amounts will be recovered principally through a sales transaction rather than through continuing use. For this to be the case, the asset or disposal group must be available for immediate sale in its present condition subject only to terms that are usual and customary for the sale of such assets or disposal groups and its sale must be highly probable. All assets and liabilities of a subsidiary classified as a disposal group are reclassified as held for sale regardless of whether the Group retains a non-controlling interest in its former subsidiary after the sale.

Non-current assets and disposal groups (other than investment properties and financial assets) classified as held for sale are measured at the lower of their carrying amounts and fair values less costs to sell. Property, plant and equipment and intangible assets classified as held for sale are not depreciated or amortised.

Intangible assets (other than goodwill)

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is the fair value at the date of acquisition. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are subsequently amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each financial year end.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangible assets are not amortised. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether the indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is accounted for on a prospective basis.

Technical know-how

Technical know-how is stated at cost less any impairment losses and is amortised on the straight-line basis over its estimated useful life of 10 to 20 years.

Research and development costs

All research costs are charged to profit or loss as incurred.

Expenditure incurred on projects to develop new products is capitalised and deferred only when the Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the project and the ability to measure reliably the expenditure during the development. Product development expenditure which does not meet these criteria is expensed when incurred.

Deferred development costs are stated at cost less any impairment losses and are amortised using the straight-line basis over the commercial lives of the underlying products.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Leases

Leases that transfer substantially all the rewards and risks of ownership of assets to the Group, other than legal title, are accounted for as finance leases. At the inception of a finance lease, the cost of the leased asset is capitalised at the present value of the minimum lease payments and recorded together with the obligation, excluding the interest element, to reflect the purchase and financing. Assets held under capitalised finance leases, including prepaid land lease payments under finance leases, are included in property, plant and equipment, and depreciated over the shorter of the lease terms and the estimated useful lives of the assets. The finance costs of such leases are charged to profit or loss so as to provide a constant periodic rate of charge over the lease terms.

Assets acquired through hire purchase contracts of a financing nature are accounted for as finance leases, but are depreciated over their estimated useful lives.

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Group is the lessee, rentals payable under operating leases net of any incentives received from the lessor are charged to profit or loss on the straight-line basis over the lease terms.

Prepaid land lease payments under operating leases are initially stated at cost and subsequently recognised on the straight-line basis over the lease terms.

When the lease payments cannot be allocated reliably between the land and buildings elements, the entire lease payments are included in the cost of the land and buildings as a finance lease in property, plant and equipment.

Investments and other financial assets

Initial recognition and measurement

Financial assets are classified, at initial recognition, as financial assets at fair value through profit or loss, loans and receivables and available-for-sale financial investments, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. When financial assets are recognised initially, they are measured at fair value plus transaction costs that are attributable to the acquisition of the financial assets, except in the case of financial assets recorded at fair value through profit or loss.

All regular way purchases and sales of financial assets are recognised on the trade date, that is, the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments and other financial assets (continued)

Subsequent measurement

The subsequent measurement of financial assets depends on their classification as follows:

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading and financial assets designated upon initial recognition as at fair value through profit or loss. Financial assets are classified as held for trading if they are acquired for the purpose of sale in the near term. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments as defined by IAS 39.

Financial assets at fair value through profit or loss are carried in the statement of financial position at fair value with positive net changes in fair value presented as other income and gains and negative net changes in fair value presented as finance costs in the statement of profit or loss. These net fair value changes do not include any dividends or interest earned on these financial assets, which are recognised in accordance with the policies set out for “Revenue recognition” below.

Financial assets designated upon initial recognition as at fair value through profit or loss are designated at the date of initial recognition and only if the criteria in IAS 39 are satisfied.

Derivatives embedded in host contracts are accounted for as separate derivatives and recorded at fair value if their economic characteristics and risks are not closely related to those of the host contracts and the host contracts are not held for trading or designated as at fair value through profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognised in profit or loss. Reassessment only occurs if there is either a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required or a reclassification of a financial asset out of the fair value through profit or loss category.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, such assets are subsequently measured at amortised cost using the effective interest rate method less any allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and includes fees or costs that are an integral part of the effective interest rate. The effective interest rate amortisation is included in other income and gains in profit or loss. The loss arising from impairment is recognised in profit or loss in finance costs for loans and in other expenses for receivables.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments and other financial assets (continued)

Available-for-sale financial investments

Available-for-sale financial investments are non-derivative financial assets in listed and unlisted equity investments and debt securities. Equity investments classified as available for sale are those which are neither classified as held for trading nor designated as at fair value through profit or loss. Debt securities in this category are those which are intended to be held for an indefinite period of time and which may be sold in response to needs for liquidity or in response to changes in market conditions.

After initial recognition, available-for-sale financial investments are subsequently measured at fair value, with unrealised gains or losses recognised as other comprehensive income in the available-for-sale investment revaluation reserve until the investment is derecognised, at which time the cumulative gain or loss is recognised in profit or loss as other income, or until the investment is determined to be impaired, when the cumulative gain or loss is reclassified from the available-for-sale investment revaluation reserve to profit or loss as other gains or losses. Interest and dividends earned whilst holding the available-for-sale financial investments are reported as interest income and dividend income, respectively and are recognised in profit or loss as other income in accordance with the policies set out for “Revenue recognition” below.

When the fair value of unlisted equity investments cannot be reliably measured because (a) the variability in the range of reasonable fair value estimates is significant for that investment or (b) the probabilities of the various estimates within the range cannot be reasonably assessed and used in estimating fair value, such investments are stated at cost less any impairment losses.

The Group evaluates whether the ability and intention to sell its available-for-sale financial assets in the near term are still appropriate. When, in rare circumstances, the Group is unable to trade these financial assets due to inactive markets, the Group may elect to reclassify these financial assets if management has the ability and intention to hold the assets for the foreseeable future or until maturity.

For a financial asset reclassified from the available-for-sale category, the fair value carrying amount at the date of reclassification becomes its new amortised cost and any previous gain or loss on that asset that has been recognised in equity is amortised to profit or loss over the remaining life of the investment using the effective interest rate. Any difference between the new amortised cost and the maturity amount is also amortised over the remaining life of the asset using the effective interest rate. If the asset is subsequently determined to be impaired, then the amount recorded in equity is reclassified to profit or loss.

Derecognition of financial assets

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is primarily derecognised (i.e., removed from the Group’s consolidated statement of financial position) when:

- the rights to receive cash flows from the asset have expired; or
- the Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a “pass-through” arrangement; and either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Derecognition of financial assets (continued)

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, it evaluates if and to what extent it has retained the risk and rewards of ownership of the asset. When it has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the Group continues to recognise the transferred asset to the extent of the Group's continuing involvement. In that case, the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Impairment of financial assets

The Group assesses at the end of each reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired. An impairment exists if one or more events that occurred after the initial recognition of the asset have an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that a debtor or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and observable data indicating that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Financial assets carried at amortised cost

For financial assets carried at amortised cost, the Group first assesses whether impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

The amount of any impairment loss identified is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not yet been incurred). The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition).

The carrying amount of the asset is reduced through the use of an allowance account and the loss is recognised in profit or loss. Interest income continues to be accrued on the reduced carrying amount using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. Loans and receivables together with any associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Group.

If, in a subsequent period, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a write-off is later recovered, the recovery is credited to other expenses in profit or loss.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment of financial assets (continued)

Assets carried at cost

If there is objective evidence that an impairment loss has been incurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, or on a derivative asset that is linked to and must be settled by delivery of such an unquoted equity instrument, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Impairment losses on these assets are not reversed.

Available-for-sale financial investments

For available-for-sale financial investments, the Group assesses at the end of each reporting period whether there is objective evidence that an investment or a group of investments is impaired.

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in profit or loss, is removed from other comprehensive income and recognised in profit or loss.

In the case of equity investments classified as available for sale, objective evidence would include a significant or prolonged decline in the fair value of an investment below its cost. "Significant" is evaluated against the original cost of the investment and "prolonged" against the period in which the fair value has been below its original cost. Where there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in profit or loss – is removed from other comprehensive income and recognised in profit or loss. Impairment losses on equity instruments classified as available for sale are not reversed through profit or loss. Increases in their fair value after impairment are recognised directly in other comprehensive income.

The determination of what is "significant" or "prolonged" requires judgement. In making this judgement, the Group evaluates, among other factors, the duration or extent to which the fair value of an investment is less than its cost.

In the case of debt instruments classified as available for sale, impairment is assessed based on the same criteria as financial assets carried at amortised cost. However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortised cost and the current fair value, less any impairment loss on that investment previously recognised in the statement of profit or loss. Future interest income continues to be accrued based on the reduced carrying amount of the asset using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded as part of finance income. Impairment losses on debt instruments are reversed through the statement of profit or loss if the subsequent increase in fair value of the instruments can be objectively related to an event occurring after the impairment loss was recognised in the statement of profit or loss.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial liabilities

Initial recognition and measurement

Financial liabilities are classified, at initial recognition, as financial liabilities at fair value through profit or loss, loans and borrowings, or as derivatives designated as hedging instruments in an effective hedge, as appropriate.

All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings, net of directly attributable transaction costs.

The Group's financial liabilities include trade and other payables, and interest-bearing bank and other borrowings.

Subsequent measurement

The subsequent measurement of financial liabilities depends on their classification as follows:

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss include financial liabilities held for trading and financial liabilities designated upon initial recognition as at fair value through profit or loss.

Financial liabilities are classified as held for trading if they are acquired for the purpose of repurchasing in the near term. This category includes derivative financial instruments entered into by the Group that are not designated as hedging instruments in hedge relationships as defined by IAS 39. Separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on liabilities held for trading are recognised in profit or loss. The net fair value gain or loss recognised in profit or loss does not include any interest charged on these financial liabilities.

Financial liabilities designated upon initial recognition as at fair value through profit or loss are designated at the date of initial recognition and only if the criteria in IAS 39 are satisfied.

Loans and borrowings

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost, using the effective interest rate method unless the effect of discounting would be immaterial, in which case they are stated at cost. Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the effective interest rate amortisation process.

Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the effective interest rate. The effective interest rate amortisation is included in finance costs in profit or loss.

Financial guarantee contracts

Financial guarantee contracts issued by the Group are those contracts that require a payment to be made to reimburse the holder for a loss it incurs because the specified debtor fails to make a payment when due in accordance with the terms of a debt instrument. A financial guarantee contract is recognised initially as a liability at its fair value, adjusted for transaction costs that are directly attributable to the issuance of the guarantee. Subsequent to initial recognition, the Group measures the financial guarantee contract at the higher of: (i) the amount of the best estimate of the expenditure required to settle the present obligation at the end of the reporting period; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Derecognition of financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled, or expires.

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and a recognition of a new liability, and the difference between the respective carrying amounts is recognised in profit or loss.

Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position if there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liabilities simultaneously.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on the first-in, first-out basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour and an appropriate proportion of overheads. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents comprise cash on hand and demand deposits, and short term highly liquid investments that are readily convertible into known amounts of cash, are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired.

For the purpose of the consolidated statement of financial position, cash and cash equivalents comprise cash on hand and at banks, including term deposits, and assets similar in nature to cash, which are not restricted as to use.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the end of the reporting period of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in profit or loss.

Provisions for product warranties granted by the Group on certain products are recognised based on sales volume and past experience of the level of repairs and returns, discounted to their present values as appropriate.

A contingent liability recognised in a business combination is initially measured at its fair value. Subsequently, it is measured at the higher of (i) the amount that would be recognised in accordance with the general guidance for provisions above; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with the guidance for revenue recognition.

Income tax

Income tax comprises current and deferred tax. Income tax relating to items recognised outside profit or loss is recognised outside profit or loss, either in other comprehensive income or directly in equity.

Current tax assets and liabilities are measured at the amount expected to be recovered from or paid to the taxation authorities, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period, taking into consideration interpretations and practices prevailing in the countries in which the Group operates.

Deferred tax is provided, using the liability method, on all temporary differences at the end of the reporting period between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences, except:

- when the deferred tax liability arises from the initial recognition of goodwill or an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries and associates, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Income tax (continued)

Deferred tax assets are recognised for all deductible temporary differences, the carryforward of unused tax credits and any unused tax losses. Deferred tax assets are recognised to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, the carryforward of unused tax credits and unused tax losses can be utilised, except:

- when the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries and associates, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at the end of each reporting period and are recognised to the extent that it has become probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Government grants

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income on a systematic basis over the periods that the costs, which it is intended to compensate, are expensed.

Grants relating to biological assets

An unconditional government grant related to a biological asset measured at its fair value less costs to sell is recognised in profit or loss when, and only when, the government grant becomes receivable. If a government grant related to a biological asset measured at its fair value less costs to sell is conditional, the Group recognises the government grant in profit or loss when, and only when, the conditions attaching to the government grant are met.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Government grants (continued)

Other grants

When the grant relates to an expense item, it is recognised as income on a systematic basis over the periods that the costs, which it is intended to compensate, are expensed.

Where the grant relates to an asset, the fair value is credited to a deferred income account and is released to profit or loss over the expected useful life of the relevant asset by equal annual instalments or deducted from the carrying amount of the asset and released to profit or loss by way of a reduced depreciation charge.

Where the Group receives grants of non-monetary assets, the grants are recorded at the fair value of the non-monetary assets and released to profit or loss over the expected useful lives of the relevant assets by equal annual instalments.

Where the Group receives government loans granted with no or at a below-market rate of interest for the construction of a qualifying asset, the initial carrying amount of the government loans is determined using the effective interest rate method, as further explained in the accounting policy for "Financial liabilities" above. The benefit of the government loans granted with no or at a below-market rate of interest, which is the difference between the initial carrying value of loans and the proceeds received, is treated as a government grant and released to profit or loss over the expected useful life of the relevant asset by equal annual instalments.

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

(a) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;

(b) interest income, on an accrual basis using the effective interest method by applying the rate that exactly discounts the estimated future cash receipts over the expected life of the financial instrument or a shorter period, when appropriate, to the net carrying amount of the financial asset; and

(c) dividend income, when the shareholders' right to receive payment has been established.

Share-based payments

The Company operates a share option scheme for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. Employees (including directors) of the Group receive remuneration in the form of share-based payments, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted. The fair value is determined by an external valuer using a binomial model, further details of which are given in note 34 to the financial statements.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Share-based payments (continued)

The cost of equity-settled transactions is recognised in employee benefit expense, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled. The cumulative expense recognised for equity-settled transactions at the end of each reporting period until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The charge or credit to profit or loss for a period represents the movement in the cumulative expense recognised as at the beginning and end of that period.

Service and non-market performance conditions are not taken into account when determining the grant date fair value of awards, but the likelihood of the conditions being met is assessed as part of the Group's best estimate of the number of equity instruments that will ultimately vest. Market performance conditions are reflected within the grant date fair value. Any other conditions attached to an award, but without an associated service requirement, are considered to be non-vesting conditions. Non-vesting conditions are reflected in the fair value of an award and lead to an immediate expensing of an award unless there are also service and/or performance conditions.

For awards that do not ultimately vest because non-market performance and/or service conditions have not been met, no expense is recognised. Where awards include a market or non-vesting condition, the transactions are treated as vesting irrespective of whether the market or non-vesting condition is satisfied, provided that all other performance and/or service conditions are satisfied.

Where the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified, if the original terms of the award are met. In addition, an expense is recognised for any modification that increases the total fair value of the share-based payments, or is otherwise beneficial to the employee as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. This includes any award where non-vesting conditions within the control of either the Group or the employee are not met. However, if a new award is substituted for the cancelled award, and is designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of earnings per share.

Other employee benefits

Pension scheme

The employees of the Groups' subsidiaries which operate in Mainland China are required to participate in a central pension scheme operated by the local municipal governments. These subsidiaries are required to contribute a certain percentage of their payroll costs to the central pension scheme. The contributions are charged to profit or loss as they become payable in accordance with the rules of the central pension scheme.

Termination benefits

Termination benefits are recognised at the earlier of when the Group can no longer withdraw the offer of those benefits and when the Group recognises restructuring costs involving the payment of termination benefits.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e., assets that necessarily take a substantial period of time to get ready for their intended use or sale, are capitalised as part of the cost of those assets. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs capitalised. All other borrowing costs are expensed in the period in which they are incurred. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

Where funds have been borrowed generally, and used for the purpose of obtaining qualifying assets, a capitalisation rate has been applied to the expenditure on the individual assets.

Dividends

Final dividends are recognised as a liability when they are approved by the shareholders in a general meeting.

Interim dividends are simultaneously proposed and declared, because the Company's memorandum and articles of association grant the directors the authority to declare interim dividends. Consequently, interim dividends are recognised immediately as a liability when they are proposed and declared.

Foreign currencies

These financial statements are presented in Renminbi ("**RMB**"). Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Foreign currency transactions recorded by the entities in the Group are initially recorded using their respective functional currency rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rates of exchange ruling at the end of the reporting period. Differences arising on settlement or translation of monetary items are recognised in profit or loss.

Differences arising on settlement or translation of monetary items are recognised in profit or loss with the exception of monetary items that are designated as part of the hedge of the Group's net investment of a foreign operation. These are recognised in other comprehensive income until the net investment is disposed of, at which time the cumulative amount is reclassified to profit or loss. Tax charges and credits attributable to exchange differences on those monetary items are also recorded in other comprehensive income.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was measured. The gain or loss arising on translation of a non-monetary item measured at fair value is treated in line with the recognition of the gain or loss on change in fair value of the item (i.e., translation difference on the item whose fair value gain or loss is recognised in other comprehensive income or profit or loss is also recognised in other comprehensive income or profit or loss, respectively).

The functional currencies of certain overseas subsidiaries are currencies other than RMB. As at the end of the reporting period, the assets and liabilities of these entities are translated into RMB at the exchange rates prevailing at the end of the reporting period and their statements of profit or loss and other comprehensive income are translated into RMB at the weighted average exchange rates for the year.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Foreign currencies (continued)

The resulting exchange differences are recognised in other comprehensive income and accumulated in the exchange fluctuation reserve. On disposal of a foreign operation, the component of other comprehensive income relating to that particular foreign operation is recognised in profit or loss.

Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on acquisition are treated as assets and liabilities of the foreign operation and translated at the closing rate.

For the purpose of the consolidated statement of cash flows, the cash flows of overseas subsidiaries are translated into RMB at the exchange rates ruling at the dates of the cash flows. Frequently recurring cash flows of overseas subsidiaries which arise throughout the year are translated into RMB at the weighted average exchange rates for the year.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

The preparation of the Group's financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and their accompanying disclosures, and the disclosure of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that could require a material adjustment to the carrying amounts of the assets or liabilities affected in the future.

Judgements

In the process of applying the Group's accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect on the amounts recognised in the financial statements:

Withholding tax arising from the distribution of dividends

The Group's determination as to whether to accrue for withholding taxes arising from the distributions of dividends from certain subsidiaries according to the relevant tax jurisdictions is subject to judgements on the timing of the payment of the dividends or the amount of profits to be retained by the relevant subsidiary. As at December 31, 2016, the deferred tax liabilities arising thereon amounted to nil (2015: Nil).

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (continued)

Estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below.

Fair value of dairy cows

The Group's dairy cows are valued at fair value less costs to sell. The fair value of dairy cows is determined based on either the market-determined prices as at each year end adjusted with reference to the species, age, growing condition, cost incurred and expected yield of the milk to reflect differences in characteristic and/or stages of growth of dairy cows; or the present value of expected net cash flows from the dairy cows discounted at a current market-determined rate, when market-determined prices are unavailable. Any changes in the estimates may affect the fair value of the dairy cows significantly. The independent qualified professional valuer and management review the assumptions and estimates periodically to identify any significant change in fair value of dairy cows. Further details are given in note 19 to the financial statements.

Impairment of receivables

Management assesses doubtful accounts for estimated losses resulting from the inability of the debtors to make the required payments. Management bases the estimates on the assessment of recoverability of individual receivable balance, customer creditworthiness, and historical write-off experience. If the financial condition of the debtors was to deteriorate, actual write-offs would be higher than estimated.

Impairment of raw materials

Management estimates net realisable value of raw materials based on the estimated selling price of finished products in which they will be incorporated, the estimated costs of completion and the estimated costs necessary to make the sale. The carrying amount of raw materials is written down below cost to net realisable value when the cost of raw materials is higher than the net realisable value. If management's estimates change, a provision for decline in the value of raw materials is recognised in profit or loss.

Impairment of non-financial assets (other than goodwill)

The Group assesses whether there are any indicators of impairment for all non-financial assets at the end of each reporting period. Indefinite life intangible assets are tested for impairment annually and at other times when such an indicator exists. Other non-financial assets are tested for impairment when there are indicators that the carrying amounts may not be recoverable. An impairment exists when the carrying value of an asset or a cash-generating unit exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The calculation of the fair value less costs to sell is based on available data from binding sales transactions in an arm's length transaction of similar assets or observable market prices less incremental costs for disposing of the asset. When value in use calculations are undertaken, management must estimate the expected future cash flows from the asset or cash-generating unit and choose a suitable discount rate in order to calculate the present value of those cash flows.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (continued)

Estimation uncertainty (continued)

Depreciation

Property, plant and equipment are depreciated on the straight-line basis over the estimated useful lives of the assets, after taking into account the estimated residual values. Management reviews the estimated useful lives and residual values of the assets regularly in order to determine the amount of depreciation expense to be recorded during any reporting period. The determination of the useful lives and residual values are based on the historical experience with similar assets and taking into account anticipated technological changes. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates.

