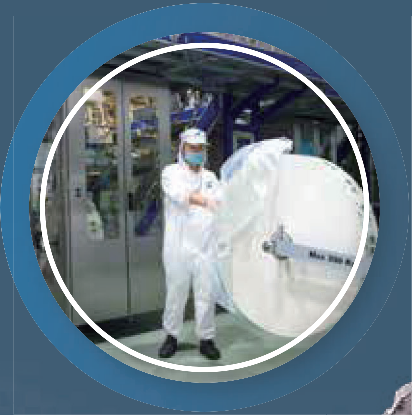
CHINA SHENGMU ORGANIC MILK LIMITED
中國聖牧有機奶業有限公司

(Incorporated in the Cayman Islands with limited liability)
Stock Code: 1432



2018
ANNUAL REPORT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ORGANIC MILK
圣牧|全程有机
ORGANIC MILK
圣牧|全程有机
有机纯牛奶
有机酸牛奶
ORGANIC MILK
有机纯牛奶
ORGANIC

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CORPORATE INFORMATION

BOARD OF DIRECTORS

Executive Directors

Mr. YAO Tongshan
Mr. WU Jianye
Mr. ZHANG Jiawang *(Chief Executive Officer)*[note]

Non-executive Directors

Mr. SHAO Genhuo *(Chairman)*
Mr. WEN Yongping
Mr. SUN Qian

Independent Non-executive Directors

Mr. FU Wenge
Mr. WANG Liyan
Mr. LI Xuan

JOINT COMPANY SECRETARIES

Mr. WU Jianye
Mr. AU Wai Keung

AUTHORISED REPRESENTATIVES

Mr. WU Jianye
Mr. AU Wai Keung

AUDIT COMMITTEE

Mr. WANG Liyan *(Chairman)*
Mr. FU Wenge
Mr. LI Xuan

REMUNERATION COMMITTEE

Mr. LI Xuan *(Chairman)*
Mr. SUN Qian
Mr. FU Wenge

NOMINATION COMMITTEE

Mr. FU Wenge *(Chairman)*
Mr. SHAO Genhuo
Mr. YAO Tongshan
Mr. LI Xuan
Mr. WANG Liyan

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

Note: Mr. ZHANG Jiawang was appointed as the executive Director of the Company on January 25, 2019, and has been appointed as the Chief Executive Officer of the Company since January 16, 2019.

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)
Baoshang Bank Co., Ltd. (Hohhot Branch)
Hengfeng Bank Co., Ltd. (Xi'an Branch)

AUDITOR

Ernst & Young

LEGAL ADVISOR

As to Hong Kong Law

Linklaters

As to Cayman Islands Law

Maples and Calder

WEBSITE

http://www.youjimilk.com

LOCATION MAP OF ORGANIC PRODUCTION BASE

SHAO GENHUO

Chairman

Dear Shareholders,

I, hereby on behalf of the board of the Company, present the annual report of the Company and its subsidiaries for the year ended December 31, 2018.

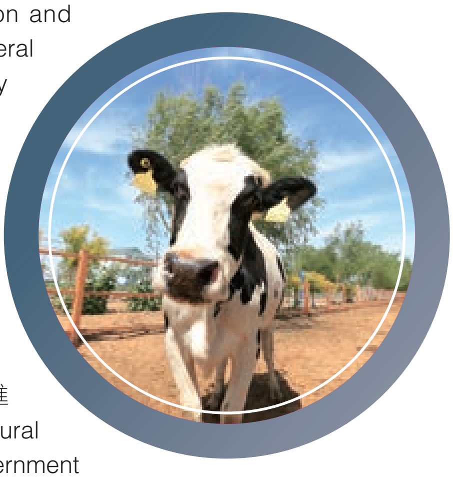
In 2018, the farming business, the upstream of the dairy industry, continued to be sluggish. Affected by the environment of the industry, China Shengmu has witnessed a decline in its operating results during the year. In the face of the complicated, severe, and challenging industrial landscape, China Shengmu improved the market awareness and reputation to some extent with respect to "Shengmu" brand by leveraging on its safe and quality desert-based grass-to-glass organic raw milk based on its unique "desert-based grass-to-glass organic production model", optimized and innovative marketing strategy, the establishment of new mode channels, upgraded product images in all respects, and improving brand building.

In light of the intense competition faced by the dairy industry in China and for the purpose of ensuring sustainable and sound development for the Group's dairy business, the Company has promptly adjusted its strategy to focus on the dairy farming business with establishing a safe base for milk sources and producing high quality organic milk as its core. An agreement was entered into between the Group and Mengniu Group to dispose 51% of its equity interests in the down-stream liquid milk business. Meanwhile, another agreement was also entered into to acquire minority interest in 12 farms located at the Ulan Buh Desert, the core area of the whole-process organic industry system in the desert. Riding cooperation with Mengniu, the Company has been able to obtain harmonious development in its dairy business, while supplementing its demand for working capital efficiently. In addition, the Company has also consolidated high-quality assets in the upstream of dairy farming business, and devoted further efforts to dairy farming business and raw milk business capitalizing on its valuable experience accumulated and advantages of barrier in the whole-process organic industry system in the desert, which has contributed to sustainable development of the Company in the long run.

MANAGEMENT DISCUSSION AND ANALYSIS

MARKET OVERVIEW

The dairy industry is an indispensable industry for healthy China and strong nations, a representative industry for safety of food, an iconic industry for modernization of agriculture, and a strategic industry for coordinated development of primary, secondary and tertiary industries. Currently, China's dairy industry is in a new stage of development and revitalization, achieving the historical highest level in terms of the dairy quality and the product safety.



In June 2018, in the "Comments on Promotion of Dairy Industry Revitalization and Protection of Quality Safety of Dairy Products" (the "**Comments**") issued by General Office of the State Council, comprehensive deployment to expedite dairy industry revitalization was introduced again. This will be beneficial for the overall improvement of the industry. Under the "Comments", by 2020, the percentage of domestic dairy farms with 100 or more cows should be more than 65% and the rate of self-supplying milk source should be maintained at more than 70%. By 2025, the dairy industry will revitalize in all respects with modernization basically achieved as well as bases for milk sources, product processing, quality of dairy products and industrial competitiveness achieving the global leading level in their entirety. In December 2018, "Certain Opinions on Further Promoting Prosperous Development of the Dairy Industry" (《關於進一步促進奶業振興的若干意見》) was jointly issued by the Ministry of Agriculture and Rural Affairs, the National Development and Reform Commission and other seven government ministries and commissions. It is proposed therein that, targeting to achieve overall prosperous development of the dairy industry, the government strives to realize an output of milk products up to 45.0 million tonnes nationwide by 2025 by optimizing the production layout of dairy industry and innovating the development way of dairy industry, so as to pragmatically boost the development quality, efficiency and competitiveness of the dairy industry in China. In China's No.1 Central Document in 2019, i.e. "Certain Opinions of Central Committee of the Communist Party of China and the State Council on Prioritizing the Development of Agriculture and Rural Areas and Providing Comprehensive Services for 'Agriculture, Rural Areas and Farmers'" (《中共中央國務院關於堅持農業農村優先發展做好"三農"工作的若干意見》), a further request was made on prosperous development of the dairy industry that "the government shall take steps for prosperous development of the dairy industry by intensifying the construction of high-quality milk source bases".

Looking back to 2018, the upstream farming enterprises still faced continuous pressure and the imbalanced development of farming and processing was still a severe problem. Against backdrop of this, in the 2018 China Top 20 Dairy Enterprises (D20) Summit held in Hulun Buir in September, a consensus has been reached in the industry in relation to benefits linkage between the upstream and downstream enterprises of the dairy industry and support from the downstream enterprises to the upstream enterprises. Under the leadership of the D20 enterprises, quality of raw milk in China constantly improved and harmonious development in industry was further promoted.

As the economy continues to develop, the average per capita consumption will increase continuously. Against such background, the market of the dairy product industry will increase in size and continue to mature and China will become the largest potential market worldwide in terms of the consumption of dairy products. At the same time, this will also spur further increase in the production of the dairy products in the PRC.

BUSINESS REVIEW

In 2018, the business of the Group comprised of dairy farming business and liquid milk business.

Shengmu is located in the Ulan Buh Desert, Inner Mongolia, a place formed by the alluviation of ancient channels of Yellow River for a thousand years, natural and unpolluted. The pure and untraveled desert environment forms a natural protection of Shengmu's base for milk sources as the desert keeps away external pollution and viruses as an effective isolation. Shengmu has implemented ecological development in the Ulan Buh Desert for many years. Shengmu has constantly planted trees and grass in the Ulan Buh Desert by using water from the Yellow River and cow dung as fertilizer and transformed desert ecological environment for over 200,000 mu while providing dairy cows with adequate and natural organic forage grass. The combination of planting and farming forms a natural and harmonious organic cycle. Shengmu has built many farms in the hinterland of the Ulan Buh Desert which have passed the organic standards of EU. Dairy cows live well in the natural and organic environment with low density, enjoying pure water, sunshine and organic grass. Shengmu respects the nature of animals, ensures the pure quality of milk sources and passes ECOCERT.

In 2018, the Company proposed internally to accelerate building of the corporate culture, brand, bases, cooperative partners and team. By exporting corporate culture, inspiration of career, strict training, the Company strives to create a great team; by conducting high-end pricing and adhering to the principle of "price and mark, first and exclusive", it strives to make its cooperative partners stronger, and share benefits with and achieve mutual success with them. In 2018, revenue of the Group reached RMB2.89 billion with a gross profit of RMB0.94 billion, of which, revenue from self-owned brand grass-to-glass organic liquid milk reached RMB0.79 billion, accounting for 27.3% of the revenue of the Group.

HIGH QUALITY, HIGH BRAND, HIGH PRICE, HIGH QUALITY TEAM AND HIGH-END CHANNELS

Focusing on high quality, Shengmu creates Shengmu grass-to-glass organic milk containing milk protein>=3.5g/100mL by fully taking the natural organic advantages of desert. This product has passed both the China Organic Food Certification and ECOCERT and was awarded the Gold Medal of Shanghai International Organic Food Expo for seven years consecutively.

Price is the best icon for a brand. Shengmu has strictly implemented the policy of high price in 2018 and ceased all low price promotion activities. Retail prices were increased at the same time to boost customers' confidence in cooperation and achieve win-win situation. Shengmu has presence in various national key chain shopping malls such as RT-Mart, Yonghui, METRO, Auchan, and Walmart, and achieved good sales results.

In 2018, the Company has developed 63 new base markets and 328 new business partners in total. Based on the trial in Haining market, a set of replicable codes for construction of a base has been concluded: model, brand and efficiency. Under the premise of adhering to adopting uniform price set by the Company, targeting to make sales to 1% of local total population, a team consisting of 3 to 5 persons will be established to enter base market and rapidly improve the presentation of products in the market together with business partners in 2 to 3 months to achieve No. 1 presentation of resources. Through promotion, Shengmu will create the best brand image and achieve good operations.

Throughout the year of 2018, Shengmu sold a total of 4.822 million sets of products through the Yunji platform on an accumulative basis. During the current year, Shengmu maintained active and good cooperation with Yunji and achieved daily presentation of all resources on the platform. They also achieved excellent results in brand linkage, including development of Yunji customized sets, development of Yunji proprietary farms, and Yunji SGS Quality 500 Certification, etc.. Shengmu will be recognized and accepted by more consumers through in-depth cooperation with Yunji platform.

Shengmu and JD.COM entered into strategic cooperation in January 2018 and jointly launched 3 JOY customized sets in May. In June, Shengmu's proprietary farm for JD.COM was established. The brand tracking team of JD.COM visited Shengmu's base in Dengkou with over ten media correspondents. The whole process was broadcast live online and viewed by more than 1 million times on an accumulative basis.

The Company established a regional office in the second year of cooperating with Easy Joy under Sinopec so as to facilitate communications with customers and handle feedback problems in time. The Company has implemented shop visits to understand the sales condition in terminal shops in a rapid and accurate way and formed a sales model of normal orders. An accumulation of approximately 1.23 million sets were sold in 2018.

ORGANIC FORAGE

Through many years of dedicated investment in the Ulan Buh Desert, Shengmu Forage has currently built an organic forage base of over 200,000 mu. Shengmu Forage has built an organic fertilizer processing plants with an annual capacity of 70,000 tons and 6 liquid fertilizer plants. It has installed 328 fertilizing systems of organic liquid fertilizer for the planting base and built 9 cow dung processing plants with annual capacity of 250,000 cubic meters for the farm. Shengmu Forage has currently been capable of guaranteeing the demand of organic forage planting for fertilizer. It has established a complete management system for planting organic forage, paving solid foundation for the development model of organic chain.

Corporate standard quality management systems "Organic Forage" and "Organic Grass" have been established and fully implemented by Shengmu Forage to further establish an industrial standard. Through standardization of planting management, grass-to-glass organic tracking, and organic product quality, Shengmu Forage has passed organic certification from authorized institutions within and outside the country for seven years consecutively and become the demonstration base for domestic large-scale organic planting industry.

ORGANIC FARMING

The Group takes the organic approach to management as its key priority. The Company has launched a stringent audit process for its products, focusing on internal audit in an organic approach to ensure the operation of each process along the industry chain is in compliance with the China organic standards of GB/T19630-2011 and the EU organic standards of EC834-2007.

In order to complement informatization management, the Group is committed to the refined management of nutrition and feeding, including but not limited to the formula management, feeding accuracy and efficiency comparison. It also upgrades Copartner (科派騰系統) and TMR from time to time and oversees the overall TMR process for the avoidance of man-made mistakes during the process of dosing and feeding. Control of feed formula and feeding accuracy at an ideal level allows the Group to trace back to the initial formula design, subsequent compound production and final feeding.

In respect of nutrition and feeding, the grass catchers are equipped with GPS to monitor the operation of mowers, improve minor aspects of on-site management and increase the intake of dry matters by the dairy cows. Advanced equipment, including thermal imager, anemograph and humiture meter, are used to determine the possibility of secondary fermentation for forage and reasonableness of the position and direction of fans and to monitor the cow barn environment to reduce the effect of heat stress on the dairy cows. Besides, upgrade of formula of fermentation material, cost control and new production process including silage wrapping and clyster are also adopted by the Group to improve the quality of raw material, strengthen the refined management of source, process and site, boost feed efficiency and maximize profit.

ADJUSTING STRATEGY TO FOCUS ON THE UPSTREAM AND BUILD SAFE MILK SOURCE BASE THROUGH EFFORTS IN THE FUTURE

In view of the intense competition in the dairy industry, our Group has devoted significant resources to secure sound development of the dairy industry over the past years. During the year, the Company has promptly adjusted its strategy to focus on the dairy farming business with establishing a safe base for milk sources and producing high quality organic milk as its core principle. An agreement was entered in to between the Group and Mengniu Group to dispose 51% of its equity interests in the down-stream liquid milk business. Meanwhile, another agreement was also entered into to acquire minority interests in 12 farms located at the Ulan Buh Desert, the core area of the whole-process organic industry system in the desert. By cooperating with Mengniu, the Company has been able to obtain harmonious development in its dairy business, while supplementing its demand for working capital efficiently. In addition, the Company has also consolidated high-quality assets in the upstream of dairy farming business, and devoted further efforts to dairy farming business and raw milk business capitalizing on its valuable experience accumulated and taking advantages of barrier of the whole-process organic industry system in the desert, which has contributed to sustainable development of the Company in the long run.

FINANCIAL REVIEW

In 2018, the Group's revenue increased by 6.7% from RMB2,706.8 million in 2017 to RMB2,887.2 million. Gross profit of the Group decreased by 13.2% from RMB1,083.0 million in 2017 to RMB939.6 million in 2018. Loss attributable to owners of the parent increased from RMB1,015.3 million in 2017 to RMB2,225.2 million in 2018.

As at December 23, 2018, a share purchase agreement was entered into between Mengniu Group and the Group. As at this reporting date, closing of the share purchase agreement has not taken place. The Group disposed 51% of its holding shares in the dairy business (Inner Mongolia Shengmu High-tech Dairy Co., Ltd. and Hohhot Shengmu High-tech Dairy Co., Ltd., being the liquid milk processing business segment of the Group, hereinafter referred to as the "**dairy business**") to Mengniu Group. According to the requirements under the IFRSs, the dairy business is stated as a held-for-sale business. With the exception of the dairy business, other businesses of the Group (hereinafter referred to as the "**farming business**") are stated as continuing operations.

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 [3]				
For the year ended December 31,	Segment revenue	Inter-segment sales[2]	External sales	External sales as % of total revenue	Segment revenue	Inter-segment sales	External sales	External sales as % of total revenue	Total revenue
2018	**2,404,084**	**356,340**	**2,047,744**	**70.9%**	**839,423**	**—**	**839,423**	**29.1%**	**2,887,167**
2017	2,502,230	1,223,040	1,279,190	47.3%	1,439,172	11,520	1,427,652	52.7%	2,706,842

(1) The dairy business is still presented as the downstream business of the entire industrial chain instead of business held for sale during the current and prior years in this table and tables below. Such presentation can reflect and analyze the operating condition and changes of the Group for the current and prior years more reasonably.

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

(3) Liquid milk business includes the dairy business and the milk powder business.

Given the rising competition existing in the dairy products market, the Group required the market terminals to stabilize prices globally, to strictly implement the strategy of high price, cease all low price promotion activities, and increase uniform retail prices, so as to improve the brand image of Shengmu, boost customers' confidence in cooperation, and achieve win-win situation. As such, the Group proactively adapted the sales structure of its upstream and downstream products and optimized the quality of sales outstanding of the Group. On the basis of ensuring the effective operation of its self-owned brand organic liquid milk, the Group expanded the sales of raw milk to clients in the industry. Sales of the Group's raw milk increased from RMB1,279.2 million in 2017 to RMB2,047.7 million in 2018, representing an increase of 60.1% as compared to the same period of last year. Sales of self-owned brand liquid milk decreased from RMB1,427.7 million in 2017 to RMB839.4 million in 2018, representing a decrease of approximately 41.2% as compared to the same period last year.

Dairy farming business

	For the year ended December 31,							
	2018				2017			
	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	1,051,283	287,066	3,662	43.8%	815,492	211,027	3,864	32.6%
Inter-segment sales(1)	325,211	76,234	4,266	13.5%	1,167,334	222,755	5,240	46.6%
Subtotal	1,376,494	363,300	3,789	57.3%	1,982,826	433,782	4,571	79.2%
Premium non-organic raw milk								
External sales	996,461	282,772	3,524	41.4%	463,698	137,412	3,375	18.6%
Inter-segment sales(2)	31,129	9,222	3,375	1.3%	55,706	14,736	3,780	2.2%
Subtotal	1,027,590	291,994	3,519	42.7%	519,404	152,148	3,414	20.8%
Daily farming segment	2,404,084	655,294	3,669	100.0%	2,502,230	585,930	4,271	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.