Deferred tax assets

Deferred tax assets are recognised for unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits together with future tax planning strategies.

Impairment of available-for-sale financial assets

The Group classifies certain assets as available for sale and recognises movements of their fair values in equity. When the fair value declines, management makes assumptions about the decline in value to determine whether there is an impairment that should be recognised in the statement of profit or loss.

4. OPERATING SEGMENT INFORMATION

For management purposes, the Group is organised into business units based on their products and services and has two reportable operating segments as follows:

(a) Dairy farming – breeding dairy cows to produce and distribute raw milk; and

(b) Liquid milk products – producing and distributing self-owned brand ultra-heat treated liquid milk, organic yogurt and other dairy products.

Management monitors the results of the Group's operating segments separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on reportable segment profit/loss, which is a measure of adjusted profit/loss for the year. The adjusted profit/loss for the year is measured consistently with the Group's profit after tax except that gain arising from fair value less costs to sell of biological assets is excluded from this measurement as management believes that such adjusted information is most relevant in evaluating the results of the dairy farming segment as compared to the results of other entities that operate within the dairy farming industry.

Segment assets exclude unallocated head office and corporate assets as these assets are managed on a group basis.

Segment liabilities exclude unallocated head office and corporate liabilities as these liabilities are managed on a group basis.

Intersegment sales and transfers are transacted with reference to the prices internally agreed between dairy farming segment and liquid milk products segment.

4. OPERATING SEGMENT INFORMATION (continued)

Year ended December 31, 2016	Dairy farming	Liquid milk products	Total
	RMB'000	RMB'000	RMB'000
Segment revenue:			
Sales to external customers	1,360,401	2,106,143	3,466,544
Intersegment sales	1,302,553	—	1,302,553
	2,662,954	2,106,143	4,769,097
Reconciliation:			
Elimination of intersegment sales			(1,302,553)
Revenue			3,466,544
Segment results	1,018,835	(5,145)	1,013,690
Reconciliation:			
Elimination of intersegment results			(25,995)
Loss arising from changes in fair value less costs to sell of biological assets			(15,729)
Corporate and other unallocated expenses			(15,158)
Profit for the year			956,808
Segment assets	9,098,425	2,189,724	11,288,149
Reconciliation:			
Elimination of intersegment receivables			(919,698)
Corporate and other unallocated assets			130,844
Total assets			10,499,295
Segment liabilities	3,488,046	1,512,368	5,000,414
Reconciliation:			
Elimination of intersegment payables			(919,698)
Corporate and other unallocated liabilities			71,452
Total liabilities			4,152,168

4. OPERATING SEGMENT INFORMATION (continued)

Year ended December 31, 2016	Dairy farming	Liquid milk products	Total
	RMB'000	RMB'000	RMB'000
Other segment information:			
Share of profits and losses of associates	1,404	(17,646)	(16,242)
Segment bank interest income	3,258	500	3,758
Corporate and other unallocated bank interest income			195
Total bank interest income			3,953
Segment finance costs	113,981	10,397	124,378
Corporate and other unallocated finance costs			289
Total finance costs			124,667
Income tax expenses	—	(11,077)	(11,077)
Share option expenses	35,566	2,728	38,294
Corporate and other unallocated share option expenses	—	—	6,857
Total share option expenses			45,151
Depreciation and amortisation	111,966	36,517	148,483
Investments in associates	35,150	77,508	112,658
Segment capital expenditure*	1,122,364	321,354	1,443,718

4. OPERATING SEGMENT INFORMATION (continued)

Year ended December 31, 2015	Dairy farming	Liquid milk products	Total
	RMB'000	RMB'000	RMB'000
Segment revenue:			
Sales to external customers	1,445,022	1,655,689	3,100,711
Intersegment sales	1,076,373	—	1,076,373
	2,521,395	1,655,689	4,177,084
Reconciliation:			
Elimination of intersegment sales			(1,076,373)
Revenue			3,100,711
Segment results	996,931	110,668	1,107,599
Reconciliation:			
Elimination of intersegment results			(72,596)
Gain arising from changes in fair value less costs to sell of biological assets			52,722
Corporate and other unallocated expenses			(4,503)
Profit for the year			1,083,222
Segment assets	8,347,005	1,537,127	9,884,132
Reconciliation:			
Elimination of intersegment receivables			(551,363)
Corporate and other unallocated assets			127,024
Total assets			9,459,793
Segment liabilities	3,560,796	1,083,123	4,643,919
Reconciliation:			
Elimination of intersegment payables			(551,363)
Corporate and other unallocated liabilities			12
Total liabilities			4,092,568

4. OPERATING SEGMENT INFORMATION (continued)

Year ended December 31, 2015	Dairy farming	Liquid milk products	Total
	RMB'000	RMB'000	RMB'000
Other segment information:			
Share of profits and losses of associates	1,192	(19,233)	(18,041)
Segment bank interest income	9,338	965	10,303
Corporate and other unallocated bank interest income			1,931
Total bank interest income			12,234
Finance costs	89,400	9,747	99,147
Income tax expenses	—	4,606	4,606
Share option expenses	25,278	1,733	27,011
Depreciation and amortisation	82,857	23,829	106,686
Investments in associates	22,880	9,175	32,055
Segment capital expenditure*	990,958	270,503	1,261,461
Corporate and other unallocated capital expenditure			34
Total capital expenditure			1,261,495

* Segment capital expenditure consists of purchases of items of property, plant and equipment, additions to prepaid land lease payments, additions to other intangible assets, purchases of biological assets, payments for breeding calves and heifers and acquisition of associates.

Geographical information

All external sales of the Group during the year were contributed by customers located in the PRC.

Over 90% of the Group's non-current assets are located in the PRC.

Information about major customers

Revenue from the following customers individually amounted to more than 10% of the Group's total revenue during the year:

	2016	2015
	RMB'000	RMB'000
Entity A	809,749	1,152,036
Entity B	529,927	266,102
	1,339,676	1,418,138

5. REVENUE, OTHER INCOME AND GAINS/(LOSSES)

Revenue represents the net invoiced value of goods sold, after allowances for returns and trade discounts.

An analysis of revenue, other income and gains/(losses) is as follows:

	2016	2015
	RMB'000	RMB'000
Revenue		
– Sales of raw milk	1,360,401	1,445,022
– Sales of liquid milk products	2,106,143	1,655,689
	3,466,544	3,100,711
Other income and gains/(losses)		
– Government grants	7,924	31,791
– Bank interest income	3,953	12,234
– Foreign exchange differences, net	(4,662)	(40)
– Loss on disposal of items of property, plant and equipment	(14,677)	(141)
– Impairment of trade receivables	(86,310)	(369)
– Others	6,626	3,949
	(87,146)	47,424
	3,379,398	3,148,135

6. PROFIT BEFORE TAX

The Group's profit before tax is arrived at after charging/(crediting):

	2016	2015
	RMB'000	RMB'000
Cost of inventories sold	1,791,133	1,623,168
Loss/(gain) arising from changes in fair value less costs to sell of biological assets	15,729	(52,722)
Depreciation of items of property, plant and equipment	146,783	105,046
Amortisation of prepaid land lease payments	266	186
Amortisation of other intangible assets	1,434	1,454
Research and development costs	11,662	8,981
Minimum lease payments under operating leases	1,200	9,532
Auditor's remuneration	2,700	3,450
Employee benefit expense (including directors' and chief executive's remuneration (note 9)):		
Wages, salaries, bonuses and allowances	241,272	236,787
Other social insurances and benefits	27,411	12,504
Pension scheme contributions	11,506	9,434
Equity-settled share option expenses	45,151	27,011
	325,340	285,736

7. OTHER EXPENSES

The Group made donations with a total amount of RMB56,233,000 (2015:Nil) during the year of 2016.

8. FINANCE COSTS

	2016	2015
	RMB'000	RMB'000
Interest on bank loans	61,373	107,319
Interest on short-term notes	5,730	250
Interest on corporate bonds	64,299	—
Interest on long term payables	6,157	—
Less: Interest capitalised	(12,892)	(8,422)
	124,667	99,147

The capitalisation rates used to determine the amount of borrowing costs eligible for capitalisation for the year ended December 31, 2016 ranged between 1.55% and 5.87% (2015: between 4.88% and 6.72%).

9. DIRECTORS' AND CHIEF EXECUTIVE'S REMUNERATION

Directors' and chief executive's remuneration for the year, disclosed pursuant to the Listing Rules, section 383(1)(a), (b), (c) and (f) of the Hong Kong Companies Ordinance and Part 2 of the Companies (Disclosure of Information about Benefits of Directors) Regulation, is as follows:

	2016	2015
	RMB'000	RMB'000
Fees	505	480
Other emoluments:		
Salaries, allowances and benefits in kind	1,278	927
Pension scheme contributions	44	40
	1,322	967
	1,827	1,447

9. DIRECTORS' AND CHIEF EXECUTIVE'S REMUNERATION (continued)

As of December 31, 2016, certain directors were granted share options in respect of their services to the Group under the share option scheme of the Company, further details of which are set out in note 34 to the financial statements. In accordance with IFRS 2, share option benefits represent the fair value at the grant date of the share options issued under the share option scheme of the Company amortised in profit or loss during the year disregarding whether the options have been vested/exercised or not. During the year, the share option benefits relating to the share options granted to Mr. YAO Tongshan, Mr. WU Jianye, Ms. GAO Lingfeng and Mr. CUI Ruicheng were approximately RMB 7,777,000 (2015: RMB 2,318,000), RMB 7,165,000 (2015: RMB2,136,000), RMB 3,533,000 (2015: RMB 1,053,000) and RMB3,533,000 (2015: RMB1,053,000). Share option benefits relating to the share options granted to the directors are not included in the above table.

(a) Independent non-executive directors

The fees paid to independent non-executive directors during the year were as follows:

	2016	2015
	RMB'000	RMB'000
Mr. LI Changqing	100	100
Ms. GE Xiaoping	100	100
Mr. YUAN Qing	100	100
Mr. WONG Kun Kau	100	100
Mr. Fu Wenge	25	—
	425	400

9. DIRECTORS' AND CHIEF EXECUTIVE'S REMUNERATION (continued)

(b) Executive directors, non-executive directors and the chief executive

	Fees	Salaries, allowances and benefits in kind	Pension scheme contributions	Total remuneration
	RMB'000	RMB'000	RMB'000	RMB'000
2016				
Executive directors:				
Mr. YAO Tongshan (also the chief executive)	20	327	11	358
Mr. WU Jianye	20	317	11	348
Ms. GAO Lingfeng	20	317	11	348
Mr. CUI Ruicheng	20	317	11	348
	80	1,278	44	1,402
Non-executive directors:				
Mr. WU Jingshui	—	—	—	—
Mr. DONG Xianli	—	—	—	—
Mr. FAN Xiang	—	—	—	—
Mr. CUI Guiyong	—	—	—	—
Mr. SUN Qian	—	—	—	—
Mr. SHAO Genhuo	—	—	—	—
Mr. ZHANG Jiawang	—	—	—	—
	—	—	—	—
	80	1,278	44	1,402
2015				
Executive directors:				
Mr. YAO Tongshan (also the chief executive)	20	251	10	281
Mr. WU Jianye	20	240	10	270
Ms. GAO Lingfeng	20	229	10	259
Mr. CUI Ruicheng	20	207	10	237
	80	927	40	1,047
Non-executive directors:				
Mr. WU Jingshui	—	—	—	—
Mr. FAN Xiang	—	—	—	—
Mr. CUI Guiyong	—	—	—	—
Mr. SUN Qian	—	—	—	—
	—	—	—	—
	80	927	40	1,047

There was no arrangement under which a director or the chief executive officer waived or agreed to waive any remuneration during the year.

10. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the year included four executive directors (2015: Nil), details of whose remuneration are set out in note 9 above. Details of the remuneration for the year of the remaining one (2015: five) highest paid employee, who is neither a director nor chief executive of the Company are as follows:

	2016	2015
	RMB'000	RMB'000
Pension scheme contributions	11	38
Salaries, allowances and benefits in kind	427	1,526
	438	1,564

The number of non-director and non-chief executive highest paid employees whose remuneration fell within the following band is as follows:

	Number of employees	
	2016	2015
Nil to HK$1,000,000	1	5

11. INCOME TAX EXPENSE

	2016	2015
	RMB'000	RMB'000
Current - PRC	12,481	4,772
Deferred (note 20)	(23,558)	(166)
	(11,077)	4,606

A reconciliation of the tax expense applicable to profit before tax at the statutory rates for the countries in which the Company and the majority of its subsidiaries are domiciled to the tax expense at the effective tax rate is as follows:

	2016	2015
	RMB'000	RMB'000
Profit before tax	945,731	1,087,828
Tax at the statutory tax rate (note (i))	236,433	271,957
Income not subject to tax (note (ii))	(265,479)	(266,858)
Lower tax rate for specific provinces (note (iii))	(3,089)	(4,073)
Expenses not deductible for tax, net (note (iv))	21,042	5,083
Adjustments in respect of current tax of previous periods	16	(1,503)
Tax charge/(credit) of the Group	(11,077)	4,606

11. INCOME TAX EXPENSE (continued)

Notes:

(i) The Company and its subsidiaries incorporated in the Cayman Islands and the British Virgin Islands are not subject to any income tax pursuant to the local rules and regulations. Hong Kong profits tax has not been provided as there were no assessable profits arising in Hong Kong during the year. Entities in the PRC were generally subject to the PRC enterprise income tax rate of 25% for the year ended December 31, 2016 (2015: 25%).

(ii) According to the Enterprise Income Tax Law of the PRC (the "**EIT Law**"), the Group's income arising from agricultural activities, such as dairy farming and processing of raw agricultural products, is exempt from income tax.

(iii) In accordance with "The notice of tax policies relating to the implementation of the Western China Development Strategy" (財政部、海關總署、國家稅務總局《關於深入實施西部大開發戰略有關稅收政策問題的通知》), the Group's taxable income arising from the processing of non-raw agricultural products is subject to a preferential tax rate of 15% from 2013 to 2020.

(iv) Non-deductible expenses are mainly share of losses of associates, donation and staff welfares exceeding the tax limit.

12. DIVIDENDS

The directors do not recommend the payment of any dividend for the year ended December 31, 2016 (2015: Nil).

13. EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT

The basic earnings per share amount is calculated by dividing the profit for the year attributable to ordinary equity holders of the parent, by the weighted average number of ordinary shares of 6,354,400,000 (2015: 6,354,400,000) in issue during the year.

The diluted earnings per share amount is calculated by dividing the profit for the year attributable to ordinary equity holders of the parent, by the weighted average number of ordinary shares used in the calculation of the basic earnings per share calculation, and the weighted average number of ordinary shares assumed to have been issued at no consideration on the deemed exercise or conversion of all dilutive potential ordinary shares into ordinary shares.

	Number of shares	
	2016	2015
Weighted average number of ordinary shares in issue during the year used in the basic earnings per share calculation	**6,354,400,000**	6,354,400,000
Effect of dilution of share options	**57,439,740**	86,155,092
Weighted average number of ordinary shares in issue during the year used in the diluted earnings per share calculation	**6,411,839,740**	6,440,555,092

14. PROPERTY, PLANT AND EQUIPMENT

	Buildings	Machinery and equipment	Office and other equipment	Motor vehicles	Construction in progress	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
December 31, 2016						
At December 31, 2015 and at January 1, 2016						
Cost	1,280,796	624,875	27,066	9,127	357,073	2,298,937
Accumulated depreciation	(95,652)	(97,483)	(8,389)	(4,183)	—	(205,707)
Net carrying amount	1,185,144	527,392	18,677	4,944	357,073	2,093,230
At January 1, 2016, net of accumulated depreciation	1,185,144	527,392	18,677	4,944	357,073	2,093,230
Additions	93,576	89,997	12,352	963	609,749	806,637
Transfers	388,319	124,700	18,311	—	(531,330)	—
Disposals	(37,192)	(4,843)	(543)	(138)	—	(42,716)
Depreciation provided during the year	(65,249)	(73,179)	(6,885)	(1,470)	—	(146,783)
At December 31, 2016, net of accumulated depreciation	1,564,598	664,067	41,912	4,299	435,492	2,710,368
At December 31, 2016						
Cost	1,721,851	834,018	56,828	9,067	435,492	3,057,256
Accumulated depreciation	(157,253)	(169,951)	(14,916)	(4,768)	—	(346,888)
Net carrying amount	1,564,598	664,067	41,912	4,299	435,492	2,710,368

14. PROPERTY, PLANT AND EQUIPMENT (continued)

	Buildings	Machinery and equipment	Office and other equipment	Motor vehicles	Construction in progress	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
December 31, 2015						
At December 31, 2014 and at January 1, 2015						
Cost	906,007	426,305	21,202	7,932	397,394	1,758,840
Accumulated depreciation	(46,077)	(47,495)	(4,602)	(2,839)	—	(101,013)
Net carrying amount	859,930	378,810	16,600	5,093	397,394	1,657,827
At January 1, 2015, net of accumulated depreciation	859,930	378,810	16,600	5,093	397,394	1,657,827
Additions	275	88,073	4,544	1,250	446,717	540,859
Transfers	374,514	111,110	1,361	53	(487,038)	—
Disposals	—	(395)	(7)	(8)	—	(410)
Depreciation provided during the year	(49,575)	(50,206)	(3,821)	(1,444)	—	(105,046)
At December 31, 2015, net of accumulated depreciation	1,185,144	527,392	18,677	4,944	357,073	2,093,230
At December 31, 2015						
Cost	1,280,796	624,875	27,066	9,127	357,073	2,298,937
Accumulated depreciation	(95,652)	(97,483)	(8,389)	(4,183)	—	(205,707)
Net carrying amount	1,185,144	527,392	18,677	4,944	357,073	2,093,230

15. PREPAID LAND LEASE PAYMENTS

	2016	2015
	RMB'000	RMB'000
Carrying amount at January 1	5,177	5,363
Additions	33,911	—
Recognised during the year	(266)	(186)
Carrying amount at December 31	38,822	5,177
Current portion included in prepayments, deposits and other receivables	(1,256)	(111)
Non-current portion	37,566	5,066

16. OTHER INTANGIBLE ASSETS

	Technical know-how	Computer software	Total
	RMB'000	RMB'000	RMB'000
December 31, 2016			
Cost at January 1, 2016, net of accumulated amortisation	11,629	3,889	15,518
Additions	—	763	763
Amortisation provided during the year	(750)	(684)	(1,434)
At December 31, 2016	10,879	3,968	14,847
At December 31, 2016			
Cost	15,004	5,786	20,790
Accumulated amortisation	(4,125)	(1,818)	(5,943)
Net carrying amount	10,879	3,968	14,847
At December 31, 2015			
Cost	15,004	5,023	20,027
Accumulated amortisation	(3,375)	(1,134)	(4,509)
Net carrying amount	11,629	3,889	15,518

16. OTHER INTANGIBLE ASSETS (continued)

	Technical know-how	Computer software	Total
	RMB'000	RMB'000	RMB'000
December 31, 2015			
Cost at January 1, 2015, net of accumulated amortisation	12,379	3,590	15,969
Additions	—	1,003	1,003
Amortisation provided during the year	(750)	(704)	(1,454)
At December 31, 2015	11,629	3,889	15,518
At December 31, 2015			
Cost	15,004	5,023	20,027
Accumulated amortisation	(3,375)	(1,134)	(4,509)
Net carrying amount	11,629	3,889	15,518
At December 31, 2014			
Cost	15,004	4,020	19,024
Accumulated amortisation	(2,625)	(430)	(3,055)
Net carrying amount	12,379	3,590	15,969

17. INVESTMENTS IN ASSOCIATES

	2016	2015
	RMB'000	RMB'000
Share of net assets	112,658	32,055

The Group's trade receivable and payable balances with the associates are disclosed in note 37 to the financial statements.

17. INVESTMENTS IN ASSOCIATES (continued)

Particulars of the material associates are as follows:

Name	Registered capital	Place of incorporation/ registration and operations	Percentage of equity interests attributable to the Group	Principal activities
Bayannur Shengmu High-tech Ecological Forage Co., Ltd.* (note (a))	RMB 273,180,000	PRC/ Mainland China	9.12%	Grass planting
Food Union Shengmu Dairy Co., Ltd. ("**Food Union Shengmu**")	USD 57,755,000	PRC/ Mainland China	20.00%	Dairy processing

Note:

(a) Although the Group only held a 9.12% equity interest in Bayannur Shengmu High-tech Ecological Forage Co., Ltd. ("**Shengmu Forage**") as at December 31, 2016, Shengmu Forage has been accounted for as an associate of the Group as the Group has had more than 20% effective voting power in Shengmu Forage. Shengmu Forage, which is considered a material associate of the Group, is a strategic partner of the Group and is engaged in grass planting.

The following table illustrates the summarised financial information of Shengmu Forage and Food Union Shengmu adjusted for any differences in accounting policies, and reconciled to the carrying amount in the consolidated financial statements:

Shengmu Forage	**2016**	2015
	RMB'000	RMB'000
Current assets	**429,716**	657,027
Non-current assets	**612,031**	483,625
Current liabilities	**(655,760)**	(886,012)
Net assets	**385,987**	254,640
Reconciliation to the Group's interest in the associate:		
Proportion of the Group's ownership	**9.12%**	9.01%
Group's share of net assets of the associate, excluding goodwill	**35,202**	22,932
Goodwill included in investment	**947**	947
Adjustments	**(999)**	(999)
Carrying amount of the investment	**35,150**	22,880
Revenue	**488,288**	426,622
Profit for the year	**15,387**	13,239
Total comprehensive income for the year	**15,387**	13,239
Dividend received	**—**	—

17. INVESTMENTS IN ASSOCIATES (continued)

Food Union Shengmu	2016	2015
	RMB'000	RMB'000
Current assets	167,198	—
Non-current assets	453,958	—
Current liabilities	(7,960)	—
Non-current liabilities	(250,851)	—
Net assets	362,345	—
Reconciliation to the Group's interest in the associate:		
Proportion of the Group's ownership	20.00%	—
Group's share of net assets of the associate, excluding goodwill	72,469	—
Carrying amount of the investment	72,469	—
Revenue	—	—
Profit /(loss) for the year	(13,376)	—
Total comprehensive income /(loss) for the year	(13,376)	
Dividend received	—	—

The following table illustrates the aggregate financial information of the Group's associates that are not individually material:

	2016	2015
	RMB'000	RMB'000
Share of the associates' loss for the year	(14,971)	(19,233)
Share of the associates' total comprehensive loss	(14,971)	(19,233)
Aggregate carrying amount of the Group's investments in the associates	5,039	9,175

The Group's shareholdings in the associates all comprise equity shares held by the subsidiaries of the Company.

All the above associates have been accounted for using the equity method in these financial statements. The Group has discontinued the recognition of its share of losses of certain associates because the share of losses of the associates exceeded the Group's interests in the associates. The amounts of the Group's unrecognised share of losses of these associates for the current year and cumulatively were RMB72,364,000 (2015: RMB18,242,000) and RMB94,078,000 (2015: RMB21,714,000), respectively.

18. AVAILABLE-FOR-SALE INVESTMENTS

	2016	2015
	RMB'000	RMB'000
Current:		
Short term investment deposits (note(i))	120,000	—
Non-current:		
Unlisted equity investments, at cost(note(ii))	1,427	1,404
	121,427	1,404

Notes:

(i) As at December 31, 2016, the Group held wealth management products of RMB120,000,000 purchased from a domestic commercial bank (December 31, 2015: Nil), which is classified as available-for-sale financial assets measured at cost less impairment.

(ii) The equity investments consist of investments which were designated as available-for-sale financial assets and have no fixed maturity date or coupon rate. The unlisted equity investments were stated at cost less impairment because the range of reasonable fair value estimates is so significant that the directors are of the opinion that their fair values cannot be measured reliably. The Group does not intend to dispose of them in the near future.

19. BIOLOGICAL ASSETS

(A) *Nature of activities*

The biological assets of the Group comprise primarily dairy cows held to produce raw milk.

The quantity of dairy cows owned by the Group at December 31, 2016 and December 31, 2015 is shown below. The Group's dairy cows include milkable cows, heifers and calves. Heifers and calves are dairy cows that have not had their first calves.

	2016	2015
	Head	Head
Dairy cows		
Milkable cows	69,887	66,790
Heifers and calves	59,442	44,605
Total dairy cows	129,329	111,395

In general, heifers are inseminated with semen when they reach the age of approximately 14 months. After approximately 9 months following a successful insemination, a calf is born and the dairy cow begins to produce raw milk and the lactation period begins. The heifers, at this time, will be transferred to the group of milkable cows. A milkable cow is typically milked for approximately 305 days before a resting period of approximately 60 days. The male calves newly born will be sold while the female calves will be bred for six months and then transferred to the group of heifers. The sale of dairy cows is not one of the Group's principal activities and the proceeds are not included as revenue.

19. BIOLOGICAL ASSETS (continued)

(A) Nature of activities (continued)

The Group is exposed to a number of risks related to its biological assets. In addition to the financial risk disclosed in note 40, the Group is exposed to the following operation risks:

(i) Regulatory and environmental risks

The Group is subject to laws and regulations in the location in which it operates breeding. The Group has established environmental policies and procedures aimed at compliance with local environmental and other laws. Management performs regular reviews to identify environmental risks to ensure that the systems in place are adequate to manage these risks.

(ii) Climate, disease and other natural risks

The Group's biological assets are exposed to the risk of damage from climatic changes, diseases and other natural forces. The Group has extensive processes in place aimed at monitoring and mitigating those risks, including regular inspections, disease control, surveys and insurance.

The Group is exposed to fair value risks arising from changes in the price of the dairy products. The directors of the Company are of the view that there are no available derivative or other contracts which the Group can enter into to manage the risk of a decline in the price of the dairy products.

(B) Value of biological assets

The values of the Group's biological assets at each year end were:

	Heifers and calves	Milkable cows	Total
	RMB'000	RMB'000	RMB'000
December 31, 2016			
At January 1, 2016	925,641	2,359,795	3,285,436
Increase	308,830	—	308,830
Increase due to raising (feeding costs and others)	711,708	—	711,708
Transfer	(759,834)	759,834	—
Decrease	(85,577)	(320,411)	(405,988)
Gain/(loss) arising from changes in fair value less costs to sell	151,480	(167,209)	(15,729)
At December 31, 2016	1,252,248	2,632,009	3,884,257

19. BIOLOGICAL ASSETS (continued)

(B) Value of biological assets (continued)

	Heifers and calves	Milkable cows	Total
	RMB'000	RMB'000	RMB'000
December 31, 2015			
At January 1, 2015	945,030	1,775,096	2,720,126
Increase	102,082	—	102,082
Increase due to raising (feeding costs and others)	636,798	—	636,798
Transfer	(754,804)	754,804	—
Decrease	(74,503)	(151,789)	(226,292)
Gain/(loss) arising from changes in fair value less costs to sell	71,038	(18,316)	52,722
At December 31, 2015	925,641	2,359,795	3,285,436

Increases of the Group's biological assets include increase due to purchase and increase due to replacement, of which the increase due to replacement amounts to RMB293 million in 2016 (2015: RMB55 million).

The Group's dairy cows in the PRC were independently valued by Jones Lang LaSalle Corporate Appraisal and Advisory Limited ("**JLL**"), a firm of independent professional qualified valuers not connected with the Group, which has appropriate qualifications and recent experience in the valuation of biological assets.

(C) Fair value hierarchy

The Group uses the following hierarchy for determining and disclosing the fair values of biological assets:

Level 1 – based on quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2 – based on valuation techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly

Level 3 – based on valuation techniques for which any inputs which have a significant effect on the recorded fair value are not based on observable market data (unobservable inputs)

	Level 1	Level 2	Level 3	Total
	RMB'000	RMB'000	RMB'000	RMB'000
As at December 31, 2016	**—**	**—**	**3,884,257**	**3,884,257**
As at December 31, 2015	—	—	3,285,436	3,285,436

19. BIOLOGICAL ASSETS (continued)

(D) Description of valuation techniques used and key inputs to valuation on biological assets

The following table shows the valuation techniques used in the determination of fair values within Level 3 of the hierarchy, as well as the key unobservable inputs used in the valuation.

Type	Valuation approach	Key unobservable inputs	In-ter-relationship between key unobservable inputs and fair value measurements
Calves and heifers	The fair value of the heifers purchased within 6 months prior to each reporting date is determined with adjustment by adding the feeding costs from the purchase date to the reporting date. For the calves and the rest of the heifers, the fair value of 14-month-old heifers is determined by referring to the market price of the actively traded market. The fair values of the heifers over 14 months of age are determined by adding the breeding costs required to raise the heifers from 14 months old to the respective specific ages plus the estimated margins that would be required by a raiser. The fair values of the heifers under 14 months of age and the fair values of the calves are determined by subtracting the breeding costs required to raise the heifers or calves from the respective specific ages to 14 months old and the margins that would be required by a raiser.	Average market price of the heifers of 14 months of age: RMB19,503 to RMB20,500 for the year of 2016 (2015: RMB20,580 to RMB21,000).	The estimated fair value increases when the market price increases.

19. BIOLOGICAL ASSETS (continued)

(D) Description of valuation techniques used and key inputs to valuation on biological assets (continued)

Type	Valuation approach	Key unobservable inputs	In-ter-relationship between key unobservable inputs and fair value measurements
Milkable cows	The fair values of milkable cows are determined by using the multi-period excess earnings method, which is based on the discounted future cash flows to be generated by such milkable cows.	For the quantity of the milkable cows, assuming the number of the existing milkable cows as at the year end will decrease in the projection period at certain culling rates due to natural or unnatural factors, which include illness, difficult birth, low milk production or completion of all lactation periods. The estimated overall culling rate ranges from over 18% up to 100% along with the increase of the number of the lactation periods.	The estimated fair value decreases when the estimated culling rate increases.
	The calving interval (including dry period and open days) is estimated based on historical data and is assumed to be 400 days (each milkable cow will give birth to a calf every 400 days). This 400-day period is one lactation cycle in this valuation exercise.	A milkable cow could have as many as six to seven lactation periods. The estimated average raw milk production volume per head for lactation period ranges from 9.1 tonnes to 10.8 tonnes for the year of 2016 (2015: 9.0 tonnes to 10.6 tonnes) depending on the number of the lactation periods and the individual physical condition.	The estimated fair value increases when the estimated raw milk production volume increases.
		The estimated feed costs per kilogram of raw milk of the year 2016 range from RMB2.00 to RMB2.30 (2015:RMB2.19 to RMB2.51)	The estimated fair value decreases when the estimated feed costs per kilogram of raw milk increases.

19. BIOLOGICAL ASSETS (continued)

(D) Description of valuation techniques used and key inputs to valuation on biological assets (continued)

Type	Valuation approach	Key unobservable inputs	In-ter-relationship between key unobservable inputs and fair value measurements
		The estimated future local market prices for raw milk per tonne for the year of 2016 range from RMB3,960 to RMB5,000 per tonne (2015:RMB4,300 to RMB5,080 per tonne).	The estimated fair value increases when the estimated future local market price for raw milk increases.
		The discount rate is 14.00% for the year 2016 (2015: 14.00%), calculated by using the capital asset pricing model.	The estimated fair value decreases when the discount rate increases.

(E) Quantity of the agriculture produce produced by the Group's biological assets

	2016	2015
	Tonne	Tonne
Raw milk	598,379	537,300

(F) Gain arising on initial recognition of agricultural produce at fair value less cost to sell at the point of harvest

	2016	2015
	RMB'000	RMB'000
Raw milk	2,628,794	2,493,643

20. DEFERRED TAX

The movements in the deferred tax assets during the year are as follows:

	2016	2015
	RMB'000	RMB'000
At January 1	1,076	910
Credited to profit or loss during the year	23,558	166
At December 31	24,634	1,076

The principal components of the Group's deferred tax are as follows:

	2016	2015
	RMB'000	RMB'000
Accrued expenses	1,473	1,021
Impairment	3,535	55
Unrealised internal profits	19,626	—
	24,634	1,076

Pursuant to the PRC Corporate Income Tax Law, a 10% withholding tax is levied on dividends declared to foreign investors from the foreign investment enterprises established in Mainland China. The requirement is effective from January 1, 2008 and applies to earnings after December 31, 2007. A lower withholding tax rate may be applied if there is a tax treaty between Mainland China and the jurisdiction of the foreign investors. For the Group, the applicable rate is 5% or 10%. The Group is therefore liable for withholding taxes on dividends distributed by those subsidiaries established in Mainland China in respect of earnings generated from January 1, 2008.