In 2018, sales volume of raw milk increased by 11.8% from 585,930 tonnes in 2017 to 655,294 tonnes in 2018. Leveraging on its sound cooperation relationship with clients in the industry, the Group expanded the sales of raw milk to its clients in the industry. The external sales volume accounted for 87.0% of sales volume of raw milk in 2018, compared to 59.5% in 2017. Affected by (1) supply and demand factors in the dairy industry, some organic raw milk were sold at a proper lower price to the industry clients, as a result, selling price of the overall organic raw milk decreased by 17.1% from RMB4,571/tonne in 2017 to RMB3,789/tonne in 2018; and (2) the Group's adjustment of deployment of dairy farming business, some organic farms no longer held organic certification. The decrease in the number of organic farms resulted in the change in the production structure of organic and non-organic raw milk in the second half of the year and the selling price of non-organic raw milk declined more significantly as compared to that of organic raw milk, as a result, revenue from the daily farming segment decreased from RMB2,502.2 million in 2017 to RMB2,404.1 million in 2018.

Liquid milk business

Due to implementation of the Group's market strategy of "sales-oriented production for end product freshness" (以銷定產，保證終端產品的新鮮度), revenue from the Group's liquid milk business decreased by 41.2% from RMB1,427.7 million in 2017 to RMB839.4 million in 2018. Revenue from liquid milk business accounted for 29.1% of total revenue of the Group in 2018, a significant decrease from 52.7% in 2017. Despite a significant decrease in sales volume of liquid milk products, unit selling price of liquid milk products improved notably as compared to 2017 and quality of sales outstanding also improved significantly, showing the effect of new market strategy.

Organic liquid milk business

	For the year ended December 31,		
	2018	2017	Increase/ (Decrease)
Revenue (RMB'000)	**786,960**	1,400,277	(43.8%)
Sales volume (Tonnes)	**68,219**	145,949	(53.3%)
Average selling price (RMB/Tonne)	**11,536**	9,594	20.2%

Cost of Sales, Gross Profit and Gross Margin

Cost of sales of the Group increased from RMB1,623.8 million in 2017 to RMB1,947.6 million in 2018. Gross profit decreased from RMB1,083.0 million in 2017 to RMB939.6 million in 2018. Gross profit margin decreased from 40.0% in 2017 to 32.5% in 2018. As (1) the Group adjusted the product sales structure as a result of adjustment of operating strategy, which led to an obvious decrease in the sales of grass-to-glass organic liquid milk which has a high gross profit; (2) affected by factors including organic raw milk supply and demand, the unit price of external sales of organic raw milk decreased significantly; and (3) the Group adjusted its deployment of dairy farming business, which led to an obvious decrease in the sales volume of organic raw milk with relative high gross profit, cost of sales of the Group in 2018 increased by 19.9% from 2017 and gross profit of the Group in 2018 decreased by 13.2% from 2017.

Other Income and Gains/(Losses) and Impairment Losses on Financial and Contract Assets (Note)

Other income and losses and impairment losses on financial and contract assets of the Group increased from net losses of RMB724.0 million in 2017 to net losses of RMB1,176.3 million in 2018, mainly attributable to the provision for impairment of trade receivables and other receivables referring to the recoverability of individual account receivables and other receivables using expected credit loss approach by the liquid milk business of Group.

Of which, other income and gains/(losses) and impairment losses on financial and contract assets of the farming business increased from net losses of RMB13.6 million in 2017 to net losses of RMB78.8 million in 2018, mainly attributable to the fact that an impairment loss of the dairy farming business was recognized in respect of the guarantee for the bank loans of Shengmu Forage, an associated company in 2018.

Note: Effective from 1 January 2018, impairment losses on financial and contractual assets are separately stated in the consolidated statement of profit or loss and other comprehensive income, while in 2017, impairment losses on assets were included in other income and losses in the consolidated statement of profit or loss and other comprehensive income. For the purpose of consistent analysis, other income and gains/(losses) and the impairment losses on financial and contractual assets are aggregated.

Selling and Distribution Expenses

Selling and distribution expenses of the Group primarily include logistics and transportation expenses, warehouse fees and relevant employees' remunerations. In 2018 and 2017, selling and distributing expenses of the Group amounted to RMB341.1 million and RMB354.4 million, respectively. The sales volume of liquid milk in 2018 declined significantly as compared to 2017. The less decrease in selling and distribution expenses was mainly attributable to the increase in the promotion expenses of liquid milk terminal market by the Group to implement the market strategy.

Of which, selling and distribution expenses of farming business were mainly logistics and transportation expenses. Selling and distribution expenses increased by approximately 82.6% from RMB34.9 million in 2017 to RMB63.7 million in 2018, mainly attributable to (1) obvious increase in the sales volume of raw milk by 11.8% from 585,930 tonnes in 2017 to 655,294 tonnes in 2018, and (2) great change in the external and internal sales structure of sale volumes of raw milk, i.e., external sales volume increased by approximately 63.5% from 348,439 tonnes in 2017 to 569,838 tonnes. As a result, costs of logistics and transportation increased significantly as compared to last year.

Administrative Expenses

Administrative expenses mainly include salary and welfare, travel expenses and transportation expenses of management and administrative employees. In 2018 and 2017, administrative expenses of the Group increased, accounting for 5.3% and 3.8% of revenue respectively. Administrative expenses in the current year increased substantially as compared to the prior year, which was mainly attributable to the damage of inventories and obviously increase in the intermediary expenses arising from transactions such as disposal of liquid milk business during the current year.

Of which, in 2018 and 2017, administrative expenses of farming business increased, accounted for 5.5% and 4.1% of revenue respectively, which was mainly attributable to the damage of inventories during the current year.

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 becomes 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.

In 2018 and 2017, the Group's net losses arising from changes in fair value less costs to sell of biological assets were RMB1,321.6 million and RMB595.5 million respectively. The significant increase in net loss from changes in fair value less costs to sell of biological assets of the Group from 2018 to 2017 was mainly attributable to the combined effects of (1) the Group's control over its cow numbers in response to the weak demand for raw milk in the market, and (2) the sharp decline of raw milk price.

Share of Profits and Losses of Associates

The Group's associates 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; (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 produces dairy products with the raw milk to be purchased by it from the Group. In 2018 and 2017, the Group recorded share of losses of associates of RMB15.6 million and RMB6.9 million, respectively.

Of which, in 2018 and 2017, the farming business recorded share of losses of associates of RMB15.2 million and RMB2.9 million, respectively.

Income Tax Credit/(Expense)

All profits of the Group were 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 (Cai Shui [2011] No.58) (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》(財稅 [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 expense of the Group was RMB27.9 million in 2018 while income tax credit was RMB7.5 million in 2017. Income tax expense of the Group in 2018 was due to the reversal of deferred income tax assets by the Group in the current year.

Loss Attributable to Owners of the Parent and (Loss)/Profit Attributable to Non-Controlling Interests

Profit/(loss) attributable to non-controlling interests mainly represents the profit for the period attributable to dairy farmers with whom we cooperate in relation to dairy farm management in our farms. In 2018, loss attributable to non-controlling interests was RMB86.0 million and in 2017, profit attributable to non-controlling interests was RMB161.5 million.

In 2018, due to combined effects of (1) a significant decrease in the sales volume of the Group's self-owned brand organic liquid milk products; (2) a sharp decrease in the selling price of the Group's raw milk as compared to last year; (3) a substantial loss arising from changes in fair value less costs to sell of biological assets attributable to the parent; and (4) the provision for asset impairment of trade receivables and other receivables, loss attributable to owners of the parent of the Group was RMB2,225.2 million, increasing by 119.2% as compared with loss of RMB1,015.3 million in 2017.

(Loss)/profit for the year of the farming business recorded a loss of RMB1,047.2 million in 2018, decreased by 625.3% as compared with profit of RMB199.3 million in 2017. Excluding losses arising from changes in fair value less costs to sell of biological assets, profit for the year of the farming business was RMB274.3 million in 2018, decreased by 65.5% from RMB794.8 million in 2017, mainly due to the sharp decline of raw milk price of the Group as compared to the previous year.

ANALYSIS ON CONSOLIDATED STATEMENT OF FINANCIAL POSITION

Current Assets

As at December 31, 2018, total current assets of the Group were RMB2,048.2 million (as at December 31, 2017: RMB3,604.3 million), primarily consisting of inventories of RMB637.0 million (as at December 31, 2017: RMB860.8 million), trade and bills receivables of RMB344.1million (as at December 31, 2017: RMB1,100.0 million), prepayments, other receivables and other assets of RMB685.3 million (as at December 31, 2017: RMB898.8 million), and cash and bank balances of RMB374.3 million (as at December 31, 2017: RMB711.2 million), and biological assets of RMB7.5 million (as at December 31, 2017: RMB33.5 million).

Trade and Bills Receivables

Unit: RMB in thousands, except percentages

	As at	
	December 31, 2018	December 31, 2017
Trade and bills receivables	1,958,362	1,840,492
Impairment	(1,614,213)	(740,486)
Total	344,149	1,100,006

	As at			
Aging	December 31, 2018		December 31, 2017	
	Amount	Percentage	Amount	Percentage
Within 6 months	317,789	92.3%	820,352	74.6%
7 to 12 months	21,941	6.4%	272,596	24.8%
Over 1 year	4,419	1.3%	7,058	0.6%
Total	344,149	100.0%	1,100,006	100.0%

Pursuant to the provision policy for asset impairment established by the Group based on its actual production and operation conditions, the Group determined the receivable group by using aging as a credit risk characteristic and, by expected credit loss approach, made provisions for bad debts in respect of account receivables, and also estimated the provisions for asset impairment with reference to the recoverability of individual trade receivables and customer creditworthiness. In 2018, the Group made a total provision of RMB832.2 million for the impairment of trade receivables.

Current Liabilities

As at December 31, 2018, total current liabilities of the Group amounted to RMB4,573.4 million (as at December 31, 2017: RMB4,341.6million), primarily consisting of trade and bills payables of RMB1,456.3 million (as at December 31, 2017: RMB1,189.0 million), receipts in advance of nil (as at December 31, 2017: RMB14.7 million), other payables and accruals of RMB715.2 million (as at December 31, 2017: RMB482.4 million), interest-bearing bank and other borrowings of RMB2,320.7 million (as at December 31, 2017: RMB2,654.0 million), derivative financial instruments of RMB81.2 million (as at December 31, 2017: nil), and income tax payable of RMB: nil (as at December 31, 2017: RMB1.5 million).

Foreign Exchange Risk

The Group's businesses are principally located in the mainland China and most transactions are conducted in RMB. As at December 31, 2018, the Group did not have significant foreign currency exposure from its operations, except for bank balances equivalent to approximately RMB6.7 million, RMB0.6 million and RMB0.3 million which were denominated in Hong Kong dollars, United States dollars and Euro, respectively. As at December 31, 2018, 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 generally not required.

Charge on Assets

As at December 31, 2018, the Group had pledged deposits of approximately RMB297.1 million (as at December 31, 2017: RMB128.9 million) in total to banks in China as deposits for the issuance of letters of credit and bank drafts. At 31 December 2018, certain of the Group's biological assets with a fair value of approximately RMB1,069.8 million (2017: nil) and equity interests in fourteen non-wholly owned subsidiaries with net assets amounted to RMB2,311.9 million in total (2017: nil) were pledged to entrusted loans amounting to RMB1,300.0 million granted to the Group.

Liquidity, Financial Resources and Capital Structure

Throughout 2018, the Group financed its daily operations mainly from internally generated cash flows and bank and other borrowings. As at December 31, 2018, the Group had (a) cash and bank balances of RMB77.3 million (as at December 31, 2017: RMB582.3 million), and (b) interest-bearing bank and other borrowings of RMB2,370.2 million (as at December 31, 2017: RMB3,374.2 million), all denominated in RMB, of which, RMB49.5 million were 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 bank borrowings) divided by total equity) was 82.3% as at December 31, 2018 (as at December 31, 2017: 62.3%). Except bank and other borrowings equivalent to RMB60.9 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. For the year ended December 31, 2018, the annual interest rate of bank borrowings ranged from 1.55% to 12.97% (for the year ended December 31, 2017: 1.55% to 6.98%).

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 2018.

Capital Commitments

As at December 31, 2018, the Group's capital commitments amounted to RMB418.3 million (as at December 31, 2017: RMB225.6 million). The Group's capital commitments at the end of 2018 increased significantly as compared to the end of 2017, which was mainly attributable to the fact that the Group proposed to acquire minority interests in 12 farming companies with partial consideration of RMB300.0 million in cash pursuant to the equity transfer framework agreement entered into with 12 natural person shareholders.

HUMAN RESOURCES

As at December 31, 2018, the Group had a total of 3,814 employees (as at December 31, 2017: 3,803 employees). Total staff costs throughout 2018 (including the emoluments of Directors and senior management of the Company) amounted to RMB293.3 million (2017: RMB285.9 million).

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.

CONTINGENT LIABILITIES

During the year and as at December 31, 2018, the Group provided guarantees with amount of RMB155,000,000 (2017: RMB252,600,000), RMB123,419,000 (2017: RMB102,880,000) and RMB22,070,000 (2017: RMB180,000,000) for the bank borrowings of Shengmu Forage, Food Union Shengmu and some distributors, respectively. The external guarantees provided by the Group were recognized in the financial statements for 2017 and 2018 on the basis of the valuation of the guarantees provided by the independent professional valuer regarded as the best estimates required to pay for the performance of the current relevant obligations in accordance with the requirements of IFRSs.

MATERIAL ACQUISITIONS AND DISPOSALS

As at December 21, 2018, the Company and Shengmu High-tech entered into the Equity Transfer Framework Agreement with 12 individual shareholders to acquire minority interests in the 12 indirectly holding subsidiaries. A circular regarding the acquisition of minority interests in the 12 Farming Companies and the issue of consideration shares under specific mandate was published as at March 12, 2019. This resolution was passed at the extraordinary general meeting on March 28, 2019.

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

Save as disclosed above in "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 production of quality-assured dairy products is conditional upon the buildup of a quality milk source base. In view of this, Shengmu selected the Ulan Buh Desert as its milk source base and conducts control over each aspect, including environment, planting, farming, processing and products, allowing the entire production chain to be traceable and resulting in high-quality milk with international and EU organic certification.

Grass Planting, ensuring high quailty forage grass

The Group proactively communicates and cooperates with domestic and international universities and research institutes and introduces cutting-edge solutions to the whole process of organic planting. It improves the technology of forage grass planting in the desert, continuously optimizes the scientific management of the organic pasture and improves the production capacity of quality forage grass to satisfy the demand for quality forage grass from dairy farming and ensure the safety and quality of dairy products.

Cow Breeding, Demonstrating Dairy Farming with High Welfare

We have been adhering to the comprehensive outlook of integrating the development of China into the world and the present with the future. In combination with the fact that China Shengmu is highly intensive and standardized in its development, and by introducing standardized management philosophy, the Company's operating quality and efficiency was further enhanced. In terms of cow breeding, the Company will promote the optimization of dairy cow variety by integrating superior resources worldwide. In terms of the healthcare of dairy cows, the Company focuses on the welfare of dairy cows to reduce the risk of disease by capitalizing its regional advantages. In terms of breeding, the Company will optimise breeding formula and provide accurate nutrition based on locally grown plants, so as to enhance the digestibility of feed and reduce the feed cost for each kilo of milk. In terms of the operation and maintenance of the milking halls, the Company will enhance operating efficiency of the milking halls by integrating the resources from globally leading equipment manufacturers, such as GEA.

Produce Premium Milk through Management and Control with Strict Standards and System

Shengmu raw milk mainly supplies high-end products such as Shengmu organic pure milk, Mengniu Deluxe (including organic Deluxe), and Mengniu milk for students, as a result, it requires higher standards of management and control of the quality of raw milk. Shengmu has established and operated a raw milk quality management system that covers every part of operation to pursue premium raw milk better than industrial standard.

Ecological Farming with Recycling Economy in Response to Policies

Adhering to the strategy of "co-development of planting and farming", Shengmu uses organic forge grass to feed its cows and uses cow dung as fertilizer for soil for the duel effect of land development and desert management. In developing planting based on farming and forming harmonious match between forge grass and herds, Shengmu pushes forward synergetic development of production and ecology, effectively achieving mutual development of ecological, economic, and social effects.

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, 2018. 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.

BUSINESSES REVIEW

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. Further details of the Group's business review of the financial year are set out in the section headed "Management Discussion and Analysis" of this annual report.

The Group is exposed to a variety of business risks, including financial risk, regulatory and environmental risks, climate, disease and other natural risks in the ordinary course of business.

Further details of the Group's principal risks, please refer to Note 18 and Note 40 of the financial statements.

RESULTS

The Group's consolidated results for the year ended December 31, 2018 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 13 to the financial statements.

DONATIONS

The Group made donations with a total amount of RMB140,000 during the year of 2018 (2017: RMB10,595,000).

DIVIDEND POLICY AND DIVIDEND DISTRIBUTION

The Board does not recommend the payment of final dividend for the year ended December 31, 2018 (2017: Nil). The Board intends to consider dividend distribution upon receiving profit contribution from the principal business of the Group.

DISTRIBUTABLE RESERVES

The Company's distributable reserves amounted to RMB2,940.8 million as at December 31, 2018. For details of the changes in the Company's reserves in 2018, please refer to Note 43 to the financial statements

SHARE CAPITAL

For details of the changes in the Company's share capital in 2018, 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, 2018, 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 21, 2019. 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 18, 2019 to June 21, 2019, 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 17, 2019.

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 2018, the five largest customers of the Group in aggregate accounted for 72.8% of the Group's total revenue and the largest customer accounted for 42.7% of the Group's total income. In 2018, the five largest suppliers of the Group accounted for 28.9% of the Group's total amount of purchases and the largest supplier accounted for 14.7% of the Group's total amount of purchases.

In 2018, to the knowledge of the Directors, 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 2018, we did not experience any material disputes with our customers or suppliers.

DIRECTORS

For the year ended December 31, 2018, the Company's Directors were as follows:

Executive Directors

Mr. YAO Tongshan (re-appointed on June 29, 2018)
Mr. WU Jianye (re-appointed on June 28, 2017)
Mr. WANG Yuehua (appointed on June 29, 2018)

The former executive Directors, Ms. GAO Lingfeng and Mr. CUI Ruicheng, retired with effect from June 29, 2018 due to their other business commitments.

Non-executive Directors

Mr. SHAO Genhuo (Chairman) (re-appointed on June 28, 2017)
Mr. WEN Yongping (re-appointed on June 29, 2018)
Mr. SUN Qian (re-appointed on June 28, 2017)

The former non-executive Directors, Mr. FAN Xiang, Mr. CUI Guiyong and Mr. ZHANG Jiawang, retired with effect from June 29, 2018 due to their other business commitments.

Independent Non-executive Directors

Mr. FU Wenge (re-appointed on June 28, 2017)
Mr. WANG Liyan (re-appointed on June 29, 2018)
Mr. LI Xuan (re-appointed on June 29, 2018)

The former independent non-executive Directors, Mr. LI Changqing and Ms. GE Xiaoping retired with effect from June 29, 2018 due to their other business commitments.

Mr. Wang Yuehua has resigned as an executive director of the Company on January 25, 2019 and Mr. Zhang Jiawang has been appointed as an executive director of the Company with effect from January 25, 2019.

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.

PERMITTED INDEMNITY PROVISION

During the financial year, the Company has maintained adequate liability insurances cover in respect of potential legal actions against its Directors.

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.

MANAGEMENT CONTRACTS

No contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or existed during the financial year.

CHANGES TO INFORMATION IN RESPECT OF DIRECTORS

Mr. SHAO Genhuo, a non-executive Director of the Company, has ceased to act as the acting chief executive officer of the Company since January 16, 2019. Mr. Zhang Jiawang has been appointed as the chief executive officer of the Company with effect from January 16, 2019.