At December 31, 2016, no (2015: Nil) deferred tax has been recognised for withholding taxes that would be payable on the unremitted earnings that are subject to withholding taxes of the Group's subsidiaries established in Mainland China. In the opinion of the directors, it is not probable that these subsidiaries will distribute such earnings in the foreseeable future. The aggregate amount of temporary differences associated with investments in subsidiaries in Mainland China for which deferred tax liabilities have not been recognised totalled approximately RMB3,409,542,000 at December 31, 2016 (2015: RMB2,575,995,000).

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

21. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

	2016	2015
	RMB'000	RMB'000
Prepayments	356,823	375,562
Deposits and other receivables	35,699	91,597
Prepaid expenses	12,991	16,987
	405,513	484,146
Non-current prepayments	(11,963)	(15,690)
Current portion	393,550	468,456

None of the above assets is either past due or impaired. The financial assets included in the above balances relate to receivables for which there was no recent history of default.

22. LONG TERM RECEIVABLES

	Contract amounts of long term receivables		Present value of long term receivables	
	2016	2015	2016	2015
	RMB'000	RMB'000	RMB'000	RMB'000
Within 1 year	3,200	—	2,289	—
1 to 2 years	3,200	—	2,402	—
2 to 5 years	9,600	—	7,934	—
Over 5 years	9,600	—	9,348	—
	25,600	—	21,973	—
Less: Uneamed finance income	(3,627)	—	N/A	N/A
Present value of long term receivables	21,973	—	21,973	
Portion classified as current assets under other receivables	(2,289)	—	(2,289)	—
Non-current portion	19,684	—	19,684	—

23. OTHER NON-CURRENT ASSETS

Other non-current assets mainly include deductible value added tax expected to be deducted after one year.

24. INVENTORIES

	2016	2015
	RMB'000	RMB'000
Consumables	35,867	32,339
Finished goods	47,908	16,023
Raw materials	845,041	776,152
	928,816	824,514

25. TRADE AND BILLS RECEIVABLES

	2016	2015
	RMB'000	RMB'000
Trade and bills receivables	1,194,299	915,681
Impairment	(85,512)	(369)
	1,108,787	915,312

The Group normally allows a credit limit or offer to its customers credit terms which are adjustable in certain circumstances. The Group closely monitors overdue balances. In view of the aforementioned and the fact that the Group's trade receivables relate to a large number of diversified customers, there is no significant concentration of credit risk. The Group does not hold any collateral or other credit enhancements over its trade receivables. The trade and bills receivables are non-interest-bearing.

An aging analysis of the trade and bills receivables as at the end of the reporting period, based on the invoice date and net of provision, is as follows:

	2016	2015
	RMB'000	RMB'000
Within 3 months	484,116	627,740
4 to 6 months	331,798	224,208
7 mouths to 1 year	268,863	60,042
Over 1 year	24,010	3,322
	1,108,787	915,312

25. TRADE AND BILLS RECEIVABLES (continued)

The movements in provision for impairment of trade receivables are as follows:

	2016	2015
	RMB'000	RMB'000
At beginning of year	369	—
Impairment losses recognised	86,310	369
Amount written off as uncollectible	(1,167)	—
	85,512	369

The aging analysis of the trade and bills receivables that are not individually nor collectively considered to be impaired is as follows:

	2016	2015
	RMB'000	RMB'000
Neither past due nor impaired	591,867	911,990

Receivables that were neither past due nor impaired relate to customers for whom there was no recent history of default.

26. CASH AND BANK BALANCE AND PLEDGED DEPOSITS

	2016	2015
	RMB'000	RMB'000
Cash and cash equivalents	932,382	1,411,499
Time deposits with original maturity of more than three months	115,000	320,260
Pledged deposits	66,791	70,277
	1,114,173	1,802,036
Less: Pledged deposits	(66,791)	(70,277)
Cash and bank balances	1,047,382	1,731,759

The Group's above balances were denominated in the following currencies as follows:

	2016	2015
	RMB'000	RMB'000
United States dollars	784	1,075
Hong Kong dollars	11,892	13,965
RMB	1,034,706	1,716,719
	1,047,382	1,731,759

26. CASH AND BANK BALANCE AND PLEDGED DEPOSITS (continued)

The RMB is not freely convertible into other currencies. However, under Mainland China's Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange RMB for other currencies through banks authorised to conduct foreign exchange business.

Cash at banks earns interest at the prevailing market interest rates. Time deposits are made for varying periods depending on the cash requirements of the Group and earn interest at the respective time deposit rates. The bank balances and pledged deposits are deposited with creditworthy banks with no recent history of default.

27. TRADE AND BILLS PAYABLES

An aging analysis of the trade payables of the Group, based on the invoice date, is as follows:

	2016	2015
	RMB'000	RMB'000
1 to 3 months	895,338	680,070
4 to 6 months	14,790	191,138
7 to 12 months	5,120	137,390
1 to 2 years	3,297	8,183
2 to 3 years	2,086	1,312
Over 3 years	—	33
	920,631	1,018,126

The trade payables are non-interest-bearing and are normally settled within 90-day terms.

28. OTHER PAYABLES AND ACCRUALS

	2016	2015
	RMB'000	RMB'000
Payables for purchases of dairy cows	15,045	15,460
Payables for taxes other than corporate income tax	15,365	2,234
Payables for third parties' deposits	23,896	42,970
Long term payables due within one year	23,900	—
Salary and welfare payables	37,702	30,562
Payables for purchases of transportation services	61,715	47,440
Payables for acquisition of items of property, plant and equipment	236,940	148,351
Others	23,987	51,276
	438,550	338,293

Other payables are non-interest-bearing and have an average term of 90 days.

29. INTEREST-BEARING BANK AND OTHER BORROWINGS

	2016			2015		
	Effective contract rate (%)	Maturity	RMB'000	Effective contract rate (%)	Maturity	RMB'000
Current						
Bank loans - unsecured	4.35-5.87	2017	853,000	4.79-7.14	2016	1,500,237
Bank loans - secured	4.35	2017	60,000	—	—	—
Current portion of long term bank and other borrowings - unsecured	1.55	2017	5,404	—	—	—
Short - term notes - unsecured			—	5.33	2016	99,618
			918,404			1,599,855
Non-current						
Bank loans - unsecured	1.55-5.23	2019-2024	160,427	5.25-7.04	2019	124,000
Domestic corporate bonds - unsecured	4.74-5.01	2018-2019	1,591,523	4.74	2018	993,000
			1,751,950			1,117,000
			2,670,354			2,716,855

	2016	2015
	RMB'000	RMB'000
Analysed into:		
Bank loans repayable:		
Within one year or on demand	918,404	1,500,237
In the second year	—	—
In the third to fifth years, inclusive	95,000	124,000
Beyond five years	65,427	—
	1,078,831	1,624,237
Other borrowings repayable:		
Within one year	—	99,618
In the second year	995,237	—
In the third to fifth years, inclusive	596,286	993,000
Beyond five years	—	—
	1,591,523	1,092,618
	2,670,354	2,716,855

29. INTEREST-BEARING BANK AND OTHER BORROWINGS (continued)

Notes:

(i) As at December 31 2016, substantially all of the Group's bank and other borrowings were denominated in RMB except for the interest-bearing bank loans of RMB70,831,000 which were denominated in Euro.

(ii) The domestic corporate bonds with an aggregate nominal amount of RMB1,000,000,000 were issued by Inner Mongolia Shengmu High-tech Farming Co., Ltd. (the "**Issuer**") to qualified investors on December 29, 2015 as approved by the China Securities Regulatory Commission. The domestic corporate bonds bear an annual interest rate of 4.48% and have a term of 5 years.

The domestic corporate bonds with an aggregate nominal amount of RMB 600,000,000 were issued by the Issuer to qualified investors on May 30, 2016 as approved by the China Securities Regulatory Commission. The domestic corporate bonds bear an annual interest rate of 4.75 % and have a term of 5 years.

The issuer has the right to adjust the interest rate of all the outstanding corporate bonds at the end of the first three year period. Upon exercise by the Issuer of such right, the holders of the bonds are entitled to sell all or any part of the outstanding corporate bonds held by them to the Issuer at the nominal amount.

(iii) As at December 31, 2016, the Group's bank loans of RMB 60,000,000 (2015:Nil) were secured by trade and bills receivables amounting to RMB 60,000,000, which have been discounted in advance but did not meet the requirements of derecognition.

30. LONG TERM PAYABLES

	Contract amounts of long term payments		Present value of long term payments	
	2016	2015	2016	2015
	RMB'000	RMB'000	RMB'000	RMB'000
Within 1 year	28,940	—	23,900	—
1 to 2 years	28,940	—	25,071	—
2 to 5 years	86,820	—	82,829	—
	144,700	—	131,800	—
Future finance charges	(12,900)	—	N/A	N/A
Present value of long term payables	131,800	—	131,800	—
Portion classified as current liabilities included in other payables	(23,900)	—	(23,900)	—
Non-current portion	107,900	—	107,900	—

31. SHARE CAPITAL

Shares

	2016	2015
	RMB'000	RMB'000
Authorised:		
30,000,000,000 ordinary shares of HK$0.00001 each (2015: 30,000,000,000 ordinary shares HK$0.00001 each)	236	236
Issued and fully paid:		
6,354,400,000 (2015: 6,354,400,000) ordinary shares	50	50

On May 13,2015, 611,620,800 shares representing approximately 9.63% of the issued share capital of the Company held by World Shining Investment Limited ("**World Shining**") were pledged to an independent third party as security for a loan provided by the said independent third party to World Shining. On May 19, 2016, the registered charge was released due to the repayment of the loan.

On October 21, 2016, some shareholders of the Company entered into a sale and purchase agreement with an independent third party, Inner Mongolia Yili Industrial Group Co., Ltd., ("**Yili**") to dispose of a total of 2,351,128,000 shares in the Company to Yili for an aggregate consideration of HK$5,290,038,000, representing HK$2.25 per share, which represented 37% of the total issued share capital of the Company as of the date of October 21, 2016. The transaction has not yet completed as at date of approval of these financial statements. Further details are set out in the Company's announcement dated November 02, 2016.

Share options

Details of the Company's share option scheme and the share options issued under the scheme are included in note 34 to the financial statements.