Mr. SHAO Genhuo has ceased to act as the president of Beijing Dabeinong Technology Group Co., Ltd. (北京大北農科技集團股份有限公司) ("**Dabeinong Group**"), a company incorporated in the PRC whose shares are listed on the Shenzhen Stock Exchange (stock code: 002385) since June 5, 2018.

Mr. WANG Yuehua, an executive Director of the Company, has ceased to act as the acting chief financial officer of the Company since January 16, 2019.

Mr. WEN Yongping, a non-executive Director of the Company, has been appointed as the general manager of the low temperature business department 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 incorporated in the Cayman Islands with limited liability whose shares are listed on the Main Board of the Stock Exchange (stock code: 2319) since September 12, 2018.

Mr. SUN Qian, a non-executive Director of the Company, has been appointed as a director of CooTek (Cayman) Inc., a company incorporated in the Cayman Islands whose shares are listed on NASDAQ (NASDAQ: CTK) and is primarily engaged in developing alternative input methods since September 2018.

Mr. WANG Liyan, an independent non-executive Director of the Company, has been appointed as an independent non-executive director of Gettop Acoustic Co., Ltd. (共達電聲股份有限公司), a company incorporated in the PRC whose shares are listed on the Shenzhen Stock Exchange (stock code: 002655) since April 12, 2018.

Save as disclosed herein, as at December 31, 2018, there was no change to the information required to be disclosed by the Directors pursuant to paragraph (a) to (e) and (g) of Rule 13.51(2) of the Listing Rules where applicable.

DIRECTORS' INTERESTS IN COMPETING BUSINESS

Mr. WEN Yongping, a non-executive Director of the Company, has been appointed as the vice president of China Mengniu and the general manager of the low temperature business department of Inner Mongolia Mengniu since March 29, 2017, Mr. WEN Yongping has been a non-executive director of China Modern Dairy Holdings Ltd. ("**China Modern Dairy**"), a company incorporated in the Cayman Islands with limited liability whose shares are listed on the Main Board of the Stock Exchange (stock code: 1117). For further information on the businesses of China Mengniu 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.

China 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 China Modern Dairy, and businesses of the Group and businesses controlled by China Modern Dairy are managed by independent entities under independent management and administration respectively, businesses of the Group and businesses controlled by China 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, 2018 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 set out in Rule 3.13 of the Listing Rules, the Company considers that Mr. FU Wenge, Mr. WANG Liyan and Mr. LI Xuan are independent parties and has received from them written confirmations on their independence.

MATERIAL ACQUISITION AND DISPOSAL OF SUBSIDIARIES AND ASSOCIATED COMPANIES

Acquisition of Minority Interest in the 12 Farming Companies

1 On December 21, 2018, the Company and Inner Mongolia Shengmu High-tech Farming Co., Ltd. (內蒙古聖牧高科牧業有限公司) ("**Shengmu High-tech**"), an indirect wholly-owned subsidiary of the Company, entered into a reorganisation memorandum with 12 individual shareholders (the "**12 Individual Shareholders**") of Inner Mongolia Shengmu Sand and Grass Industry Co., Ltd. (內蒙古聖牧沙草業有限公司) ("**Shengmu Sand and Grass**"), pursuant to which, the 12 Individual Shareholders agreed to complete a reorganisation (the "**Reorganisation**") for the purpose of implementation of the Acquisition (as defined hereunder). Upon completion of the Reorganisation, the 12 Individual Shareholders will directly hold 60% equity interest in Shengmu Sand and Grass and will hold 100% equity interest in 12 holding companies to be established by the 12 Individual Shareholders in the BVI respectively (the "**BVI Companies I**") which in turns hold 100% equity interest together in a holding company to be established in the BVI (the "**BVI Company II**") which will hold 100% equity interest in a holding company to be established in Hong Kong (the "**HK Company**"). The HK Company will hold the other 40% equity interest in Shengmu Sand and Grass.

On December 21, 2018, the Company and Shengmu High-tech entered into an equity transfer framework agreement (the "**Equity Transfer Framework Agreement**") with the 12 Individual Shareholders, pursuant to which, (i) Shengmu High-tech agreed to acquire 60% equity interest in Shengmu Sand and Grass (which holds the minority interest in the 12 farming companies, the "**12 Farming Companies**") from the 12 Individual Shareholders upon completion of the Reorganisation by cash in the amount of RMB300.00 million; and (ii) the Company agreed to issue a total of 688,705,234 new shares (the "**Consideration Shares**") of the Company at an issue price of HK$0.33 per share to the BVI Companies I to acquire 100% equity interest in BVI Company II which in turn indirectly hold the other 40% equity interest in Shengmu Sand and Grass upon completion of the Reorganisation (the "**Acquisition**").

The Consideration Shares represent (i) approximately 10.84% of the existing issued share capital of the Company as at December 21, 2018 (the date when the Equity Transfer Framework Agreement was entered into) and (ii) approximately 9.78% of the issued share capital of the Company as enlarged by the allotment and issuance of the Consideration Shares.

Immediately upon completion of the Acquisition, Shengmu Sand and Grass and the 12 Farming Companies will become indirect wholly-owned subsidiaries of the Company. The financial results of Shengmu Sand and Grass and the 12 Farming Companies will be fully consolidated into the consolidated financial statements of the Group upon completion of the Acquisition.

Completion of the Equity Transfer Framework Agreement is conditional upon the fulfilment or waiver of the conditions set out in the section headed "The Equity Transfer Framework Agreement — Conditions Precedent" in the announcement of the Company dated December 21, 2018.

Details of the Equity Transfer Framework Agreement are set out in the announcement and the circular of the Company dated December 21, 2018 and March 13, 2019 respectively.

Disposal of a Subsidiary of the Company

2 On December 23, 2018, Inner Mongolia Mengniu, Inner Mongolia Shengmu Holding Co., Ltd. (內蒙古聖牧控股有限公司) ("**Shengmu Holding**") (an indirectly wholly-owned subsidiary of the Company), Shengmu High-tech, Inner Mongolia Shengmu High-tech Dairy Co., Ltd. (內蒙古聖牧高科奶業有限公司) (the "**Target Company**") (a wholly-owned subsidiary of the Company) and the Company entered into a share purchase agreement (the "**Share Purchase Agreement**"), pursuant to which Shengmu Holding agreed to sell to Inner Mongolia Mengniu 26.67% interest in the Target Company, and Shengmu High-tech agreed to sell to Inner Mongolia Mengniu 24.33% interest in the Target Company. The consideration for the sale and purchase of the shares under the Share Purchase Agreement is RMB303,419,400 (equivalent to approximately HK$345,061,411).

Upon completion of the Share Purchase Agreement, Inner Mongolia Mengniu and the Company will hold 51% and 49% interests in the Target Company respectively. The Target Company will cease to be recognised as a subsidiary in the consolidated financial statements of the Company, and is expected to be recognised as a subsidiary of Inner Mongolia Mengniu in their consolidated financial statements. The Company will retain an equity interest of 49% in the Target Company upon completion of the Share Purchase Agreement.

Completion of the Share Purchase Agreement is conditional upon the fulfilment or waiver of the conditions set out in the section headed "Letter from the Board — (1) The Investment Agreements — The Share Purchase Agreement - Conditions Precedent" in the circular of the Company dated January 7, 2019.

Details of the Share Purchase Agreement are set out in the announcements and circular of the Company dated December 24, 2018, December 27, 2018, January 7, 2019 and January 11, 2019 respectively.

Save as disclosed above, for the year ended December 31, 2018 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, 2018, 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
SHAO Genhuo	Interest of a controlled corporation(1)	1,301,651,000(1)	20.48%
YAO Tongshan	Beneficial owner	409,092,700	6.44%
WU Jianye	Beneficial owner	32,706,261	0.51%

(1) 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 Co., Ltd ("**Nong You**"). Therefore, Mr. Shao is deemed to be interested in the Shares held by Nong You.

For details of changes of share numbers held by the executive Directors of the Company, please refer to the section of "Pre-IPO Share Option Scheme and Share Option Scheme" of this report.

(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%

Save as disclosed above and to the best knowledge of the Directors, as at December 31, 2018, 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.

DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBT SECURITIES

Save as disclosed in the section headed "Pre-IPO Share Option Scheme and Share Option Scheme" in this report, at no time during the year ended December 31, 2018 was the Company or any of its subsidiaries a party to any arrangements to enable the directors of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

INTERESTS OF THE SUBSTANTIAL SHAREHOLDERS

So far as is known to any Director or chief executive of the Company, as at December 31, 2018, 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
Start Great Holdings Limited	Beneficial owner	1,467,193,490 (L)	23.09%(L)
China Mengniu	Interest of a controlled corporation	1,467,193,490 (L)	23.09% (L)
Greenbelt Global Limited	Beneficial owner	536,097,305 (L)	8.44% (L)
Baring Private Equity Asia GP V Limited	Interest of a controlled corporation	536,097,305 (L)	8.44% (L)
Baring Private Equity Asia GP V LP	Interest of a controlled corporation	536,097,305 (L)	8.44% (L)
The Baring Asia Private Equity Fund V LP	Interest of a controlled corporation	536,097,305 (L)	8.44% (L)
Salata Jean	Interest of a controlled corporation	536,097,305 (L)	8.44% (L)
Zhang Junli (張軍力)	Interest of the spouse	409,092,700 (L)	6.44% (L)
Sequoia Capital 2010 CGF Holdco, Ltd.	Beneficial owner	378,320,000 (L)	5.95% (L)
SC China Growth 2010 Management, L.P.	Interest of a controlled corporation	378,320,000 (L)	5.95% (L)
SC China Holding Limited	Interest of a controlled corporation	378,320,000 (L)	5.95% (L)
Sequoia Capital China Advisors Limited	Interest of a controlled corporation	378,320,000 (L)	5.95% (L)
Sequoia Capital China Growth 2010, L.P.	Interest of a controlled corporation	378,320,000 (L)	5.95% (L)
SNP China Enterprises Limited	Interest of a controlled corporation	378,320,000 (L)	5.95% (L)
SHEN Nanpeng (沈南鵬)	Interest of a controlled corporation	378,320,000 (L)	5.95% (L)
The Goldman Sachs Group, Inc.	Beneficial owner	405,551,200 (L) 9,647,000 (S)	6.38% (L) 0.15% (S)
Nong You Co., Ltd.	Beneficial owner	1,301,651,000 (L)	20.48%
Beijing Zhi Nong Investment Co., Ltd.	Interest of a controlled corporation	1,301,651,000 (L)	20.48%

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%
Shengmu Sand and Grass	Bayannur Shengmu Hateng Farming Co., Ltd. (巴彥淖爾市聖牧哈騰牧業有限公司)	35.00%[1]
Shengmu Sand and Grass	Bayannur Shengmu Taohai Farming Co., Ltd. (巴彥淖爾市聖牧套海牧業有限公司)	45.00%[2]
Shengmu Sand and Grass	Bayannur Shengmu Liuhe Farming Co., Ltd. (巴彥淖爾市聖牧六和牧業有限公司)	35.00%[3]
Shengmu Sand and Grass	Alxa Shengmu Wuxing Farming Co., Ltd. (阿拉善盟聖牧五星牧業有限公司)	35.00%[4]
Shengmu Sand and Grass	Bayannur Shengmu Qixing Farming Co., Ltd. (巴彥淖爾市聖牧七星牧業有限公司)	35.00%[5]
Shengmu Sand and Grass	Bayannur Shengmu Beidou Farming Co., Ltd. (巴彥淖爾市聖牧北斗牧業有限公司)	26.00%[6]
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)	9.00%[6]
Shengmu Sand and Grass	Bayannur Shengmu Xinhe Farming Co., Ltd. (巴彥淖爾市聖牧新禾牧業有限公司)	35.00%[7]
Shengmu Sand and Grass	Bayannur Shengmu Zhenghe Farming Co., Ltd. (巴彥淖爾市聖牧正和牧業有限公司)	15.48%[8]
Shengmu Sand and Grass	Bayannur Shengmu Weiye Farming Co., Ltd. (巴彥淖爾市聖牧偉業牧業有限公司)	35.00%[9]
Shengmu Sand and Grass	Alxa Shengmu Zhaofeng Farming Co., Ltd. (阿拉善盟聖牧兆豐牧業有限公司)	23.40%[10]
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)	11.60%[10]
Shengmu Sand and Grass	Bayannur Shengmu Sanli Farming Co., Ltd. (巴彥淖爾市聖牧三利牧業有限公司)	26.00%[11]
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)	9.00%[11]
Shengmu Sand and Grass	Bayannur Shengmu Shajin Farming Co., Ltd. (巴彥淖爾市聖牧沙金牧業有限公司)	26.00%[12]
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)	9.00%[12]

Notes:

1. In August 2017, CHEN Qingjun transferred all shares of Bayannur Shengmu Hateng Farming Co., Ltd. (巴彥淖爾市聖牧哈騰牧業有限公司) held by him to Shengmu Sand and Grass.

2. In August 2017, LI Yongqiang transferred all shares of Bayannur Shengmu Taohai Farming Co., Ltd. (巴彥淖爾市聖牧套海牧業有限公司) held by him to Shengmu Sand and Grass.

3. In August 2017, DING Gaohuai transferred all shares of Bayannur Shengmu Liuhe Farming Co., Ltd. (巴彥淖爾市聖牧六和牧業有限公司) held by him to Shengmu Sand and Grass.

4. In August 2017, WANG Qiang transferred all shares of Alxa Shengmu Wuxing Farming Co., Ltd. (阿拉善盟聖牧五星牧業有限公司) held by him to Shengmu Sand and Grass.

5. In August 2017, LI Ruijun transferred all shares of Bayannur Shengmu Qixing Farming Co., Ltd. (巴彥淖爾市聖牧七星牧業有限公司) held by him to Shengmu Sand and Grass.

6. In August 2017, YUAN Lun transferred 26.00% shares of Bayannur Shengmu Beidou Farming Co., Ltd. (巴彥淖爾市聖牧北斗牧業有限公司) to Shengmu Sand and Grass.

7. In August 2017, WANG Lixin transferred all shares of Bayannur Shengmu Xinhe Farming Co., Ltd. (巴彥淖爾市聖牧新禾牧業有限公司) held by him to Shengmu Sand and Grass.

8. In August 2017, CHANG Zhiba transferred all shares of Bayannur Shengmu Zhenghe Farming Co., Ltd. (巴彥淖爾市聖牧正和牧業有限公司) held by him to Shengmu Sand and Grass.

9. In August 2017, HOU Liubin transferred all shares of Bayannur Shengmu Weiye Farming Co., Ltd. (巴彥淖爾市聖牧偉業牧業有限公司) held by him to Shengmu Sand and Grass.

10. In August 2017, GUO Yongfeng transferred 23.40% shares of Alxa Shengmu Zhaofeng Farming Co., Ltd. (阿拉善盟聖牧兆豐牧業有限公司) to Shengmu Sand and Grass.

11. In August 2017, REN Junming transferred 26.00% shares of Bayannur Shengmu Sanli Farming Co., Ltd. (巴彥淖爾市聖牧三利牧業有限公司) to Shengmu Sand and Grass.

12. In August 2017, YU Gong transferred 26.00% shares of Bayannur Shengmu Shajin Farming Co., Ltd. (巴彥淖爾市聖牧沙金牧業有限公司) to Shengmu Sand and Grass.

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, 2018, 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.

ISSUE OF UNLISTED WARRANTS UNDER SPECIFIC MANDATE

On December 10, 2018 and December 23, 2018, Shengmu High-tech and Inner Mongolia Mengniu entered into two entrusted loan agreements respectively, where term loan facilities in the aggregated amount of RMB1.3 billion (the "**Loan Facilities**") were granted, via the Horinger County Branch of Agricultural Bank of China Limited, to Shengmu High-tech. The Company considers that the terms of the Loan Facilities are more favourable than the terms available to the Group from independent third parties.

On December 23, 2018, the Company entered into a warrant subscription agreement (the "**Warrant Subscription Agreement A**") with Start Great Holdings Limited (the "**Subscriber A**") in relation to the warrant subscription of a total of 1,197,327,890 unlisted warrants (the "**Warrants A**") by the Subscriber A in consideration of the grant of the Loan Facilities by Inner Mongolia Mengniu to Shengmu High-tech at more favourable terms than available from independent third parties. Upon the exercise of the subscription rights attaching to the Warrants A in full, a maximum of 1,197,327,890 new ordinary shares (the "**Warrant Shares A**") of par value HK$0.00001 each in the issued share capital of the Company (with an aggregate nominal value of HK$11,973.2789), will be issued and allotted by the Company at a subscription price of HK$0.33 per Warrant Share A.

On the same day, the Company entered into a warrant subscription agreement (the "**Warrant Subscription Agreement B**", together with Warrant Subscription Agreement A, the "**Warrant Subscription Agreements**") with Greenbelt Global Limited (the "**Subscriber B**") in relation to the warrant subscription of a total of 140,862,105 unlisted warrants (the "**Warrants B**") by the Subscriber B at the warrant issue price of HK$0.0427 per Warrant B. Upon the exercise of the subscription rights attaching to the Warrants B in full, a maximum of 140,862,105 new ordinary shares (the "**Warrant Shares B**", together with Warrant Shares A, the "**Warrant Shares**") of par value HK$0.00001 each in the issued share capital of the Company (with an aggregate nominal value of HK$1,408.62105), will be issued and allotted by the Company at a subscription price of HK$0.33 per Warrant Share B.

As at December 23, 2018 (the date when the Warrant Subscription Agreements were entered into), the market closing price per shares of the Company was HK$0.3.

Completion of the Warrant Subscription Agreement A is conditional upon the fulfilment or waiver of the conditions set out in the sections headed "Letter from the Board — (2) Warrant Subscription Agreements — (i) Warrant Subscription Agreement A — Conditions for the issue of the Tranche 1 Warrants A" and "Letter from the Board — (2) Warrant Subscription Agreements — (i) Warrant Subscription Agreement A — Conditions for the issue of the Tranche 2 Warrants A" in the circular of the Company dated January 7, 2019.

Completion of the Warrant Subscription Agreement B is conditional upon the fulfilment or waiver of the conditions set out in the sections headed "Letter from the Board — (2) Warrant Subscription Agreements — (i) Warrant Subscription Agreement B — Conditions for the issue of the Tranche 1 Warrants B" and "Letter from the Board — (2) Warrant Subscription Agreements — (i) Warrant Subscription Agreement B — Conditions for the issue of the Tranche 2 Warrants B" in the circular of the Company dated January 7, 2019.

Details of the Warrant Subscription Agreements are set out in the announcements and circular of the Company dated December 24, 2018, December 27, 2018, January 3, 2019, January 7, 2019 and January 11, 2019 respectively.

The Board considered that the issue of Warrant Shares represented an opportunity to raise additional funds for the Company while broadening the capital base of the Company.

During the year ended December 31, 2018, none of the Warrant Subscription Agreements has been completed and hence no warrants have been exercised.

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 (as defined below), 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, the "**Vesting Date**"), 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 remained in force for a period of four years commencing on the date on which an option is granted pursuant to the scheme, and accordingly expired on April 30, 2018.

As at May 4, 2017, 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 had been fully vested. As none of such 408,835,800 options were exercised on or prior to May 4, 2017, all such options had lapsed in accordance with the terms of the Pre-IPO Share Option Scheme as amended by way of shareholders' approval on November 3, 2015. Pursuant to the terms of the Pre-IPO Share Option Scheme, no further share options may be granted under the Pre-IPO Share Option Scheme.

The Pre-IPO Share Option Scheme has expired on April 30, 2018.

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.

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 above said 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.

EQUITY-LINKED AGREEMENTS

Save as disclosed in sections headed "Material Acquisition and Disposal of Subsidiaries and Associated Companies", "Issue of Unlisted Warrants under Specific Mandate" and "Pre-IPO Share Option Scheme and Share Option Scheme" of this report, during the year ended December 31, 2018, the Company has not entered into any equity-linked agreement (as defined in section 6 of the Companies (Directors' Report) Regulation (Chapter 622D of the Laws of Hong Kong)).

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, 2018, the net proceeds were applied as follows:

	Funds utilized as at December 31, 2018 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 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, an entity connected with 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, 2018.

CONNECTED AND CONTINUING CONNECTED TRANSACTIONS

The Company's connected and continuing connected transactions during the year of 2018 are as follows:

1 Pursuant to the Equity Transfer Framework Agreement set out in the section headed "Material Acquisition and Disposal of Subsidiaries and Associated Companies" in this annual report, immediately after the Reorganisation but prior to the Acquisition, the 12 Individual Shareholders will directly and indirectly hold 100% equity interest in Shengmu Sand and Grass. Each of the 12 Individual Shareholders will directly and indirectly hold more than 10% equity interest in the 12 Farming Companies respectively, thus will be substantial shareholder of each of the 12 Farming Companies. Therefore, the 12 Individual Shareholders are connected persons at the subsidiary level as defined under Rule 14A.06(9) of the Listing Rules. Accordingly, the Acquisition contemplated under the Equity Transfer Framework Agreement constitutes a connected transaction of the Company as defined under Chapter 14A of the Listing Rules. The Acquisition is in the interests of the Company and the shareholders as a whole as it aligns to the national policies encouraged by the Chinese government and the needs of consumers for food safety, and contributes to the stability of prices of unpasteurised milk. Details of the Equity Transfer Framework Agreement are set out in the announcement of the Company dated December 21, 2018 with respect to connected transaction of the Company.

2 On November 22, 2016, Shengmu Pangu and Shengmu High-tech 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 High-tech. 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. For the year ended 31 December 2018, the total annual purchase amount of organic raw milk by the Group (excluding Shengmu Pangu) from Shengmu Pangu was RMB24.1 million. 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.

3 On November 22, 2016, Shengmu Pangu and Shengmu High-tech 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. For the year ended December 31, 2018, the total annual purchase amount of cows by the Group (excluding Shengmu Pangu) from Shengmu Pangu was RMB5.5 million, and the total annual sale amount of cows by the Group to Shengmu Pangu was nil. 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.

4 On November 22, 2016, Shengmu High-tech 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. For the year ended December 31, 2018, no financial assistance in the form of guarantees was provided by the Group (excluding Shengmu Pangu) to Shengmu Pangu. 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 High-tech 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.

5 On November 22, 2016, Shengmu High-tech 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 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. For the period from January 1, 2018 to March 20, 2018, the total annual purchase amount of feed by the Group from Sijichun was RMB8.9 million. 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 Feed Supply Framework Agreement was terminated on March 20, 2018 as set out in the announcement of the Company dated March 20, 2018.

6. On March 20, 2018, Shengmu Holding (for itself and on behalf of the Group) and Dabeinong Group entered into a framework agreement in relation to purchase of feed by the Group from Dabeinong Group (the "**Dabeinong Group Feed Supply Framework Agreement**"). As Mr. SHAO Genhuo, a non-executive Director of the Company, holds more than 30% equity interest in Dabeinong Group, Dabeinong Group is a connected person of the Company as defined under the Listing Rules. Accordingly, the transactions contemplated under the Dabeinong Group Feed Supply Framework Agreement constitute continuing connected transactions of the Company. The term of the Dabeinong Group Feed Supply Framework Agreement is from March 20, 2018 to December 31, 2020. The total annual purchase amount by the Group from Dabeinong Group under the Dabeinong Group Feed Supply Framework Agreement shall not exceed RMB60 million for each of the three years ending 31 December 2018, 2019 and 2020, respectively. For the period from March 20, 2018 to December 31, 2018, the total annual purchase amount of feed by the Group from Dabeinong Group was RMB36.7 million. Reasons and benefits of the transactions under the Dabeinong Group Feed Supply Framework Agreement are that as a leading feed provider in the PRC, the products of Dabeinong Group accord to very high technological and quality and safety assurance levels. Details of the Dabeinong Group Feed Supply Framework Agreement are set out in the announcement of the Company dated March 20, 2018.

The Directors (including the independent non-executive Directors) are of the view that the connected and 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 connected and 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 connected and continuing connected transactions set out above, nothing has come to their attention that causes them to believe that the disclosed connected and 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 distributors 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) providing guarantee for the bank loans of the associate distributors; (3) sale of raw materials to Shengmu Low Temperature; (4) purchase of forage from Shengmu Forage; (5) providing guarantee for the bank loans of Shengmu Forage and Food Union Shengmu; (6) purchase of feed from Sijichun in accordance with the Feed Supply Framework Agreement; (7) purchase of feed from Dabeinong Group with the Dabeinong Group Feed Supply Framework Agreement; and (8) payment of emoluments to key management of the Group.

EMPLOYEES

As at December 31, 2018, the Group had a total of 3,814 employees (3,803 employees in total as at December 31, 2017). Total staff costs for 2018 (including the emoluments of Directors and senior management of the Company) amounted to RMB293.3 million (RMB285.9 million in 2017). 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 2018, 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. Except for Mr. Wang Yuehua who agrees to waive any emoluments from the Group, none of the other Directors has waived any emoluments for the year ended December 31, 2018.

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 7 and 8 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.

COMPLIANCE WITH THE CORPORATE GOVERNANCE CODE

For details of the Company's corporate governance practices, please refer to the section headed Report on Corporate Governance Practices in this annual report.

AUDITORS

Ernst & Young has audited the financial statements for the year ended December 31, 2018. A resolution for the reappointment of Ernst & Young as auditors of the Company will be proposed at the forthcoming annual general meeting.

All references in this part of the annual report (Report of the Directors) to other parts, sections of or notes in the annual report, form part of the Report of the Directors.

By Order of the Board of
China Shengmu Organic Milk Limited
Shao Genhuo
Chairman

Hong Kong, March 28, 2019

EXECUTIVE DIRECTORS

Mr. **YAO Tongshan (姚同山)**, aged 62, is the founder and executive Director of the Group. He is also a member of the nomination committee of the Company. Mr. YAO was appointed to the Board in February 2014. He has over 15 years of experience in the dairy industry, with extensive industry and management experiences.

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), a company 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 and which is principally engaged in the manufacturing of liquid milk, ice cream and other dairy products, between October 2001 and January 2010.

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 as a senior economist (高級經濟師) by the 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 any directorship in any public listed companies in the last three years.

Mr. **WU Jianye (武建鄴)**, aged 45, is the president and executive Director of the Company. He is primarily responsible for the management and operation of the Group, and facilitating the realization of the key performance indicators of Shengmu Marketing. Mr. WU has been appointed as a Joint Company Secretary and an Authorised representative of the Company since June 29, 2018. Mr. WU was appointed to the 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 13 years of management experience in various different industries. Mr. WU joined the Group in September 2010 as an assistant to chief executive officer and was designated as the president of Shengmu Holding in August 2013.

Mr. WU graduated from the University of Inner Mongolia (內蒙古大學) and also received his executive master of business administration (EMBA) degree from Tsinghua University in July 2009.

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

Mr. **ZHANG Jiawang (張家旺)**, aged 40, is the chief executive officer and an executive Director of the Company. He was appointed to the Board on January 25, 2019.

Mr. ZHANG Jiawang was a vice president and manager of strategy and development of Da Bei Nong Group before he was appointed as the chief executive officer of the Company. Mr. ZHANG joined Da Bei Nong 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 a bachelor's degree in horticulture from Inner Mongolia Agricultural University (內蒙古農業大學) in July 2001 and an EMBA degree from People's University of China (中國人民大學) in January 2010.

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

NON-EXECUTIVE DIRECTORS

Mr. **SHAO Genhuo (邵根夥)**, aged 53, is the chairman of the Board and non-executive director of the Company. He is also a member of the nomination committee of the Company. He was appointed to the Board on September 26, 2016.

Mr. SHAO Genhuo is currently the chairman of the board of directors of Da Bei Nong 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 Da Bei Nong Group. Mr. SHAO founded Da Bei Nong Group in October 1994 and has 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 any directorship in any public listed companies in the last three years.

Mr. **WEN Yongping (溫永平)**, aged 44, is the vice president and the general manager of the low temperature business department of Inner Mongolia Mengniu Dairy Group Limited (內蒙古蒙牛乳業 (集團) 股份有限公司), a subsidiary of China Mengniu Dairy Company Limited, a company incorporated in the Cayman Islands with limited liability whose shares are listed on the Main Board of the Stock Exchange (stock code: 2319). Mr. Wen joined Mengniu in 1999 and has held various managerial positions since then. Since 29 March 2017, Mr. Wen has been a non-executive director of China Modern Diary Holdings Limited, a company incorporated in the Cayman Islands with limited liability whose shares are listed on the Main Board of the Stock Exchange (stock code: 1117).

Mr. WEN obtained a master's degree of agriculture study (major: agriculture marketing) in 2009 from Inner Mongolia Agricultural University (內蒙古農業大學). Mr. WEN obtained an EMBA degree from Peking University (北京大學) in 2011.

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

Mr. **SUN Qian (孫謙)**, aged 45, is a non-executive Director of the Company. He was appointed to the 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 a master's degree in business administration from Harvard University and a juris doctor's 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 was a director of COOTEK (NASDAQ: CTK), a company with input method being its core business, in September 2018.

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

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. **FU Wenge (付文革)**, aged 52, is an independent non-executive Director of the Company. He was appointed to the Board on September 26, 2016. He is the chairman of the nomination committee.

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 an 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 any directorship in any public listed companies in the last three years.

Mr. **WANG Liyan (王立彥)**, aged 61, is an independent non-executive director of the Company, and member of the audit committee and nomination committee. He is currently a professor of the Department of Accounting, a doctoral advisor, and a director of Center for Responsibility and Social Value, of Guanghua School of Management in Peking University and a certified public accountant in the PRC. He obtained his doctor's degree from Peking University, and is a visiting scholar at University of Hertfordshire in England and Hong Kong University of Science and Technology, a visiting professor at Menlo College in California, US. and a visiting scholar at the World Resources Institute. His major research area lies in accounting information and corporate value, overseas listing, dual financial report and corporate governance system. He also serves as the chief editor of China Accounting Review and China Management Accounting. Mr. Wang has been an independent director of Huaxin Cement Co., Ltd., a company listed on the Shanghai Stock Exchange (stock code: 600801), since April 23, 2015 and an independent director of Unigroup Guoxin Co., Ltd., a company listed on the Shenzhen Stock Exchange (stock code: 002049), since March 23, 2017. Mr. Wang has been an independent director of the Gettop Acoustic Co., Ltd., a company listed on the Shenzhen Stock Exchange (stock code: 002655), since April 12, 2018.

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

Mr. **LI Xuan (李軒)**, aged 50, is an independent non-executive director of the Company and member of the remuneration Committee. He obtained a doctor of laws degree from China University of Political Science and Law and currently serves as a university teacher. He is the Head of the LL.M Education Centre of Central University of Finance and Economics, the General Secretary of Case Study Committee of China Law Society (中國案例法學研究會) and a lawyer of ZiLue Law Offices (北京市資略律師事務所). He has been an independent director of the BOE Technology Group Co., Ltd., a company listed on the Shenzhen Stock Exchange (stock code: A: 000725; B: 200725), since August 19, 2016 and an independent supervisor of China National Building Material Company Limited (中國建材股份有限公司), a company listed on the Stock Exchange of Hong Kong Limited ((stock code: 3323), since 27 May 2016.

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

SENIOR MANAGEMENT

Mr. **SHAO Genhuo (邵根夥)**, aged 53, is chairman and non-executive Director of the Company. His biographical details are set out under the section "Non-Executive Directors" above.

Mr. **WU Jianye (武建鄴)**, aged 45, is the president, executive Director and Joint Company Secretary of the Company. His biographical details are set out under the section "Executive Directors" above.

Mr. **ZHANG Jiawang (張家旺)**, aged 40, is the chief executive officer and executive Director of the Company. His biographical details are set out under the section "Executive Directors" above.

Mr. **AU Wai Keung (區偉強)**, aged 47, is a Joint Company Secretary of the 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), Xin Point Holdings Limited (stock code: 1571), 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 fellow member of the Institute of Chartered Accountants in England and Wales.

For details of Directors' interests (as defined in Part XV of the Securities and Futures Ordinance) in shares of the Company, 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.

OVERVIEW

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 as a whole.

We have adopted, applied and complied with the code provisions contained in the Code on Corporate Governance and Corporate Governance Report (the "**Corporate Governance 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, 2018.

Pursuant to provision A2.1 of the Corporate Governance Code, the roles of chairman and chief executive officer should be separated and should not be performed by the same individual. During the year of 2018, Mr. SHAO Genhuo performed these two roles (chairman and acting chief executive officer). The Company has been reviewing this practice continuously and considering to split the roles of chairman of the Board and chief executive officer of the Company. Mr. Zhang Jiawang has been appointed as the chief executive officer of the Company with effect from January 16, 2019 and Mr. SHAO Genhuo has ceased to act as the acting chief executive officer of the Company since January 16, 2019.

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, 2018, 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 Board include: formulation and review of corporate governance policies and practices of the Company; review and monitoring of the training and continuous professional development of the Directors and senior management; review and monitoring 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

As at the date of this report, the Board was comprised of nine Directors, including three executive Directors (Mr. YAO Tongshan, Mr. WU Jianye and Mr. Zhang Jiawang); three non-executive Directors (Mr. SHAO Genhuo, Mr. WEN Yongping and Mr. SUN Qian); and three independent non-executive Directors (Mr. FU Wenge, Mr. WANG Liyan and Mr. LI Xuan). The Chairman of the Board of the Company is Mr. SHAO Genhuo. Mr. Zhang Jiawang was appointed as an executive Director of the Company on January 25, 2019.

There was no financial, business, family or other material relationship between the Directors of the Company and in particular, between the Chairman of the Board of the Company and the chief executive officer.

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

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

During the reporting period, the Company complied with Rule 3.10(1) and 3.10(2) of the Listing Rules which requires the Company to maintain at least three independent non-executive Directors and have an independent non-executive Director with appropriate professional qualifications or accounting or related financial management expertise. Mr. WANG Liyan, one of the independent non-executive Directors of the Company is a certified public accountant in the PRC.

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 2018, the Board held six meetings at which the operating results, investment issues, etc. of the Company were considered and discussed.

Attendance record is below:

Members	Meetings attended/ meetings held since respective appointment date	Attendance
Executive Directors		
Mr. YAO Tongshan	4/6	66.7%
Mr. WU Jianye	6/6	100%
Mr. WANG Yuehua (Note 1)	5/5	100%
Ms. GAO Lingfeng (Note 2)	1/1	100%
Mr. CUI Ruicheng (Note 2)	1/1	100%
Non-executive Directors		
Mr. SHAO Genhuo (Chairman)	6/6	100%
Mr. WEN Yongping	5/6	83.3%
Mr. FAN Xiang (Note 3)	1/1	100%
Mr. CUI Guiyong (Note 3)	1/1	100%
Mr. SUN Qian	5/6	83.3%
Mr. ZHANG Jiawang (Note 3)	1/1	100%
Independent non-executive Directors		
Mr. LI Changqing (Note 4)	1/1	100%
Ms. GE Xiaoping (Note 4)	0/1	0%
Mr. FU Wenge	5/6	83.3%
Mr. WANG Liyan	5/6	83.3%
Mr. LI Xuan	5/6	83.3%

Notes:

(1) Mr. WANG Yuehua was appointed as an executive Director with effect from June 29, 2018. He was entitled to attend the relevant Board meetings convened after his appointment.

(2) Ms. GAO Lingfeng and Mr. CUI Ruicheng resigned as executive Directors with effect from June 29, 2018. They were entitled to attend the relevant Board meetings convened before their resignation.

(3) Mr. FAN Xiang, Mr. CUI Guiyong and Mr. ZHANG Jiawang resigned as non-executive Directors with effect from June 29, 2018. They were entitled to attend the relevant Board meetings convened before their resignation.

(4) Mr. LI Changqing and Ms. GE Xiaoping resigned as independent non-executive Directors with effect from June 29, 2018. They were entitled to attend the relevant Board meetings convened before their 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, Mr. Zhang Jiawang, Mr. SHAO Genhuo, Mr. WEN Yongping, Mr. SUN Qian, Mr. FU Wenge, Mr. WANG Liyan and Mr. LI Xuan) 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, 2018, the Remuneration Committee comprised two independent non-executive Directors (Mr. FU Wenge and Mr. LI Xuan) and one non-executive Director (Mr. SUN Qian) and was chaired by Mr. LI Xuan.

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 2018, the Remuneration Committee convened one meeting, 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, 2018, the Nomination Committee comprised three independent non-executive Directors (Mr. FU Wenge, Mr. WANG Liyan and Mr. LI Xuan), one executive Director (Mr. YAO Tongshan) and one non-executive Director (Mr. SHAO Genhuo) and was chaired by Mr. FU Wenge.

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 2018, the Nomination Committee convened one meeting, whereby the members discussed the structure and composition of the Board of the Company, performed qualification review on preliminary candidates recommended by the management of the Company and identified suitable candidates, 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. Prior to election of new Directors, the chairman of the Nomination Committee submitted recommendations and relevant materials of the directorial candidates to the Board of the Company.

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, 2018, the Audit Committee comprised three independent non-executive Directors (Mr. FU Wenge, Mr. WANG Liyan and Mr. LI Xuan) and was chaired by Mr. WANG Liyan.

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 and interim results for 2018.

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 2018, the Audit Committee convened a total of two meetings, whereby the members discussed various matters, including the 2017 annual results and 2018 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
SHAO Genhuo	NA	1/1	NA
YAO Tongshan	NA	1/1	NA
GE Xiaoping (Note 1)	NA	NA	1/1
LI Changqing (Note 2)	NA	NA	1/1
WANG Liyan (Note 3)	NA	1/1	2/2
SUN Qian	1/1	NA	NA
LI Xuan (Note 4)	1/1	1/1	1/1
FU Wenge (Note 5)	1/1	1/1	1/1

Note:

(1) Ms. GE Xiaoping ceased to be a member of the Audit Committee of the Company with effect from June 29, 2018.

(2) Mr. LI Changqing ceased to be the chairman of the Remuneration Committee and a member of each of the Audit Committee and the Nomination Committee of the Company with effect from June 29, 2018.

(3) Mr. WANG Liyan was appointed as the chairman of the Audit Committee with effect from June 29, 2018.

(4) Mr. LI Xuan was appointed as the chairman of the Remuneration Committee and a member of each of the Nomination Committee and the Audit Committee with effect from June 29, 2018.