32. RESERVES

(i) Movements in components of equity

The amounts of the Group's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity of the financial statements.

(ii) Contributed surplus

The Group's contributed surplus represents the excess of the net assets value of the subsidiaries acquired by the Company over the nominal amount of the shares issued by the Company as consideration pursuant to the Reorganisation.

(iii) Reserve fund

In accordance with the relevant PRC laws and the articles of association of the PRC subsidiaries of the Group, the PRC subsidiaries are required to set up certain statutory reserves, which are non-distributable. The PRC statutory reserves can only be utilised for predetermined means upon approval by the relevant authority.

33. PARTLY-OWNED SUBSIDIARIES WITH MATERIAL NON-CONTROLLING INTERESTS

Details of the Group's subsidiary, that has material non-controlling interests, are set out below:

Shengmu Pangu	2016	2015
Percentage of equity interest held by non-controlling interests	45%	45%
Profit for the year allocated to non-controlling interests	53,566	53,192
Accumulated balances of non-controlling interests at the end of reporting period	217,785	164,219

The following tables illustrate the summarised financial information of Shengmu Pangu. The amounts disclosed are before any inter-company eliminations:

	2016	2015
	RMB'000	RMB'000
Revenue	241,861	231,713
Profit for the year	123,538	122,734
Total comprehensive income for the year	123,538	122,734
Current assets	262,484	200,968
Biological assets	299,979	236,325
Other non-current assets	122,655	101,352
Current liabilities	(119,026)	(79,974)
Non-current liabilities	(59,000)	(76,000)
Net cash flows from operating activities	174,849	69,671
Net cash flows used in investing activities	(84,549)	(41,299)
Net cash flows used in financing activities	(83,406)	(30,851)
Net increase/(decrease) in cash and cash equivalents	6,894	(2,479)

34. SHARE OPTION SCHEME

The Company has approved and adopted a pre-IPO share option scheme pursuant to the resolutions of the shareholders passed on April 30, 2014 (the "**Pre-IPO Share Option Scheme**"). The purpose of the Pre-IPO Share Option Scheme is to attract, retain and motivate the directors and senior management of the Group and Shengmu Forage, to provide a means to compensate them through the grant of options under the Pre-IPO Share Option Scheme for their contributions to the growth and profits of the Group, and to allow them to participate in the future growth and profitability of the Group. Participants of the Pre-IPO Share Option Scheme include (a) the executive directors, (b) senior management of the Group, (c) management of the subsidiaries of the Company, and (d) management of Shengmu Forage. The Pre-IPO Share Option Scheme became effective on April 30, 2014 and, unless otherwise cancelled or amended, will remain in force for 4 years from that date.

Prior to the listing date of the Company on The Main Board of The Stock Exchange of Hong Kong Limited (the "**Listing Date**"), options to subscribe for an aggregate of 504,480,000 shares have been conditionally granted to a total of 189 grantees under the Pre-IPO Share Option Scheme by the Company. The shares subject to the options granted under the Pre-IPO Share Option Scheme represent (i) approximately 7.94% of the Company's issued share capital as of December 31, 2016 (excluding any options granted under the Pre-IPO Share Option Scheme); and (ii) approximately 7.36% of the Company's issued share capital as of December 31, 2016, assuming that all options granted under the Pre-IPO Share Option Scheme have been exercised. Save for the options which have been granted before July 15, 2014, the Company's listing date on the Stock Exchange of Hong Kong Limited, no further options will be granted under the Pre-IPO Share Option Scheme on or after the Listing Date.

The offer of a grant of share options may be acceptable within 5 days from the date of offer, upon payment of a nominal consideration of HK$1 in total by the grantee. An option granted under the Pre-IPO Share Scheme shall lapse immediately if the grantee ceased employment with the Group or Shengmu Forage during the vesting period. The exercise period of the share options granted is determinable by the directors, and commences after a vesting period of one year and ends on a date which is not later than six months from the date of the vesting date.

On May 4, 2015, out of the 504,480,000 units of share options, 488,484,000 units of share options were vested to 181 grantees, meanwhile 15,996,000 units of share options lapsed as certain grantees ceased to be employees of the Group.

Pursuant to a resolution approved by the Company's shareholders at the extraordinary general meeting on November 3, 2015, the outstanding 488,484,000 units of share options relating to the Pre-IPO Share Option Scheme were amended as follows("**the Amendment**"):

34. SHARE OPTION SCHEME (continued)

(1) All the shares issued pursuant to the exercise of options during the Amended Exercise Period (as defined hereunder) would not be subject to any restriction applicable during the Lock-up Period (being the period from May 4, 2015 to May 4, 2017). Grantees are entitled to sell or otherwise dispose of any interest in the shares after they exercise the options during the Amended Exercise Period.

(2) The exercise period provided under the Pre-IPO Share Option Scheme (from May 4, 2015 to November 4, 2015) was changed to the "Amended Exercise Period" in the following manner:

Amended Exercise Period	Maximum percentage of options exercisable during the respective Amended Exercise Period
From May 4, 2016 to May 4, 2017	50% of the options vested
From November 4, 2016 to May 4, 2017	50% of the options vested

If the grantee ceased employment with the Group or Shengmu Forage before May 4, 2016, 100% of the options held by him/her would lapse immediately, and if the grantee ceased employment with the Group or Shengmu Forage on or after May 4, 2016 but before November 4, 2016, 50% of the options held by him/her would lapse immediately.

Apart from the above amendments, the other terms of the Pre-IPO Share Option Scheme remain the same.

The incremental fair value as a result of the Amendment was estimated to be RMB91,239,000 in total, using the measurement method as described below.

During the period from November 3, 2015 to December 31, 2015, 38,985,600 units of share options lapsed due to cessation of employment. During the year ended December 31, 2016, a further 40,662,600 units of share options lapsed due to cessation of employment.

The exercise price in respect of each option granted under the Pre-IPO Share Option Scheme is HK$1.56.

Share options do not confer rights on the holders to dividends or to vote at shareholders' meetings.

The following share options were outstanding under the Pre-IPO Share Option Scheme during the year:

2016

Date of grant	Exercise price HK$ per share	As at January 1, 2016	Granted during the year	Lapsed during the year	Exercised during the year	As at December 31 2016
April 30, 2014	**1.56**	**449,498,400**	**—**	**40,662,600**	**—**	**408,835,800**

2015

Date of grant	Exercise price HK$ per share	As at January 1, 2015	Granted during the year	Lapsed during the year	Exercised during the year	As at December 31 2015
April 30, 2014	1.56	504,480,000	—	54,981,600	—	449,498,400

34. SHARE OPTION SCHEME (continued)

The Group recognised a share option expense of HK$ 52,327,000 (equivalent to RMB 45,151,000) (2015: HK$33,211,000 (equivalent to RMB27,011,000)) during the year ended December 31, 2016.

The fair value of equity-settled share options amended in the year of 2015 was estimated as at the date of amendment, using a binomial model, taking into account the terms and conditions upon which the options were amended. The following table lists the inputs to the model used:

	2015
Dividend yield (%)	3.00
Expected volatility (%)	42.40
Risk-free interest rate (%)	0.27
Expected life of options (year)	1.5
Weighted average share price (HK$ per share)	1.69

The expected volatility reflects the assumption that the historical volatility of comparable companies is indicative of future trends, which may also not necessarily be the actual outcome. No other feature of the options granted/amended was incorporated into the measurement of fair value.

At the end of the reporting period, the Company had 408,835,800 share options outstanding under the Scheme. The exercise in full of the outstanding share options would, under the present capital structure of the Company, result in the issue of 408,835,800 additional ordinary shares of the Company and additional share capital of HK$4,089 and share premium of HK$637,779,759 (before issue expenses).

At the date of approval of these financial statements, the Company had 408,835,800 share options outstanding under the Pre-IPO Share Option Scheme, which represented approximately 6.43% of the Company's shares issued at that date.

35. OPERATING LEASE ARRANGEMENTS

As lessee

The Group leases from third parties certain office properties and dairy farms, including buildings and equipment under operating lease arrangements.

At the year end, the Group had total future minimum lease payments under non-cancellable operating leases falling due as follows:

	2016	2015
	RMB'000	RMB'000
Within one year	1,547	8,599
In the second to fifth years, inclusive	—	16,560
	1,547	25,159

36. COMMITMENTS

In addition to the operating lease commitments detailed in note 35 above, the Group had the following capital commitments at the year end:

	2016	2015
	RMB'000	RMB'000
Contracted, but not provided for:		
Plant and machinery	143,568	13,885
Land and buildings	208,984	187,322
	352,552	201,207

37. RELATED PARTY DISCLOSURES

(A) The Group had the following significant transactions with related parties

Name	Note	2016	2015
		RMB'000	RMB'000
Associates:			
Sales of products	(i)	983,296	651,612
Purchases of raw materials	(i)	507,918	443,063
Sales of raw materials	(i)	8,614	14,447
Affliates of a substantial shareholder:			
Purchases of raw materials	(i)	9,227	—

Note:

(i) The considerations were determined with reference to the then prevailing market prices/rates and the prices charged to third parties.

37. RELATED PARTY DISCLOSURES (continued)

(B) Other transactions with related parties

During the year, Shengmu Forage provided bio-waste (i.e., cow dung) cleaning services to the Group's dairy farms for free. Such services include collecting and cleaning unprocessed bio-waste from the Group's farms. In return, Shengmu Forage collected free unprocessed bio-waste from the Group's farms.

During the year and as of December 31, 2016, the Group provided guarantees with amounts of RMB 300,000,000 (2015: RMB 300,000,000) and RMB 51,450,000 (2015: Nil) for the bank loans of Shengmu Forage and Food Union Shengmu, respectively.

(C) Compensation of key management personnel of the Group

	2016	2015
	RMB'000	RMB'000
Short term employee benefits	1,783	1,654
Pension scheme contributions	44	47
	1,827	1,701

Further details of directors' and the chief executive's emoluments are included in note 9 to the financial statements.

(D) Outstanding balances with related parties

	2016	2015
	RMB'000	RMB'000
Amounts owed by/(owed to) associates included in:		
– Trade and bills receivables	671,104	439,289
– Trade and bills payables	(26,729)	(169,193)
– Prepayments, deposits and other receivables	250,567	336,466
– Other payables and accruals	(2,260)	(2,679)

Other than those balances included in trade receivables and trade payables, the above balances with related parties are unsecured, interest-free and have no fixed terms of repayment. Trade receivables and trade payables with related parties have similar credit terms to those offered by/to third parties.