(5) Mr. FU Wenge was appointed as a member of the Remuneration Committee with effect from June 29, 2018.

GENERAL MEETINGS

For the year ended December 31, 2018, the attendance record of each Director at General Meetings is as follows:

Directors	Number of attendances/ meetings Annual General Meeting
YAO Tongshan	0/1
WU Jianye	1/1
WANG Yuehua (Note 1)	0/0
GAO Lingfeng (Note 2)	0/1
CUI Ruicheng (Note 2)	0/1
SHAO Genhuo	1/1
WEN Yongping	0/1
FAN Xiang (Note 3)	0/1
CUI Guiyong (Note 3)	0/1
SUN Qian	0/1
ZHANG Jiawang (Note 3)	1/1
LI Changqing (Note 4)	1/1
GE Xiaoping (Note 4)	0/1
FU Wenge	0/1
WANG Liyan	0/1
LI Xuan	1/1

Notes:

(1) Mr. WANG Yuehua was appointed as an executive Director with effect from June 29, 2018, which was the date of the annual general meeting.

(2) Ms. GAO Lingfeng and Mr. CUI Ruicheng resigned as executive Directors with effect from June 29, 2018, which was the date of the annual general meeting.

(3) Mr. FAN Xiang, Mr. CUI Guiyong and Mr. ZHANG Jiawang resigned as non-executive Directors with effect from June 29, 2018, which was the date of the annual general meeting.

(4) Mr. LI Changqing and Ms. GE Xiaoping resigned as independent non-executive Directors with effect from June 29, 2018, which was the date of the annual general meeting.

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, 2018.

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, 2018 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 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 Board also ensures the adequacy of resources, staff qualifications and experience, training programmes and budget of the Company's accounting, internal audit and financial reporting functions. The Board conducts review of the risk management and internal control systems of the Group once every year. The Board conducted a review of the effectiveness of the Group's risk management and internal control systems, including all material controls, including financial, operational and compliance controls in 2018 and the Company considers them effective and adequate.

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, 2018.

JOINT COMPANY SECRETARIES

Mr. WU Jianye (武建鄴) ("**Mr. WU**"), one of our joint company secretaries, is a full-time employee of the Company. Mr. WU 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) ("**Mr. AU**"), who possesses the qualification required under Rule 3.28, to act as another joint company secretary. Mr. WU, the executive Director of the Company, is the usual contact person to liaise with Mr. AU.

Mr. AU and Mr. WU cooperate with each other to jointly discharge the duties and responsibilities of company secretaries. Meanwhile, Mr. WU 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 2018, Mr. WU 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, 2018, the emoluments paid or payable for the audit and non-audit services provided by Ernst & Young was as follows:

	Amount (RMB)
Audit Services	5,220,000
Non-audit Services	250,000
Total	5,470,000

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 of the Company, 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 or, in the event the Company ceases to have such a principal office, the registered office 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, 2018, there was no change in or amendment to the Company's constitutional documents.

ABOUT THIS REPORT

As a H-share listed company, China Shengmu operates in strict accordance with relevant regulations of the Hong Kong Stock Exchange and performs corporate information disclosure, investor relations management and service work in a proper manner according to law. This report was prepared in accordance with the *Environmental, Social and Governance (ESG) Reporting Guide of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited* (hereinafter referred to as the "ESG Reporting Guide").

The ESG Reporting Guide provides the following principles for ESG reporting:

Materiality: To prepare this report, the Group made a materiality analysis to determine the issues to be disclosed in this report and the detail and accuracy of each issue. The materiality matrix in 2018 is listed in Section 1.3 herein.

Quantitative: This report disclosed quantitative data in both environmental and social aspects to demonstrate the Company's performance in each indicator.

Balance: The Company strives to achieve objective and unbiased information disclosure. The content of the report came from the Company's internal management documents, statistics and public disclosures, as well as public media reports, with no improper revisions.

Consistency: The indicators disclosed in this report are presented as much as possible in the form of comparative data of two consecutive years based on actual conditions of operation, in order to help readers better understand the trend of indicators. Unless otherwise stated, the data disclosed in this report are statistics based on the unified information collection process and working mechanism established by the Company to ensure that the data is comparable year after year.

1. SUSTAINABLE DEVELOPMENT MANAGEMENT

China Shengmu adheres to the "desert-based grass-to-grass organic production model". On the Ulan Buh organic pure land gifted by nature, China Shengmu breaks ground only to deliver natural pure, nutrient-rich organic milk to households with layer-by-layer control from environment, grassland, pasture, factory to table. China Shengmu is leading Chinese dairy industry towards a safety and health-oriented future, so as to contribute to the open, sharing and win-win development of the food industry.

China Shengmu's Contribution to Sustainable Development

- More than **200 thousands mu** of desert have been transformed into fine grassland, more than **200 square kilometers** of desert into oasis. **11** reservoirs have been built in Ulan Buh Desert.
- **1** bio-organic fertilizer processing plant, **9** organic manure fermentation plants and **6** liquid fertilizer production plants have been built.
- A total of **35** dairy farms have been built, including 12 in Hohhot and 23 in Bayannur.
- A total of **193.3 kilometers** of roads have been built and **277.9 kilometers** of power transmission lines built in the desert.

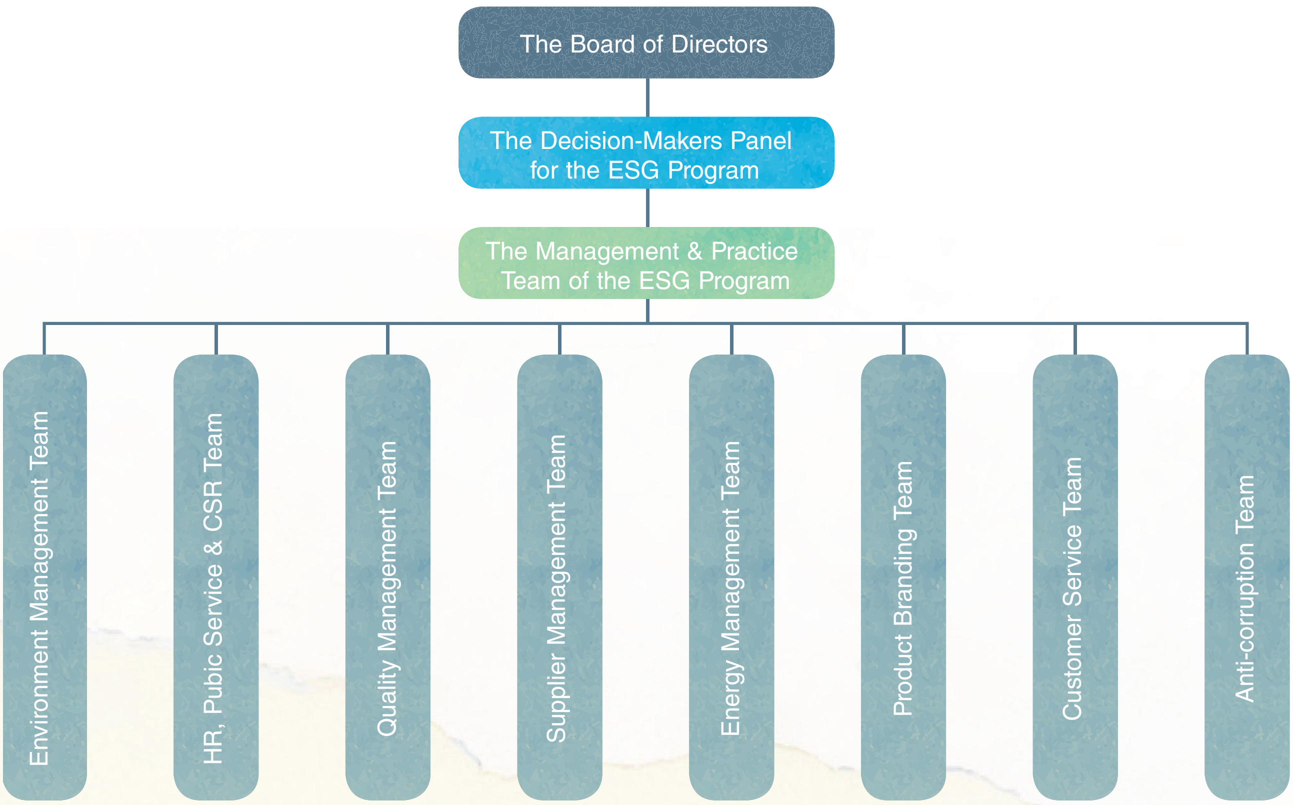
China Shengmu 2018 Honors & Awards

- 2018 "Corporate Contributor to Food Safety" Award
- The 12th BIOFACH China "Most Innovative Product" Award
- 2018 Outstanding Processing Enterprise of Quality Dairy Products

1.1 Sustainability Management Structure

The Group is actively engaged in various social responsibility management activities by establishing and improving the ESG work system and promoting the full integration of ESG concept into the management and operation of the Group. An organizational structure for ESG management was established affiliated by an ESG project decision-making group and an ESG project management and execution group, both of which report to the Board of Directors. Responsible for the Group's environmental, social and governance strategies and reports, the Board of Directors reviews on a regular basis sustainability management issues that may affect the Group's operations, shareholders and other stakeholders, and formulates policies, strategies and objectives of the Group's sustainability management.

ESG Management Structure of China Shengmu



1.2 Stakeholder Engagement

The Company places great emphasis on stakeholders' opinions and feedback in strategic decision making and management effectiveness assessment. The Company continuously communicates with stakeholders to understand their needs in depth and respond in a timely manner in 2018.

Stakeholder Concerned Issues and Communication Channels

Key stakeholders	Issues of Concern	Communication Channel	Main Responses
Shareholders	• Consistent and stable return on investment • Timely disclosure of information • Compliance operations	• Shareholders' meeting • Annual Report and corporate announcements	• Improving business operation and consolidating the Group's leading position in the Industry • Regular disclosure of information • Improving internal compliance systems
Employees	• Creating space for personal career development • Adequate compensation and benefits • Improving health security and safety protection	• Intranet • Enterprise journal • General manager Mailbox • Transparent communication meetings	• Improving internal management schemes such as employee recruitment and promotion • Enriching employee life • Providing diverse job and life securities
Suppliers	• Fair and open procurement process • Fulfilling contracts and agreements on time • Driving business growth and achieving win-win results	• Public notices on procurement and bidding • Regular communication on quality requirements • Supplier conference	• Ensuring the transparency of the procurement process • Guarantee of timely payment • Promoting communication with suppliers • Supporting supplier growth

Key stakeholders	Issues of Concern	Communication Channel	Main Responses
Dealers	• High-quality products and services • Responding to customer requests in a timely manner	• Customer callbacks • Regular visits • Satisfaction surveys	• Strengthening product quality controls • Establishing a comprehensive service response system • Improving the customer complaint handling process
Consumers	• Food safety • Product quality	• Trade fairs and promotional activities • WeChat, Weibo	• Strengthening food safety control • Organizing consumer representatives to visit production lines
Government	• Driving the development of local and peripheral industries • Compliant operations • Paying taxes according to law	• Government meetings • Regular visits • Supervision and inspection by government staff	• Providing jobs, contributing to tax revenue • Cooperating with government supervision, improving internal compliance monitoring systems • Complying with laws and regulations
Community	• Supporting community development • Participating in public service	• Dialogue with community representatives • Public service and Volunteer activities	• Maintaining close communication • Charitable donation and assistance

1.3 Materiality Analysis

In 2018, we made different forms of interaction and communication with various stakeholders, a benchmarking analysis of the issues disclosed in the sustainability report of peers, and a keyword analysis of press coverage of the Group's dynamics in 2018. Based on these efforts, we identified 19 social responsibility issues in four aspects of governance, operation, environment and society pursuant to the requirements of the ESG Reporting Guide. A questionnaire was used to determine the extent and boundaries of disclosure, thus to ensure more accurate and complete disclosure of operation and management-related information. In 2018, we recovered 12 copies of the Group's executive questionnaire and 278 copies of the stakeholder questionnaire, and collected opinions and suggestions from various stakeholders on the sustainable development management of the Group. These served as important basis and guidelines of Group's sustainable development management in the future. Based on evaluation of all social responsibility issues by stakeholders and executives, the 2018 materiality matrix was finally determined as follows:

Matrix of ESG Material Issues in 2018

2. SUSTAINABLE OPERATIONS

With the mission of "enabling all Chinese nationals to enjoy dairy products of the highest quality worldwide", China Shengmu strictly controls the quality from raw materials to finished products by establishing a circular organic ecosystem. We continuously improve customer service, meets diversified consumer demands, and exert our own advantages and experience to promote the development of the grass-to-grass organic milk industry.

2.1 Conscientiously Raise Cows to Produce Quality Milk

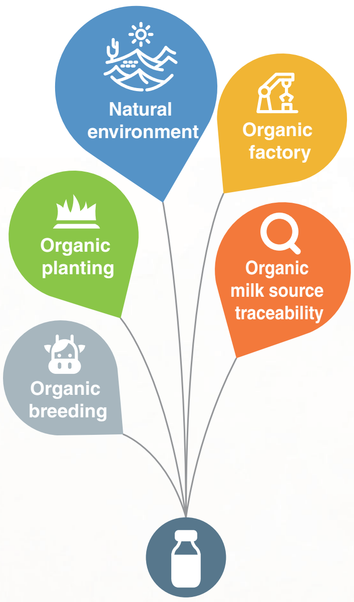
Shengmu always aims to produce the best milk in China. It established a quality management system with most strict control layer by layer from milk source to finished products and created a grass-to-grass organic industry chain with traceable organic grassland, organic dairy farm, organic factory and organic milk source to provide consumers with the most reliable organic milk.

Guarantees of China Shengmu's Organic Milk

Natural environment, rooted in a pure, pollution-free hinterland
Our production base is located in the Ulan Buh Desert of Inner Mongolia free from industrial, chemical and agricultural pollution, which makes it a superior grass growing environment with little pollution, less bacteria, fewer viruses and pests.

Organic planting, creating an oasis in desert
Our strategic partner Shengmu Forage owns over 200,000mu of organic grassland in the hinterland of the Ulan Buh Desert, which uses the organic fertilizer from dairy farms to enhance soil fertility and thus supplies exclusive quality roughage.

Organic breeding, to strengthen national livestock industry
The Group has built 8 organic dairy farms in the desert hinterland which raise nearly 40,000 organic dairy cows. We have specialized nutritionists, a professional health care system, and an exclusive eco-friendly system to provide the cows with good animal welfare.



Organic factory, producing safe milk products
The Group's liquid milk products are produced by the world's most advanced Swedish Tetra Pak A3 production equipment. We produce organic milk in strict accordance with GB/T19630-2011 Chinese National Standards on Organic Products and EU Organic Standard. There are no preservatives, artificial coloring or artificial flavoring in the production process.

Organic milk source traceability, allowing consumers to have milk with assurance
Every pack of Shengmu's grass-to-grass organic milk is printed with a code issued by China National Certification and Accreditation Administration to trace its source of production.

Shengmu takes full advantage of local conditions. Using the natural and pollution-free environment of the desert, a desert grass-based integrated organic circular model of "planting, breeding, processing and sales" was explored to establish the desert-based grass-to-grass organic industrial chain. At present, the Group has 23 dairy farms in the desert, including 8 organic ones raising more than 40,000 organic dairy cows, which makes us able to provide quality products to consumers in 31 provinces and cities nationwide.

- *Ensuring Feed Source Security*

  Shengmu implements a scientific and rigorous technical management process to fully guarantee the quality of feed. In the process of selecting seeds, suppliers are required to provide non-GMO test reports and non-organic banned substances-involved processing credentials. The forage varieties need to adapt to desert environment with pest and disease resistance, cold tolerance, drought tolerance and salt and alkali resistance.

  Shengmu owns more than 200 thousands mu of organic grassland. Making full use of Ulan Buh Desert's abundant sunlight, strong ultraviolet rays and dry climate, it plants natural grasses such as alfalfa, corn and oil sunflower as feed. We insist on the use of organic fertilizers and reject pesticides and fertilizers. We own a bio-organic fertilizer processing plant, nine organic manure fermentation plants and six liquid fertilizer production plants. Under the guidance of organic fertilizer experts from China Agricultural University and Chinese Academy of Agricultural Sciences, a unique organic fertilizer system has been formed to truly achieve the quality assurance of the source.

  When introducing new varieties, we will carry out several small-scale trials in the base. Combined with our planting experience in desert land, the combination of medium to late-maturing and early-maturing maize varieties is adopted in planting to avoid reduced quality of products due to late-maturing varieties unable to fully mature from the impact of wind-sand disaster in desert area.

  A grass-to-glass scientific management system was established from soil, irrigation water quality monitoring, organic fertilizer production, fine seed selection, scientific sowing, refined field management, environmental and meteorological monitoring to large-scale mechanized planting to improve the quality of feed production.

- *Strengthening dairy farm management*

  Shengmu firmly believes that high-quality organic milk comes from healthy and comfortable dairy cows, and therefore attaches great importance to dairy farm management. It started with scientific feeding and a comfortable breeding environment to ensure the healthy growth of dairy cows.

  China Shengmu formulated the Compilation of Management Systems for Feeding Nutrition Centers to regulate the operation procedures in terms of feeding, forage grass, barn, total mixed ration (TMR), manure clearing, and grass leveling. We use only organic forage and concentrate to provide a healthy source of nutrition for dairy cows, and carry out feed management in strict accordance with the standards for the production of organic raw milk.

TMR monitoring system and near-infrared (NIR) spectroscopy detection instrument are used to assist in reasonable mix of different fodder formulae and precise feeding based on information on the target herd's different stages of growth, milk production, milk fat, protein, gestational age, parity, body weight, body fat, climate, etc.

We have built 12 dairy farms in the Hohhot area, 23 dairy farms in the Ulan Buh Desert hinterland of Bayannur area, including 8 desert-based organic dairy farms. The dry desert environment can protect the cows from the epidemic, combined with the reverse osmosis technology-processed "mineral water", making our cows the "purest cows" in China. We formulated the *Herd Epidemic Prevention and Occupational Disease Prevention and Management System* to regulate the various processes of disinfection, immunization, quarantine and harmless treatment of dead cows due to illness. We disinfect the cows activity ranges, barns, maternity wards, and farm roads every day. The cows are regularly vaccinated with foot-and-mouth disease vaccine, brucellosis vaccine, IBR vaccine and BVDV vaccine.

We are committed to providing the most comfortable breeding environment for dairy cows. The low-density, low-pressure feeding method allows each cow's active area to cover an average of 60-80 square meters, ensuring ample range of activities; special personnel are arranged to clean up barns to ensure the clean environment for the cows; regular work-and-rest timetable was established to effectively prevent diseases such as mastitis, thereby improving the quality of milk production. In 2018, Bayannur Shengmu Pangu Farming Co., Ltd. was named the demonstration farm for standardized livestock and poultry breeding by the Ministry of Agriculture.

- *Standardizing Production*

We strictly follow the *Food Safety Law of the People's Republic of China*, ISO9001 quality management system and HACCP system certification standards. Our *Quality Management Assessment System* was established to conduct multiple inspections on raw milk, raw materials and packaging materials used in the production process. Compliance assessments are carried out on process operations and assessment results incorporated into employee performance. The "Shengmu Grass-to-Grass Organic Milk" produced by us has become the domestic milk brand with double organic certifications of EU and China Organic Food Certification Center (COFCC).