38. FINANCIAL INSTRUMENTS BY CATEGORY

The carrying amounts of each of the categories of financial in-struments as at the end of the reporting period are as follows:

Financial assets

	2016	2015
	RMB'000	RMB'000
Loans and receivables:		
Long term receivables	19,684	—
Financial assets included in prepayments, deposits and other receivables	37,989	91,597
Pledged deposits	66,791	70,277
Cash and bank balances	1,047,382	1,731,759
Trade and bills receivables	1,108,787	915,312
	2,280,633	2,808,945
Available-for-sale financial assets:	121,427	1,404

Financial liabilities

	2016	2015
	RMB'000	RMB'000
Financial liabilities at amortised cost:		
Long term payables	107,900	—
Financial liabilities included in other payables and accruals	385,485	305,497
Trade and bills payables	920,631	1,018,126
Interest-bearing bank and other borrowings	2,670,354	2,716,855
	4,084,370	4,040,478

39. FAIR VALUE AND FAIR VALUE HIERARCHY OF FINANCIAL INSTRUMENTS

The carrying amounts and fair values of the Group's financial instruments, other than those with carrying amounts that reasonably approximate to the fair values, are as follows:

	Carrying amounts As at December 31		Fair values As at December 31	
	2016	2015	**2016**	2015
	RMB'000	RMB'000	**RMB'000**	RMB'000
Financial liabilities				
Interest-bearing bank and other borrowings	**2,670,354**	2,716,855	**2,727,672**	2,731,172

Management has assessed that the fair values of cash and cash equivalents, short term pledged deposits, trade and bills re-ceivables, trade and bills payables, financial assets included in prepayments, deposits and other receivables, financial liabilities included in other payables and accruals approximate to their carrying amounts largely due to the short term maturities of these instruments.

The fair values of the financial assets and liabilities are determined at the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

The following methods and assumptions were used to estimate the fair values:

The fair values of interest-bearing bank and other borrowings have been calculated by discounting the expected future cash flows using rates currently available for instruments with similar terms, credit risk and remaining maturities.

The fair values of the non-current portion of other financial assets, long-term pledged deposits, long-term time deposits, the non-current portion of interest-bearing bank loans and long term payables and other non-current financial liabilities have been calculated by discounting the expected future cash flows using rates currently available for instruments with similar terms, credit risk and remaining maturities.

39. FAIR VALUE AND FAIR VALUE HIERARCHY OF FINANCIAL INSTRUMENTS (continued)

The following table illustrates the fair value measurement hierarchy of the Group's financial instruments of which fair value is disclosed:

	Fair value measurement using significant unobservable inputs (Level 3)	
	2016	2015
	RMB'000	RMB'000
Interest-bearing bank and other borrowings	2,727,672	2,731,172

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments comprise interest-bearing bank and other borrowings, pledged deposits, and cash and cash balances. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets and liabilities such as trade and bills receivable and trade and bills payables, which arise directly from its operations.

The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk, credit risk and liquidity risk. The board of directors reviews and agrees policies for managing each of these risks and they are summarised below:

Interest rate risk

The Group is exposed to cash flow interest rate risk due to fluctuations in the prevailing market interest rates on cash and cash balances, and pledged bank deposits. Management considers that these bank balances are not sensitive to fluctuations in interest rates.

The Group's fair value interest rate risk relates primarily to variable-rate bank and other borrowings. The Group currently does not have an interest rate hedging policy. However, management monitors interest rate exposure and will consider hedging sig-nificant interest rate exposure should the need arise. The Group's interest rate profile set out in note 29.

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

Interest rate risk (continued)

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the Group's profit before tax through the impact on floating rate borrowings and the Group's equity.

	Increase/ (decrease) in basis points	Increase/ (decrease) in profit before tax	Increase/ (decrease) in equity*
		RMB'000	RMB'000
2016			
RMB	50	(3,121)	(3,121)
RMB	(50)	3,121	3,121
2015			
RMB	50	(1,919)	(1,919)
RMB	(50)	1,919	1,919

* Excluding retained profits

Foreign currency risk

The Group's businesses are principally located in Mainland China and substantially all transactions are conducted in RMB, except for the purchases of imported machinery and equipment. During the year, substantially all of the Group's assets and liabilities were denominated in RMB except that as at December 31, 2016, cash and bank balances of approximately RMB784,000 (2015: RMB1,075,000) and RMB11,892,000 (2015: RMB13,965,000) were denominated in United States dollars ("**USD**") and Hong Kong dollars ("**HK$**"), respectively, the interest-bearing bank and other borrowings of approximately RMB70,831,000 (2015: Nil) were denominated in Euro, respectively. The fluctuations of the exchange rates of RMB against foreign currencies could slightly affect the Group's results of operations.

The following table demonstrates the sensitivity to a reasonably possible change in the HK$ exchange rate (2015: USD exchange rate) with all other variables held constant, of the Group's profit before tax (due to changes in the fair value of monetary assets and liabilities):

	Increase/(decrease) in rate	Increase/(decrease) in profit before tax
	%	RMB'000
2016	5%	3,444
	(5%)	(3,444)
2015	5%	33
	(5%)	(33)

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

Credit risk

The Group trades only with recognised and creditworthy third parties. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis and the Group's exposure to bad debts is not significant.

Credit risk of the Group's other financial assets, which comprise cash and bank balances, and other receivables, arises from default of the counterparty with a maximum exposure equal to the carrying amounts of these instruments.

Since the Group trades only with recognised and creditworthy third parties, there is no requirement for collateral.

There were no significant concentrations of credit risk within the Group as the customer bases of the Group's trade receivables were widely dispersed as at December 31, 2016 and 2015.

Further quantitative data in respect of the Group's exposure to credit risk arising from trade and bills receivables are disclosed in note 25 to the financial statements.

Liquidity risk

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of bank and other borrowings and projected cash flows from operations.

The table below summarises the maturity profile of the Group's financial liabilities as at the end of the reporting period, based on contractual undiscounted payments.

	On demand	Less than 1 year	1 to 5 years	Total
	RMB'000	RMB'000	RMB'000	RMB'000
2016				
Long term payables	—	28,940	115,760	144,700
Financial liabilities included in other payables and accruals	385,485	—	—	385,485
Trade and bills payables	920,631	—	—	920,631
Interest-bearing bank and other borrowings	—	931,314	1,941,056	2,872,370
	1,306,116	960,254	2,056,816	4,323,186
2015				
Financial liabilities included in other payables and accruals	305,497	—	—	305,497
Trade and bills payables	1,018,126	—	—	1,018,126
Interest-bearing bank and other borrowings	—	1,636,509	1,286,889	2,923,398
	1,323,623	1,636,509	1,286,889	4,247,021

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

Capital management

The primary objectives of the Group's capital management are to safeguard the Group's ability to continue as a going concern and to maintain healthy capital ratios in order to support its business and maximise shareholders' value.

The Group manages its capital structure and makes adjustment to it in light of changes in economic conditions and the risk charac-teristics of the underlying assets. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders or issue new shares. No changes were made to the objectives, policies or processes for managing capital during the year.

The Group monitors capital using a gearing ratio, which is total debt divided by the total capital. Total debt includes interest-bearing bank and other borrowings. Total capital is the equity as shown in the consolidated statement of financial position. The Group's policy is to maintain a healthy gearing ratio. The gearing ratios at the end of the reporting periods were as follows:

	2016	2015
	RMB'000	RMB'000
Interest-bearing bank and other borrowings	2,670,354	2,716,855
Total equity	6,347,127	5,367,225
Gearing ratio	42.1%	50.6%

41. STATEMENT OF FINANCIAL POSITION OF THE COMPANY

Information about the statement of financial position of the Company at the end of the reporting period is as follows:

	December 31 2016	December 31 2015
	RMB'000	RMB'000
NON-CURRENT ASSETS		
Other intangible assets	—	21
Investments in subsidiaries	216,730	229,434
Due from subsidiaries	3,178,949	2,679,757
Total non-current assets	3,395,679	2,909,212
CURRENT ASSETS		
Prepayments, deposits and other receivables	2,630	2,648
Cash and cash equivalents	12,492	14,595
Due from subsidiaries	121,510	310,969
Total current assets	136,632	328,212
CURRENT LIABILITIES		
Other payables and accruals	(2,683)	—
Total current liabilities	(2,683)	—
NET CURRENT ASSETS	133,949	328,212
TOTAL ASSETS LESS CURRENT LIABILITIES	3,529,628	3,237,424
NON-CURRENT LIABILITIES		
Interest-bearing bank borrowings	(70,831)	—
Total non-current liabilities	(70,831)	—
Net assets	3,458,797	3,237,424
EQUITY		
Share capital	50	50
Reserves (note)	3,458,747	3,237,374
Total equity	3,458,797	3,237,424

41. STATEMENT OF FINANCIAL POSITION OF THE COMPANY (continued)

Note:

A summary of the Company's reserves is as follows:

	Share premium account	Share option reserve	Accumulated losses	Exchange fluctuation reserve	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
At January 1, 2015	3,024,937	23,396	(44,827)	(13,002)	2,990,504
Profit for the year	—	—	34,604	—	34,604
Other comprehensive income	—	—	—	185,255	185,255
Total comprehensive income for the year	—	—	34,604	185,255	219,859
Equity-settled share option arrangement	—	27,011	—	—	27,011
At December 31, 2015	3,024,937	50,407	(10,223)	172,253	3,237,374
Profit for the year	—	—	(178)	—	(178)
Other comprehensive income	—	—	—	214,693	214,693
Total comprehensive income for the year	—	—	(178)	214,693	214,515
Equity-settled share option arrangement	—	6,858	—	—	6,858
At December 31, 2016	3,024,937	57,265	(10,401)	386,946	3,458,747

The share option reserve comprises the fair value of share options granted which are yet to be exercised, as further explained in the accounting policy for share-based payments in note 2.4 to the financial statements. The amount will either be transferred to the share premium account when the related options are exercised, or be transferred to retained profits should the related options expire or be forfeited.

42. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on March 20, 2017.

FINANCIAL SUMMARY

Below is the summary of audited financial statement of the Group for the relevant years:

Unit: RMB in thousand	For the year ended December 31,				
	2016	2015	2014	2013	2012
Revenue	**3,466,544**	3,100,711	2,132,428	1,143,709	700,763
Profit for the year	**956,808**	1,083,222	883,808	374,498	198,903
Of which: profits attributable to the owners of the parent	**680,615**	800,652	711,228	327,309	195,782
Earnings per share attributable to ordinary equity holders of the parent:					
Basic	**RMB0.107**	RMB0.126	RMB 0.118	RMB0.075	—
Diluted	**RMB0.106**	RMB0.124	RMB 0.116	RMB0.075	—

	As at December 31,				
	2016	2015	2014	2013	2012
Total assets	**10,499,295**	9,459,793	6,491,244	3,112,608	1,816,728
Total liabilities	**4,152,168**	4,092,568	2,236,145	1,404,716	598,259
Net assets	**6,347,127**	5,367,225	4,255,099	1,707,892	1,218,469
Of which: equity attributable to the owner of the parent:	**5,339,039**	4,551,655	3,721,898	1,494,160	1,166,851