We established a comprehensive Product Recall Emergency Plan in accordance with the *Administrative Measures for Food Recalls*. The food recalls are divided into three levels according to the food safety risk level, and different recall processing procedures are adopted correspondingly; regular recall exercises are conducted to enhance food safety emergency response capabilities. In 2018, we did not have a product recall due to safety issues.


Dairy Cows with Comfortable Living Conditions
Spacious barns
Sunbathing
Music broadcast
Dry and comfortable sand beds

In March 2018, we carried out "Quality Month" activities. The key issues uncovered from unannounced food safety inspections last year were reviewed to improve solutions in a more refined and targeted manner and to clarify the direction and goals of future work on food quality and safety. The responsible persons of all departments signed the *Food Safety Responsibility Letter*, so that ideologically priority is given to product quality and production process compliance, and actions taken with attention to detail, striving to meet the highest quality standard.

- *Traceable Management*

  We established a comprehensive product traceability program to achieve comprehensive, timely and informative information traceability throughout the industry chain. In the grass planting stage, we record all kinds of farming activities to ensure the traceability of the forage material. In the dairy breeding stage, we create an exclusive file for each cow to record its physical condition, feeding situation and milk production in real time. In the milk processing and production process, the origin and organic certification of products are clearly recorded, production and transportation monitored and tracked throughout the process, and each package of milk produced stamped with spray code, the organic traceability code authorized by the Certification and Accreditation Administration of the People's Republic of China (CNCA). We implement an intelligent management system across the industry chain, using the most advanced equipment and technology to ensure product quality.

2.2 Broadening Sales Channels and Improving Customer Service

As a domestic grass-to-grass organic dairy company, China Shengmu is committed to providing consumers with the highest-quality products and services. We continuously expand sales channels with focus on customer demand feedback and consumer privacy protection, and improve product packaging, use friendliness and customer service through customer habit analysis.

- *Sales Layout*

  China Shengmu's sales network covers the first- and second-tier cities and the key third- and fourth-tier cities in the country, while continuously expanding to other third- and fourth-tier cities. At present, we have sales outlets for liquid milk in more than 400 cities in the country including cities in Tibet, Xinjiang, Hainan and other frontier regions.

  At the same time, we increased efforts to launch online sales channels by reaching cooperation with mainstream e-commerce platforms such as Suning and Joybuy, thus to expand scope of sales and provide real organic milk to more consumers.

- *Meeting Consumer Demand*

  We focus on improving customer service by establishing a sound complaint handling mechanism. Our *End Market Complaint Management System* was established, 400 consumer service hotlines opened, required to timely respond to, follow up and rapidly handle customer complaints. Consumer satisfaction survey is conducted on a regular basis to actively understand consumer needs and improve ourselves according to consumer opinions.

  In 2018, we teamed up with Joybuy to create high-quality consumer service. We established an organic dairy farm exclusive to Joybuy in order to ensure the stable supply of Shengmu products to Joybuy. Warehouse-to-warehouse pairing was realized between Shengmu and Joybuy, or a temporary turnover warehouse set up next to Joybuy's main warehouse to effectively shorten the commodity turnaround time and make timely replenishment. At the same time, using Joybuy's online consumption data we built customer profiles so as to provide more accurate products for consumers of different ages and consumption habits. In 2018, in order to meet the group-buy consumer needs and household consumption, we for the first time launched 5-pack and 20-pack simple packaged yogurt, which was greatly welcomed by consumers.

2.3 Supply Chain Management

Shengmu has strict requirements for supplier management by controlling product quality from the source to reduce the quality risks caused by suppliers. While ensuring the development of its own products, Shengmu has not forgotten to promote the development of the whole industry chain by exerting technological advantages and industry experience to help suppliers improve their technical capabilities and obtain relevant qualification certification.

Our *Supplier Management System* was established to regulate supplier access, evaluation and assessment processes in detail, to clarify departmental responsibilities and authorities, and to improve supplier management process. We give priority to qualified suppliers for cooperation, requiring them to have three-in-one certificate and business license, production license, quality management system certification, environmental management system certification, fire acceptance certificate, national and EU organic standard certificates, etc. We also investigate supplier compliance, cleanliness, environment, and safety, etc. Cooperation assessments and on-site inspections of suppliers are carried out on a regular basis, and suppliers are adjusted based on the results.

We share the experience of dairy farming, pasture planting and combining breeding and planting with supplier partners across the industry chain to help them build professional capacities, and assist suppliers to obtain organic certification.

2.4 Anti-Corruption

Shengmu resolutely prohibit corruption and commercial bribery. It strictly follows the provisions of the *Company Law of the People's Republic of China*, and the Corporate Governance Code and the *Basic Internal Control Norms for Enterprises of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong* and their supporting guidelines. Our *Discipline Inspection and Supervision Management System, Implementation Measures for Investigation and Handling of Violations and Disciplinary Breaches, and Whistle-blowing Management and Whistle-blower Rewarding System* were formulated to clearly define internal production order, personnel norms and strict punishments for violations and disciplinary breaches. Internal whistle-blowing channels were established to promote mutual supervision and mutual constraint between employees and to create a clean and honest working atmosphere. We sign anti-bribery contracts with all partners and actively build fair and transparent partnerships.

Internal Whistle-Blowing Channels

1. Online channels on official website, OA platform, and WeChat account
2. Disciplinary violation report bulletin board in production and office areas of all units
3. Internal and external liaisons for key posts and circulation links

Violation Clues Collection

1. From daily work inspections and special work inspections
2. In the process of participating in the work and meetings of functional departments
3. In the management process of monitoring and positioning systems
4. From the analysis of big data

3. ENVIRONMENTAL RESPONSIBILITY

The Group attaches great importance to corporate environmental responsibility by continuously improving environmental performance. Giving priority to ecological conservation and intensive use of resource is a prerequisite for the development of Shengmu. We created an industrial sand control model and built an ecological conservation demonstration zone. We fulfill our environmental protection responsibilities by creating a desert-based green industrial chain. During the reporting year, the Group complied with all environmental laws and regulations that have a significant impact on the Group, such as the *Environmental Protection Law of the People's Republic of China*.

3.1 Desertification Control

Shengmu puts effort in ecological conservation of the Ulan Buh Desert by persistently planting trees and grasses. At present, there are more than 200 thousands mu of organic grassland created by water-saving irrigation technology, and natural forage grasses such as alfalfa and corn planted. Adhering to the concept of harmonious coexistence between human and nature, we organically combine ecological conservation with business development by scientifically controlling sandstorms and making rational use of local natural resources. After entering the Ulan Buh Desert, Shengmu transformed the hinterland of Ulan Buh Desert into a vibrant oasis. The vegetation coverage rate of Shengmu organic planting and breeding park is currently over 90%, forming a fine microclimate in the area and greatly improving the environment. By 2018, Shengmu had transformed more than 200 thousands mu of desert into fine grassland.

3.2 Resourceful Utilization of Manure

In the process of raising organic cows, a large amount of farming waste is produced such as cow dung and cow urine. After decomposition and fermentation, it becomes a good organic fertilizer. The application of organic fertilizer can produce more aggregate structure of sandy soil and improve the soil's water retention, fertilizer retention and organic matter content, and thus improve the drought resistance of crops. Thanks to the unique and superior ecological environment of Ulan Buh Desert, Shengmu uses organic fertilizer produced from cow dung from organic dairy farms to protect the organic environment of Ulan Buh Desert and maintain and improve soil conditions for resource recycling. By 2018, Shengmu had built a bio-organic fertilizer processing plant, nine organic manure fermentation plants and six liquid fertilizer production plants to provide organic fertilizer for desert-based grassland.

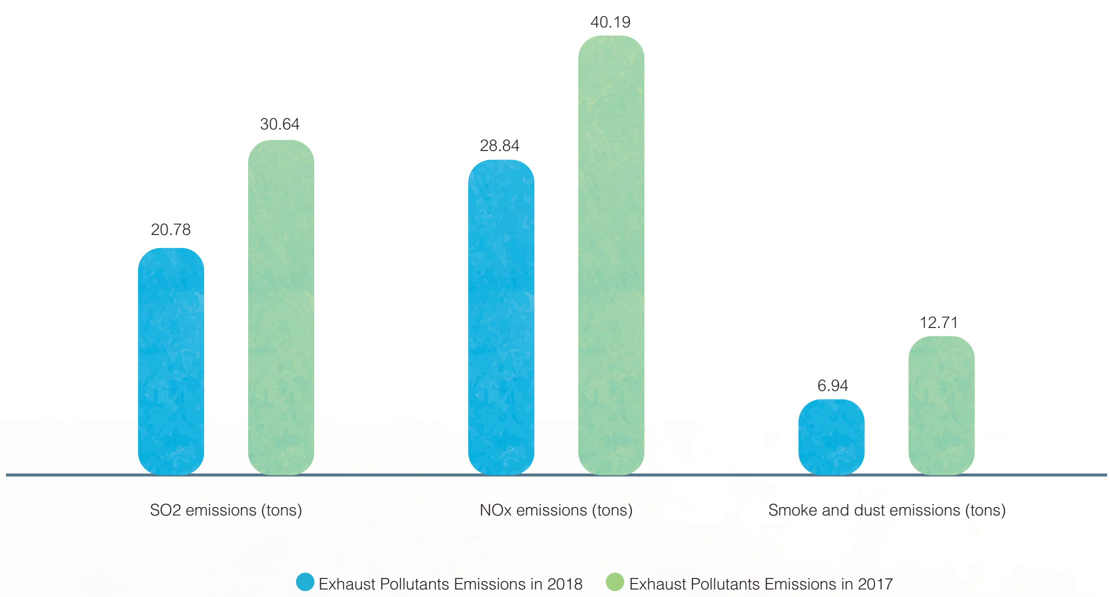
3.3 Reducing Emissions

The Group manages pollutants and greenhouse gas emissions in a standardized manner, and minimizes the impact of emissions during production according to environmental requirements. For different emissions, we take appropriate measures to reduce emissions and pollution. During the reporting year, we complied with all environmental laws and regulations that have a significant impact on the Group.

- *Exhaust Gas*

  The Group standardizes the management of exhaust gas during the operation process by strictly controlling the discharge of gaseous pollutants. In 2018, the total amount of waste gas emissions was 143,431,271.04 cubic meters, down 34.5% from 2017, showing effectiveness of our management of exhaust gas emissions.

Exhaust Pollutants Emissions in 2018



- *Wastewater*

  In the course of its operation, the Group strictly complies with the national laws and regulations on environmental protection for wastewater treatment by formulating an internal Sewage Treatment Management System. The wastewater from dairy production is treated by the factory's sewage treatment facility to meet the Standard B specified in the Standards for Sewage Discharged into Urban Sewers (CJ343-2010), and then discharged into a sewage treatment plant in Dengkou County, and the sludge is delivered to landfill by local environmental protection bureau. While complying with relevant environmental regulations, we continue to improve the process to enhance operational efficiency. A large amount of sludge is produced every day during actual operation. In 2018, we reduced the amount of sludge produced and the cost of sludge transportation by transforming the pipelines. After technical modification of existing pipelines, the sludge produced every day is digested by the Company itself and no longer needs to be transported to an external treatment center. The project effectively improves the efficiency of wastewater management by saving costs of RMB73,000 per year.

- *Other waste*

  Other waste produced in the production process includes medical waste, dead cows due to illness, and slag. The total waste produced in 2018 was 7,527.41 tons. The Group has been managing waste properly. According to the latest *Environmental Protection Law of the People's Republic of China*, we established internally *Waste Disposal Management System, Medical Waste Disposal Management System*, and *Harmless Treatment Management System*. The general solid waste and hazardous waste are collected separately and transferred respectively to units with corresponding processing qualifications. The compliance and legality of third-party processing qualifications is strictly reviewed, so that 100% of the solid wastes are disposed of in a standardized manner. Medical waste is disposed of by a qualified third party. In 2018, we implemented a desulfurization drug replacement project, using idle equipment to transform the desulfurization facilities from using caustic soda to using industrial grade white ash to ensure that the exhaust gas treatment fully meets the requirements for environmental protection.

- *Greenhouse gases*

  The Group's greenhouse gas emissions are mainly derived from indirect energy emissions from the use of electricity and direct emissions from the use of coal and diesel.

Sources of Green Gas emissions		CO2 emissions in 2018 (tons)
Indirect energy emissions	Use of electricity in production and offices (KWh)	71,452.59
Direct energy emissions	Coal consumption (tons)	41,060.97
	Diesel consumption (tons)	14,118.61
	Total	126,632.18
	CO2 emissions per RMB10,000 of output value (tons)	0.44

Note: Electricity consumption per megawatt-hour in North China is converted into 0.9680 tons of CO2 emissions according to Emission Factors of China Regional Power Grid Baseline in Emission Reduction Project of 2017. CO2 emissions from fossil fuels are calculated according to 2006 IPCC Guidelines for National Greenhouse Gas Inventories.

3.4 *Saving Resources*

Shengmu combines resource conservation with production and operation by establishing the concept of ecological conservation and promoting long-term progress and virtuous circle of production. We take full advantage of the desert's clean and safe production environment, abundant optical energy, soil conditions of water and fertilizer retention, and geographically superior water resources. Within the overall framework of focusing on ecological security, we have fully tapped resources and rationally and efficiently utilized them, and created a harmonious development model for environmental protection and economic and social development in the desert area. In 2018, we used a total of 2,600 tons of packaging materials in the production process.

- *Energy Management*

  The Group formulated a comprehensive energy management and control system, the *Energy Management System*. Energy consumption targets are set for each department which is then supervised and urged to implement energy conservation tasks and track the completion of tasks monthly to achieve rationalization of energy use. We analyze existing technologies and continuously improve performance in energy conservation and emission reduction. In 2018, we carried out a technical transformation project for boiler treatment upgrading. After analyzing the statistical data of the past years, we de-scaled the boiler and increased the exhaust air volume to improve the boiler combustion performance. Compared with 2016, between May 2017 and February 2018, the boiler transformation project saved 2,798.62 tons of coal, while saving costs of RMB1,399,310.

  The energy consumption of the Group during the reporting period was as follows:

Energy type	Consumption in 2018	Consumption in 2017
Power (KWh)	73,814,661.94	70,647,564.09
Coal (tons)	15,644.6	16,551.78
Diesel (tons)	4,467.19	5,512.53
Energy use per RMB10,000 of output value (tons of standard coal)	0.093	0.105

- *Water Resources Management*

  Shengmu Organic Planting Base is located in the Ulan Buh Desert, where the evaporation is much larger than the precipitation, making water resources especially precious. The Group actively promotes water resources management by adopting water recycling and water-saving irrigation and continuously improving water-saving technologies. We made technical improvements to water flow for workshop cleaning and milk tanker washing time to improve water-saving performance. In 2018, the Group's total water consumption was 2,036,411.80 tons.

Case: Shengmu Promotes Water Use Efficiency in Operations

From July 2018, in order to reduce the consumption of water resources during the washing process, Shengmu instructed the cleaning agent manufacturer to test the flushing flow and the washing time for adjustment and verification. By tracking the water quality data during the cleaning process of cleaning points, the test found that the water-saving performance was obvious with estimated water saving of 2,428 tons per month.

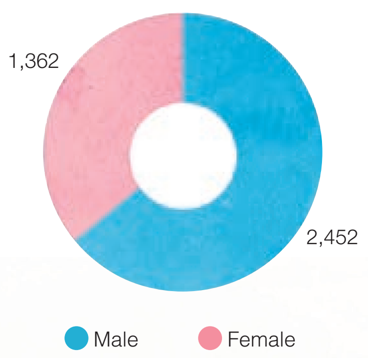
In 2018, we optimized the milk tanker washing time. According to repeated verification of water quality, Shengmu established a reasonable washing timetable, reducing washing time from previous 600s to 300s or even 150s, saving 450s for the overall cleaning of a milk tanker.

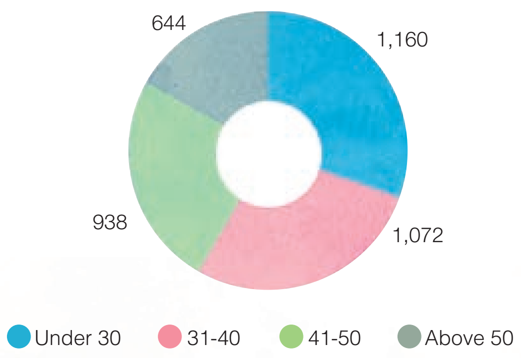
4. CARING FOR EMPLOYEES

Shengmu promotes a people-oriented talent management concept by safeguarding the rights and interests of employees and continuously expanding the career development channels and platforms for employees. At the same time, we care for the physical and mental health of employees by actively supporting employees in difficulty, striving to promote the common growth of employees and the Company.

4.1 *Protecting Rights and Interests*

The Group strictly abides by the *Labour Law of the People's Republic of China, the Labour Contract Law of the People's Republic of China*, and other relevant laws and regulations. Our *Administrative System for Recruitment and Employment* was formulated to prevent the employment of underage workers and the use of any form of forced Labour. Shengmu follows the employment principle of "open recruitment, equal competition, comprehensive assessment, and merit-based recruitment". In terms of on-boarding management, the System requires that new employees directly engaged in food production and operation before take physical checkups before getting on jobs; and those previously engaged in dairy farming take physical checkups for pre-employment occupational disease screening. As of December 31, 2018, the Group had a total of 3,814 employees.





According to Shengmu's development needs and industry characteristics, the Group divides the positions into five categories: managers, functional personnel, marketing personnel, technical personnel and operators. Taking into account the principles of fairness, stability, incentives and economical efficiency, China Shengmu formulated the Wide-range Remuneration Management System, which widens the range of salary fluctuation, covering different remuneration standards corresponding to position value and work performance, thereby opening the salary raise channel. The System clearly defines salary grading and criteria for adjustment of salary.

4.2 Training and Development

In order to streamline the career development channel of employees and standardize the promotion procedures for managers, a fair and just internal promotion environment was established, and a platform for employee promotion and career development created. The Group formulated the *Administrative System for Promotion of Managers*, which clearly stipulates the principle, conditions, procedures and channel settings for promotion.

Promotion Principles

The Group developed the *Training Management System* to help employees improve their work skills, professional quality and work efficiency. The System requires the senior management give open class at least twice annually within the Company and the middle-level management give open class at least once a year within the Company and four times a year within the department. Personnel responsible for key procedures must be trained by employees with rich work experience and only after they pass the assessment can they be allowed to get on jobs.

In order to improve the talent training mechanism and provide talent support for the Company's sustainable development, the Group started the talent echelon construction and reserve talent training in March 2018 in the principle of "equal emphasis on ability and integrity, internal training, dynamic management, and accelerated growth". A reserve talent library of "three levels, two echelons" was created which by the end of 2018 included 304 reserve talents. We promote the rapid growth of reserve talents by formulating effective and targeted curriculum training, on-the-job coaching, special tasks, and temporary (part-time) posts and other talent development programs. In July 2018, we organized a reserve elite training camp for 100 people and offered four training sessions respectively on thematic military training, comprehensive management ability training for middle management, amoeba management practice, and non-cash incentives to upgrade reserve elites' management skills and professional level.

4.3 *Occupational Health*

China Shengmu strictly abides by *Production Safety Law of PRC, Law of PRC on Prevention and Control of Occupational Diseases, Production Safety Regulations of Inner Mongolia Autonomous Region, Temporary Provision Rules for Health Supervision and Management in Workplace, Measures for Declaration and Administration of Occupational Hazard in Workplace and Supervision and Administration Regulations on Labour Protection Articles*. With strengthening its production safety management and affirming its production safety duty, the Group aims to prevent and reduce production accidents and create a safe and healthy working environment for employees. The Group adheres to the safe production policy with the principle of "safety first, prevention prime and comprehensive administration". In 2018, Collection of Production Safety Administration System was revised as to modify and supplement production safety duty, safety education and training, safety detection and hidden trouble rectification, dangerous working, occupational health, funding safety, survival safety conference and so on. In the *Occupational Health and Safety Administration System*, the Group regulated and set requirements on the notification and declaration of occupational diseases, training and education of occupational health publicity, management of occupational diseases' protection articles, daily monitoring on occupational hazard, surveillance archives of occupational health and so on.

China Shengmu had achieved auditing and certification of Occupational Health Safety Administration system's OHSAS 18001:2007 System and Environment Administration System's ISO 14001:2004 System. Shengmu pasture carries out detection and assessment on occupational disease hazard factors in workplace annually and organizes its employees to have an occupational health examination. In order to intensify occupational health management, assure employees' health, fully learn the condition of occupational disease hazard factors in feed processing workshop and employees' health condition, the Group organized employees in pasture to have an occupational health examination in May 2018; in December 2018, the Group made detection and assessment on occupational disease hazard factors in feed processing workshop, so as to help employees take control of its existence and adopt corresponding precautionary measures, and thus to protect employees' healthy rights and interests better.

4.4 Employee Care Activities

The Group devoted itself to the creation of a harmonious working environment and the construction of a warm Shengmu family for employees. We have carried out a series of activities to care for employees' life, improve employees' physical and mental quality and promote the construction and development of corporate spiritual civilization.

With 2018 Spring Festival's approaching, the dairy sector of the Group launched a warmth delivering visit to the needy employees and employees with special requirements, visiting its 8 employees and bringing them solatium and necessities of life as rice, flour and oil. With stepping into production line and visiting employees kept working there during the Spring Festival, we brought them fruit basket to express our gratitude for their hard work. During 2018 International Women's Day, we organized an indoor fun activity named "March as Women's Day, as well as Graceful Queen's Festival" for female employees, to promote their all aspects of quality and make them into a bright scenery line in both corporate production and their life. For the motivation of employees' vigorous and aggressive spiritual outlook, we held indoor skills contest on ball games and board games, from which to enrich their spare-time life and enhance team spirit. In order to lead young employees to inherit and carry forward the May Fourth spirit, the Group conducted gymnastics competition of "composing a magnificent movement on youth, revealing Shengmu's elegant demeanors", which responded the title slogan of "Following the Party by Holding High The League Flag, Devoting Youth Based on Our Jobs".

Visiting front-line workers in the Spring Festival

Indoor fun activity on the Women's Day

Group photo of winners of games

Gymnastics competition on the China's Youth Day

5. PUBLIC SERVICE IN COMMUNITY

Shengmu achieved public recognition through its contribution to desert economy and exploration of organic industries. While shaping the first brand of desert organic dairy industry, we unceasingly explored a sustainable new economic pattern on desertification control, which could drive local industry's development and help local farmers and herdsmen overcome poverty. Besides, we took part in social charity activities and public services responding to the public's trust in Shengmu with practical action. In 2018, China Shengmu donated RMB140,000, and its 210 volunteers participated the voluntary activities for 630 hours in total.

5.1 "Organic" Travels to Witness Desert Miracles

Shengmu upholds its vision of "turning Ulan Buh Desert of 1000 square kilometers into oasis", closely combining corporate development with desertification control activity to realize the win-win of economic benefit, ecological benefit and social benefit and provide new thoughts and valuable reference for the economic development of desert areas. In 2018, Shengmu had a good influence of an activity named "Organic Travels to Witness Desert Miracles" on the whole society. With constantly enhancing desert afforestation, we invited thousands of business partners, consumers, industry leaders and experts and media to ulan buh desert to experience the efficiency of Shengmu's desert afforestation and innovative business mode on organic industry chain. The activity offered the public a chance to know the flexibility of desert economic development and effectively promote consumers' awareness of pollution free and zero-additive organic food. In December 2018, Shengmu Group's Industrial Tourist Attraction in Bayan Nur City was graded as 3A industrial tourist attraction by the Cultural Tourism Department of Inner Mongolia Autonomous Region.

Travel in desert

5.2 *Serving Community to Create a Win-Win Situation*

Shengmu's rapid development drove its local economic development, offering thousands of jobs for Bayan Nur city and the surrounding areas, which relieved the local employment pressure.

The Group formulated *Administration System of Philanthropic Activities*, to form regulations on the process of affirming the target of philanthropic sponsorship, implementing correlated plan and assessing its results. To further regulate community service and volunteer service, China Shengmu in September 2017 formulated *China Shengmu Headquarters' Volunteer Activity Programme*, aiming to serve company, society and employees by Shengmu's volunteers. According to incomplete statistics, Shengmu carried out a series of voluntary services in 2018, whose recipients included the elderly in nursing homes, children in orphanages, the elderly without family members and other vulnerable groups. Besides, the Group paid visits to fire fighters and launched the Volunteer Day for its young employees.

Case:

The Joint Party Branch of Shengmu Dairy and Baleng Village Expressed Regards to Farmers and Herdsmen before the Spring Festival

On 13th February 2018, with the approaching of the Spring Festival, the members of Joint Party Branch of Shengmu Dairy and Baleng Village and the members of Baleng Village committee brought 12 farmers herdsmen rice, oil and Shengmu organic milk as new year's gifts to build a happy and peaceful festival atmosphere for veteran party members, veteran cadre and the poor.

The Joint Party Branch of Shengmu Dairy and Baleng Village expressed regards to farmers and herdsmen before the Spring Festival

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 83 to 179, which comprise the consolidated statement of financial position as at 31 December 2018, 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 31 December 2018, 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 the 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 beef cattle were measured at fair value less costs to sell, and amounted to RMB2,674,919,000 as of 31 December 2018. Dairy cows of the Group included milkable cows, heifers and calves, which were raised for the purpose of producing raw milk. Beef cattle were raised to three to six months old and then for sale. The fair value of biological assets as assessed by management was significant to the Company's consolidated financial statements since (i) the carrying values of such biological assets accounted for approximately 35% of the total assets of the Group; and (ii) significant estimates were involved in management's fair value assessment. Management engaged an external valuation expert to assist in the valuation of the biological assets as at 31 December 2018. The accounting policies and disclosures for biological assets are included in note 2.4 summary of significant accounting policies, note 3 significant accounting judgements and estimates and note 18 biological assets 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 were used as inputs for the valuation. We evaluated the reasonableness of the underlying basis and assumptions used by management. 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. We checked the computation of the fair value of biological assets and also reviewed the adequacy and appropriateness of the accounting policy and the disclosures relating to the fair value measurement of biological assets.
Recoverability of trade receivables	
The Group had a significant trade receivable balance of RMB333,924,000 as at 31 December 2018. The ageing profile of such receivables has deteriorated since 31 December 2015. During the year, the Group applied the simplified approach in calculating expected credit losses and established a provision matrix that was based on its historical credit loss experience, adjusted for forward-looking factors specific to the debtors and the economic environment. This is a key audit matter due to the magnitude, the complexity and the significant judgement and estimations by management involved in the computation of expected credit losses. The accounting policies and related disclosures are included in note 2.4 summary of significant accounting policies, note 3 significant accounting judgements and estimates and note 24 trade and bills receivables to the consolidated financial statements.	We performed audit procedures on understanding and evaluating the effectiveness of the Group's internal control process over the assessment of the recoverability of trade receivables. We assessed whether the Group's accounting policy for recognising expected credit losses for trade receivables was in compliance with the corresponding accounting standards. We assessed appropriateness of the approach and the models used to recognise expected credit losses on trade receivables. We tested the accuracy of the trade receivable balances and the ageing by tracing selected samples to supporting documents. We reviewed the Group's historical credit loss experience and assessed the reasonableness of the factors considered and estimations made by management regarding the forward-looking information after taking into account the subsequent settlement from customers, ageing profile, financial conditions of customers and their respective credit ratings. We tested the underlying calculation and assessed the appropriateness of the disclosures of the trade receivables in the consolidated financial statements.

Key audit matter	How our audit addressed the key audit matter
Financial guarantee contracts	
During the year ended 31 December 2018, it was identified by management that there were unrecorded and undisclosed financial guarantees in the consolidated financial statements for prior periods. Accordingly, management performed an investigation on the completeness of the financial guarantees provided to other parties and assessed their impact on the consolidated financial statements. The financial guarantee contracts should be fair-valued on the initial date of transaction and determination of fair value and expected credit losses arising from the Group's financial guarantee contracts was judgmental and involved significant estimates. Based on the valuation reports issued by an independent qualified professional valuer engaged by management, the Group had liabilities of RMB43,203,000 and RMB40,669,000 as at 31 December 2018 and 2017, respectively, in relation to the financial guarantee contracts executed, and their impact on the profits and losses for the year ended 31 December 2018 and 2017 was RMB124,236,000 and RMB29,479,000, respectively. Management accounted for the financial guarantee contracts in the consolidated financial statements for the year ended 31 December 2018 with correction of prior period errors. The impact was significant to the consolidated financial statements. The details of financial guarantee contracts are disclosed in note 2.4 summary of significant accounting policies, note 2.5 correction of prior period errors, note 3 significant accounting judgements and estimates and note 27 other payables and accruals to the consolidated financial statements.	We performed audit procedures on understanding and testing the Group's internal control process related to the assessment of the completeness and the measurement of the Group's financial guarantees. We discussed with management and the Audit Committee on the investigation procedures and reviewed the results of the investigation performed by management. We conducted interviews with banks and other parties who were granted guarantees, reviewed bank confirmations, credit reports and other external audit evidence provided by banks and other parties as well as investigated evidence provided by management to evaluate the completeness of the financial guarantee contracts executed by the Group. We reviewed the key assumptions used and computation performed in the valuation reports issued by the independent qualified professional valuer to assess the reasonableness of the fair value of the Group's financial guarantee contracts executed and the expected credit losses arising from the guarantees executed. We also reviewed the adequacy and appropriateness of the disclosures related to the financial guarantee contracts, including the correction of prior period errors.

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 ISAs 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 ISAs, 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
28 March 2019

CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

Year ended 31 December 2018

	Notes	2018 RMB'000	2017 Restated* RMB'000
CONTINUING OPERATIONS			
REVENUE	4	2,164,449	1,860,722
Cost of sales		(1,468,427)	(792,295)
Gross profit		696,022	1,068,427
Loss arising from changes in fair value less costs to sell of biological assets	18	(1,321,554)	(595,479)
Other income and gains/(losses)	4	12,576	(13,550)
Selling and distribution expenses		(63,723)	(34,907)
Administrative expenses		(119,262)	(76,171)
Impairment losses on financial and contract assets		(91,345)	—
Other expenses		(36)	—
Finance costs	6	(144,995)	(146,015)
Share of losses of associates		(15,180)	(2,937)
(LOSS)/PROFIT BEFORE TAX FROM CONTINUING OPERATIONS	5	(1,047,497)	199,368
Income tax credit/(expense)	9	280	(23)
(LOSS)/PROFIT FOR THE YEAR FROM CONTINUING OPERATIONS		(1,047,217)	199,345
DISCONTINUED OPERATION			
Loss for the year from a discontinued operation	10	(1,264,000)	(1,053,135)
LOSS FOR THE YEAR		(2,311,217)	(853,790)
(Loss)/profit attributable to:			
Owners of the parent		(2,225,200)	(1,015,266)
Non-controlling interests		(86,017)	161,476
		(2,311,217)	(853,790)
(LOSS)/EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT	12		
Basic			
– For loss for the year		(RMB 0.350)	(RMB0.160)
– For (loss)/profit for continuing operations		(RMB 0.151)	RMB0.006
Diluted			
– For loss for the year		(RMB 0.350)	(RMB0.160)
– For (loss)/profit for continuing operations		(RMB 0.151)	RMB0.006

* Certain amounts shown here do not correspond to the 2017 financial statements and reflect adjustments made. Refer to note 2.5 to the consolidated financial statements.

	2018 RMB'000	2017 Restated* RMB'000
OTHER COMPREHENSIVE INCOME		
Exchange differences on translation of foreign operations	(2,360)	3,081
Net other comprehensive (loss)/income that may be reclassified to profit or loss in subsequent periods	(2,360)	3,081
OTHER COMPREHENSIVE (LOSS)/INCOME FOR THE YEAR, NET OF TAX	(2,360)	3,081
TOTAL COMPREHENSIVE LOSS FOR THE YEAR	(2,313,577)	(850,709)
(Loss)/profit attributable to:		
Owners of the parent	(2,227,560)	(1,012,185)
Non-controlling interests	(86,017)	161,476
	(2,313,577)	(850,709)

* Certain amounts shown here do not correspond to the 2017 financial statements and reflect adjustments made. Refer to note 2.5 to the consolidated financial statements.

	Notes	31 December 2018 RMB'000	31 December 2017 Restated* RMB'000	1 January 2017 Restated* RMB'000
NON-CURRENT ASSETS				
Property, plant and equipment	13	2,087,045	2,798,328	2,710,368
Prepaid land lease payments	14	18,845	36,550	37,566
Other intangible assets	15	11,463	13,611	14,847
Investments in associates	16	90,328	105,784	112,658
Available-for-sale investments	17	—	2,007	1,427
Biological assets	18	2,667,427	3,867,389	3,884,257
Prepayments for property, plant and equipment and biological assets	20	1,014	6,209	11,963
Long term receivables	21	11,516	14,059	19,684
Deferred tax assets	19	410	32,197	24,634
Other non-current assets	22	9,930	39,212	16,565
Total non-current assets		4,897,978	6,915,346	6,833,969
CURRENT ASSETS				
Inventories	23	604,060	860,828	928,816
Biological assets	18	7,492	33,511	—
Trade and bills receivables	24	246,715	1,100,006	1,108,787
Prepayments, other receivables and other assets	20	599,092	898,837	393,550
Available-for-sale investments		—	—	120,000
Pledged deposits	25	150,617	128,884	66,791
Cash and bank balances	25	74,052	582,283	1,047,382
Assets of a disposal group classified as held for sale	10	978,355	—	—
Total current assets		2,660,383	3,604,349	3,665,326
CURRENT LIABILITIES				
Trade and bills payables	26	997,085	1,188,964	920,631
Receipts in advance		—	14,700	13,152
Other payables and accruals	27	486,235	482,387	449,742
Derivative financial instruments	28	81,238	—	—
Interest-bearing bank and other borrowings	29	2,218,864	2,654,046	918,404
Income tax payable		—	1,455	1,581
Liabilities directly associated with the assets classified as held for sale	10	790,006	—	—
Total current liabilities		4,573,428	4,341,552	2,303,510
NET CURRENT LIABILITIES		(1,913,045)	(737,203)	1,361,816
TOTAL ASSETS LESS CURRENT LIABILITIES		2,984,933	6,178,143	8,195,785

* Certain amounts shown here do not correspond to the 2017 financial statements and reflect adjustments made. Refer to note 2.5 to the consolidated financial statements.

	Notes	31 December 2018 RMB'000	31 December 2017 Restated* RMB'000	1 January 2017 Restated* RMB'000
NON-CURRENT LIABILITIES				
Interest-bearing bank and other borrowings	29	49,518	720,201	1,751,950
Long term payables	30	56,528	82,829	107,900
Total non-current liabilities		106,046	803,030	1,859,850
Net assets		2,878,887	5,375,113	6,335,935
EQUITY				
Equity attributable to owners of the parent		50	50	50
Share capital	31	2,017,863	4,315,612	5,327,797
Reserves	32	2,017,913	4,315,662	5,327,847
Non-controlling interests		860,974	1,059,451	1,008,088
Total equity		2,878,887	5,375,113	6,335,935

* Certain amounts shown here do not correspond to the 2017 financial statements and reflect adjustments made. Refer to note 2.5 to the consolidated financial statements.

Zhang Jiawang
Director

Wu Jianye
Director

Year ended 31 December 2018

	Notes	Attributable to owners of the parent								Non-controlling interests	Total equity
		Share capital	Share premium account	Contributed surplus	Share option reserve	Reserve funds	Exchange fluctuation reserve	Retained profits/ (accumulated losses)	Total		
		RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
At 1 January 2017		50	1,757,767	423,317	95,558	412,737	16,830	2,632,780	5,339,039	1,008,088	6,347,127
Correction of prior period errors at 1 January 2017	2.5	–	–	–	–	–	–	(11,192)	(11,192)	–	(11,192)
At 1 January 2017 (restated*)		50	1,757,767	423,317	95,558	412,737	16,830	2,621,588	5,327,847	1,008,088	6,335,935
Loss for the year as reported in the 2017 financial statements		–	–	–	–	–	–	(985,789)	(985,789)	161,476	(824,313)
Correction of prior period errors for the year	2.5	–	–	–	–	–	–	(29,477)	(29,477)	–	(29,477)
Loss for the year (restated*)		–	–	–	–	–	–	(1,015,266)	(1,015,266)	161,476	(853,790)
Exchange differences related to foreign operations		–	–	–	–	–	3,081	–	3,081	–	3,081
Total comprehensive loss for the year:		–	–	–	–	–	3,081	(1,015,266)	(1,012,185)	161,476	(850,709)
Equity-settled share option arrangements		–	–	–	–	–	–	–	–	–	–
Capital withdrawal by non-controlling shareholders		–	–	–	–	–	–	–	–	(217,430)	(217,430)
Capital injection by non-controlling shareholders		–	–	–	–	–	–	–	–	219,530	219,530
Distribution of dividends to non-controlling shareholders		–	–	–	–	–	–	–	–	(112,213)	(112,213)
Transfer from retained profits		–	–	–	–	50,393	–	(50,393)	–	–	–
At 31 December 2017		50	1,757,767	423,317	95,558	463,130	19,911	1,555,929	4,315,662	1,059,451	5,375,113
Effect of adoption of IFRS 9	2.2(b)	–	–	–	–	–	–	(70,189)	(70,189)	–	(70,189)
At 1 January 2018 (restated*)		50	1,757,767	423,317	95,558	463,130	19,911	1,485,740	4,245,473	1,059,451	5,304,924
Loss for the year		–	–	–	–	–	–	(2,225,200)	(2,225,200)	(86,017)	(2,311,217)
Exchange differences related to foreign operations		–	–	–	–	–	(2,360)	–	(2,360)	–	(2,360)
Total comprehensive loss for the year		–	–	–	–	–	(2,360)	(2,225,200)	2,227,560	(86,017)	(2,313,577)
Distribution of dividends to non-controlling shareholders		–	–	–	–	–	–	–	–	(112,460)	(112,460)
Transfer from retained profits		–	–	–	–	1,431	–	(1,431)	–	–	–
At 31 December 2018		50	1,757,767#	423,317#	95,558#	464,561#	17,551#	(740,891)#	2,017,913	860,974	2,878,887

* Certain amounts shown here do not correspond to the 2017 financial statements and reflect adjustments made. Refer to note 2.5 to the consolidated financial statements.

\# These reserve accounts comprise the consolidated reserves of RMB2,017,863 (2017: RMB4,315,612) in the consolidated statement of financial position.

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended 31 December 2018

	Notes	2018 RMB'000	2017 RMB'000 Restated*
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit before tax:		(2,283,308)	(861,330)
From continuing operations		(1,047,497)	199,368
From a discontinued operation		(1,235,811)	(1,060,698)
Adjustments for:			
Change in fair value of biological assets	18	1,321,554	595,479
Interest income		(7,140)	(8,739)
Finance costs	6,10	155,755	150,531
Share of profits and losses of associates		15,649	6,874
Fair value losses, net:			
Equity investments at fair value through profit or loss		1,310	—
Derivative financial instruments	4	6,539	—
Depreciation	13	211,598	187,250
Amortisation of prepaid land lease payments	14	1,626	2,251
Amortisation of other intangible assets	15	1,689	1,395
Loss on disposal of items of property, plant and equipment		1,114	2,402
Foreign exchange differences, net		(9,501)	30,694
		(583,115)	(106,807)
(Increase)/decrease in inventories		258,731	(4,173)
Decrease in trade and bills receivables		714,374	8,781
(Increase)/decrease in deposits and other receivables		211,170	(453,812)
Increase in pledged deposits		(57,554)	(62,093)
(Increase)/decrease in other non-current assets		29,282	(22,647)
Increase in trade and bills payables		267,341	268,333
Increase in receipts in advance		167,494	1,548
Increase/(decrease) in other payables and accruals		(43,891)	36,313
Cash generated from/(used in) operations		963,832	(120,943)
Interest received		6,464	7,910
Income taxes paid		2,207	(125)
Net cash flows from/(used in) operating activities		972,503	(113,158)

* Certain amounts shown here do not correspond to the 2017 financial statements and reflect adjustments made. Refer to note 2.5 to the consolidated financial statements.

	Notes	2018 RMB'000	2017 RMB'000 Restated*
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of items of property, plant and equipment		(40,019)	(328,040)
Additions to prepaid land lease payments		(1,891)	(1,487)
Additions to other intangible assets		(1,437)	(159)
Purchases of biological assets		(3,891)	(84,857)
Reversal of prepayment of biological assets		5,143	—
Payments for breeding calves and heifers		(438,573)	(746,317)
Proceeds from disposal of biological assets		310,463	257,993
Proceeds from disposal of items of property, plant and equipment		3,607	5,333
Purchases of time deposits with original maturity of more than three months		(110,817)	(284,611)
Proceeds from disposal of time deposits with original maturity of more than three months		284,611	115,000
Purchases of available-for-sale investments		—	(1,060)
Deemed disposal of associates		320	—
Proceeds from disposal of available-for-sale investments		—	120,480
Net cash flows from/(used) in investing activities		7,516	(947,725)
CASH FLOWS FROM FINANCING ACTIVITIES			
Capital injection by non-controlling shareholders		—	2,100
Dividends paid to non-controlling interests		(112,460)	(112,213)
New bank loans and other borrowings	34	1,722,106	1,347,888
Derivative financial instruments		67,093	
Proceeds from issue of super short-term notes		—	400,000
Repayment of short-term notes	34	(398,800)	(1,200)
Repayment of corporate bonds	34	(1,000,000)	—
Repayment of bank loans	34	(1,331,264)	(1,046,548)
Interest paid		(154,425)	(136,239)
Net cash flows (used in)/from financing activities		(1,207,750)	453,788
NET DECREASE IN CASH AND CASH EQUIVALENTS		(227,731)	(607,095)
Cash and cash equivalents at beginning of year		297,672	932,382
Effect of foreign exchange rate changes, net		7,142	(27,615)
CASH AND CASH EQUIVALENTS AT END OF YEAR		77,083	297,672
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS			
Cash and bank balances	25	74,052	582,283
Time deposits with original maturity of more than three months	25	(200)	(284,611)
Cash and short term deposits attributable to a discontinued operation	10	3,231	—
CASH AND CASH EQUIVALENTS AT END OF YEAR		77,083	297,672

* Certain amounts shown here do not correspond to the 2017 financial statements and reflect adjustments made. Refer to note 2.5 to the consolidated financial statements.

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. ("Shengmu High-tech")# (note (i))	PRC/ Mainland China	RMB 888,700,000	—	100	Production and distribution of raw milk
內蒙古聖牧控股有限公司 Inner Mongolia Shengmu Holding Co., Ltd. ("Shengmu Holding")# (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 Mongolia Shengmu High-tech Dairy Co., Ltd.#	PRC/ Mainland China	RMB 2,490,000,000	—	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 the 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, agricultural produce, derivative financial liabilities and financial asset at fair value through profit or loss 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 31 December 2018. 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.

2.1 BASIS OF PREPARATION (CONTINUED)

Going concern

The Group had net current liabilities of RMB1,913,045,000 and capital commitment of RMB418,257,000 as at 31 December 2018 (2017: net current liability of RMB737,203,000 and capital commitment of RMB225,565,000). In view of the net current liabilities position, the board of directors (the "Directors") have given careful consideration to the future liquidity and performance of the Group and its available sources of finance in assessing whether the Group will have sufficient financial resources to continue as a going concern.

Having considered the unutilised banking facilities of RMB1,458,000,000 as at 31 December 2018, the entrusted loan facility of RMB1,000,000,000 with the maturity date extended to 24 December 2020 and cash flow projections for the year ending 31 December 2019, the directors are satisfied that the Group is able to meet in full its financial obligations as they fall due for the foreseeable future. To mitigate any liquidity issues that might be faced by the Group, the Group may curtail or defer its expansion plans based on the availability of sufficient funds. Accordingly, the directors have prepared the consolidated financial statements on a going concern basis.

Should the Group be unable to continue in business as a going concern, adjustments would have to be made to restate the values of assets to their recoverable amounts, to provide for any further liabilities which might arise and to reclassify non-current assets as current assets. The financial statements do not include any adjustments that would result from the failure of the Group to continue in business as a going concern.

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 2	*Classification and Measurement of Share-based Payment Transactions*
Amendments to IFRS 4	*Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts*
IFRS 9	*Financial Instruments*
IFRS 15	*Revenue from Contracts with Customers*
Amendments to IFRS 15	*Clarifications to IFRS 15 Revenue from Contracts with Customers*
Amendments to IAS 40	*Transfers of Investment Property*
IFRIC 22	*Foreign Currency Transactions and Advance Consideration*
Annual Improvements 2014-2016 Cycle	*Amendments to IFRS 1 and IAS 28*

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES (CONTINUED)

Except for the amendments to IFRS 4 and Annual Improvements 2014-2016 Cycle, which are not relevant to the preparation of the Group's financial statements, the nature and the impact of the new and revised IFRS standards are described below:

(a) Amendments to IFRS 2 address three main areas: the effects of vesting conditions on the measurement of a cash-settled share-based payment transaction; the classification of a share-based payment transaction with net settlement features for withholding a certain amount in order to meet an employee's tax obligation associated with the share-based payment; and accounting where a modification to the terms and conditions of a share-based payment transaction changes its classification from cash-settled to equity-settled. The amendments clarify that the approach used to account for vesting conditions when measuring equity-settled share-based payments also applies to cash-settled share-based payments. The amendments introduce an exception so that a share-based payment transaction with net share settlement features for withholding a certain amount in order to meet the employee's tax obligation is classified in its entirety as an equity-settled share-based payment transaction when certain conditions are met. Furthermore, the amendments clarify that if the terms and conditions of a cash-settled share-based payment transaction are modified, with the result that it becomes an equity-settled share-based payment transaction, the transaction is accounted for as an equity-settled transaction from the date of the modification. The amendments have had no impact on the financial position or performance of the Group as the Group does not have any cash-settled share-based payment transactions and has no share-based payment transactions with net settlement features for withholding tax.

(b) IFRS 9 *Financial Instruments* replaces IAS 39 *Financial Instruments: Recognition and Measurement* for annual periods beginning on or after 1 January 2018, bringing together all three aspects of the accounting for financial instruments: classification and measurement, impairment and hedge accounting.

With the exception of hedge accounting, which the Group has applied prospectively, the Group has recognised the transition adjustments against the applicable opening balances in equity at 1 January 2018. Therefore, the comparative information was not restated and continues to be reported under IAS 39.

Classification and measurement

The following information sets out the impacts of adopting IFRS 9 on the statement of financial position, including the effect of replacing IAS 39's incurred credit loss calculations with IFRS 9's expected credit losses ("ECLs").

A reconciliation between the carrying amounts under IAS 39 and the balances reported under IFRS 9 as at 1 January 2018 is as follows:

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES (CONTINUED)

(b) (continued)

Classification and measurement (continued)

		IAS 39 Measurement					IFRS 9 Measurement	
	Notes	Category	Amount	Re-classification	ECL	Other	Amount	Category
			RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	
Financial assets								
Equity investments designated at fair value through other comprehensive income		N/A	—	—	—	—	—	FVOCI[5] (equity)
Debt investments designated at fair value through other comprehensive income		N/A	—	—	—	—	—	FVOCI (debt)
Financial assets at fair value through profit or loss		FVPL[3]	—	2,007	—	—	2,007	FVPL (mandatory)
Available-for-sale investments	(i)	AFS[1]	2,007	(2,007)	—	—	—	N/A
Long term receivables			14,059	—	—	—	14,059	AC[4]
Trade and bills receivables	(ii)	L&R[2]	1,100,006	—	(41,483)	—	1,058,523	AC
Financial assets included in prepayments, other receivables and other assets	(ii)	L&R	327,774	—	(28,706)	—	299,068	AC
Pledged deposits		L&R	128,884	—	—	—	128,884	AC
Cash and cash equivalents		L&R	582,283	—	—	—	582,283	AC
			2,155,013	—	(70,189)	—	2,084,824	
Other assets								
Contract assets			—	—	—	—	—	
Deferred tax assets			32,197	—	—	—	32,197	
			32,197	—	—	—	32,197	
Total assets			2,187,210	—	(70,189)	—	2,117,021	
Financial liabilities								
Trade and bills payables		AC	1,188,964	—	—	—	1,188,964	AC
Long term payables		AC	82,829	—	—	—	82,829	AC
Financial liabilities included in other payables and accruals		AC	397,509	—	—	—	397,509	AC
Interest-bearing bank and other borrowings		AC	3,374,247	—	—	—	3,374,247	AC
Loans from associates		AC	—	—	—	—	—	AC
Due to the ultimate holding company		AC	—	—	—	—	—	AC
Financial guarantee contracts		FVPL	40,669	—	—	—	40,669	FVPL (mandatory)
Other liabilities		AC	—	—	—	—	—	AC
			5,084,218	—	—	—	5,084,218	
Other liabilities								
Defer tax liabilities			—	—	—	—	—	
Total liabilities			5,084,218	—	—	—	5,084,218	

1 AFS: Available-for-sale investments
2 L&R: Loans and receivables
3 FVPL: Financial assets at fair value through profit or loss
4 AC: Financial assets or financial liabilities at amortised cost
5 FVOCI: Financial assets at fair value through other comprehensive income

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES (CONTINUED)

(b) (continued)

Classification and measurement (continued)

Notes:

(i) The Group has classified its unlisted investments previously classified as available-for-sale investments as financial assets measured at fair value through profit or loss as these non-equity investments did not pass the contractual cash flow characteristics test in IFRS 9.

(ii) The gross carrying amounts of the trade and bills receivables and the financial assets included in prepayments, other receivables and other asset under the column "IAS 39 measurement – Amount" represent the amounts after adjustments for the adoption of IFRS 15 but before the measurement of ECLs. Further details of the adjustments for the adoption of IFRS 15 are included in note 2.2(c) to the financial statements.

(iii) The Group has remeasured the carrying amounts of the financial guarantees given to banks in connection with borrowing facilities granted to associates and extended distributors based on the ECL allowance.

As of 1 January 2018, the Group classified equity investments previously classified as available-for-sale investments as equity investments. These instruments didn't pass the contractual cash flow characteristics test in IFRS 9, which were held with the intention to sell.

The fair value of these instruments that the Group still held as at 31 December 2018 was nil. The change in fair value of these instruments in 2018, that would have been recorded in other income and loss had these instruments continued to be revalued through profit and loss, would have been nil.

Impairment

The following table reconciles the aggregate opening impairment allowances under IAS 39 to the ECL allowances under IFRS 9. Further details are disclosed in notes 20 and 24 to the financial statements.

	Impairment allowances under IAS 39 at 31 December 2017	Re-measurement	ECL allowances under IFRS 9 at 1 January 2018
	RMB'000	RMB'000	RMB'000
Trade and bills receivables	740,486	41,483	781,969
Financial asset included in prepayments, other receivables and other assets	—	28,706	28,706
	740,486	70,189	810,675

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES (CONTINUED)

(b) (continued)

Impairment on retained profits

The impact of transition to IFRS 9 on retained profits is as follows:

	Retained profits RMB'000
Balance as at 31 December 2017 under IAS 39	1,555,929
Recognition of expected credit losses for trade and bills receivables under IFRS 9	(41,483)
Recognition of expected credit losses for financial assets included in prepayments, other receivables and other assets under IFRS 9	(28,706)
Balance as at 1 January 2018 under IFRS 9	1,485,740

(c) IFRS 15 and its amendments replace IAS 11 Construction Contracts, IAS 18 Revenue and related interpretations and it applies, with limited exceptions, to all revenue arising from contracts with customers. IFRS 15, establishes a new five-step model to account for revenue arising from contracts with customers. Under IFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The principles in IFRS 15 provide a more structured approach for measuring and recognising revenue. The standard also introduces extensive qualitative and quantitative disclosure requirements, including disaggregation of total revenue, information about performance obligations, changes in contract asset and liability account balances between periods and key judgements and estimates. The disclosures are included in notes 3 and 4 to the financial statements. As a result of the application of IFRS 15, the Group has changed the accounting policy with respect to revenue recognition in note 2.4 to the financial statements.

Before the adoption of IFRS 15, the Group recognised consideration received from customers in advance as receipts in advance. Under IFRS 15, the amount is classified as contract liabilities which is included in other payables and accruals.

Therefore, upon adoption of IFRS 15, the Group has reclassified RMB14,700,000 from receipts in advance to contract liabilities as at 1 January 2018 in relation to the consideration received from customers in advance as at 1 January 2018.

As at 31 December 2018, under IFRS 15, RMB119,680,000 was reclassified from receipts in advance to contract liabilities in relation to the consideration received from customers in advance for the sale of goods.

(d) Amendments to IAS 40, clarify when an entity should transfer property, including property under construction or development, into or out of investment property. The amendments state that a change in use occurs when the property meets, or ceases to meet, the definition of investment property and there is evidence of the change in use. A mere change in management's intentions for the use of a property does not provide evidence of a change in use. The amendments have had no impact on the financial position or performance of the Group.

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES (CONTINUED)

(e) IFRIC 22 provides guidance on how to determine the date of the transaction when applying IAS 21 to the situation where an entity receives or pays advance consideration in a foreign currency and recognises a non-monetary asset or liability. The interpretation clarifies that the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) is the date on which an entity initially recognises the non-monetary asset (such as a prepayment) or non-monetary liability (such as deferred income) arising from the payment or receipt of the advance consideration. If there are multiple payments or receipts in advance of recognising the related item, the entity must determine the transaction date for each payment or receipt of the advance consideration. The interpretation has had no impact on the Group's financial statements as the Group's accounting policy for the determination of the exchange rate applied for initial recognition of non-monetary assets or non-monetary liabilities is consistent with the guidance provided in the interpretation.

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 3	*Definition of a Business*[2]
Amendments to IFRS 9	*Prepayment Features with Negative Compensation*[1]
Amendments to IFRS 10 and IAS 28	*Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*[4]
IFRS 16	*Leases*[1]
IFRS 17	*Insurance Contracts*[3]
Amendments to IAS 1 and IAS 8	*Definition of Material*[2]
Amendments to IAS 19	*Plan Amendment, Curtailment or Settlement*[1]
Amendments to IAS 28	*Long-term Interests in Associates and Joint Ventures*[1]
IFRIC 23	*Uncertainty over Income Tax Treatments*[1]
Annual Improvements 2015-2017 Cycle	*Amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23*[1]

1 Effective for annual periods beginning on or after 1 January 2019
2 Effective for annual periods beginning on or after 1 January 2020
3 Effective for annual periods beginning on or after 1 January 2021
4 No mandatory effective date yet determined but available for adoption

Further information about those IFRSs that are expected to be applicable to the Group is described below.

Amendments to IFRS 3 clarify and provide additional guidance on the definition of a business. The amendments clarify that for an integrated set of activities and assets to be considered a business, it must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create output. A business can exist without including all of the inputs and processes needed to create outputs. The amendments remove the assessment of whether market participants are capable of acquiring the business and continue to produce outputs. Instead, the focus is on whether acquired inputs and acquired substantive processes together significantly contribute to the ability to create outputs. The amendments have also narrowed the definition of outputs to focus on goods or services provided to customers, investment income or other income from ordinary activities. Furthermore, the amendments provide guidance to assess whether an acquired process is substantive and introduce an optional fair value concentration test to permit a simplified assessment of whether an acquired set of activities and assets is not a business. The Group expects to adopt the amendments prospectively from 1 January 2020.

2.3 ISSUED BUT NOT YET EFFECTIVE INTERNATIONAL FINANCIAL REPORTING STANDARDS (CONTINUED)

Amendments to IFRS 10 and IAS 28 address an inconsistency between the requirements in IFRS 10 and in IAS 28 in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The amendments require a full recognition of a gain or loss when the sale or contribution of assets between an investor and its associate or joint venture constitutes a business. For a transaction involving assets that do not constitute a business, a gain or loss resulting from the transaction is recognised in the investor's profit or loss only to the extent of the unrelated investor's interest in that associate or joint venture. The amendments are to be applied prospectively. The previous mandatory effective date of amendments to IFRS 10 and IAS 28 was removed by the IASB in December 2015 and a new mandatory effective date will be determined after the completion of a broader review of accounting for associates and joint ventures. However, the amendments are available for adoption now.

IFRS 16, replaces IAS 17 Leases, IFRIC 4 *Determining whether an Arrangement contains a Lease,* SIC 15 *Operating Leases-Incentives* and SIC 27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease.* The standard sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to recognise assets and liabilities for most leases. The standard includes two elective recognition exemptions for lessees – leases of low-value assets and short-term leases. At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). The right-of-use asset is subsequently measured at cost less accumulated depreciation and any impairment losses unless the right-of-use asset meets the definition of investment property in IAS 40, or relates to a class of property, plant and equipment to which the revaluation model is applied. The lease liability is subsequently increased to reflect the interest on the lease liability and reduced for the lease payments. Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset.

Lessees will also be required to remeasure the lease liability upon the occurrence of certain events, such as change in the lease term and change in future lease payments resulting from a change in an index or rate used to determine those payments. Lessees will generally recognise the amount of the re-measurement of the lease liability as an adjustment to the right-of-use asset. Lessor accounting under IFRS 16 is substantially unchanged from the accounting under IAS 17. Lessors will continue to classify all leases using the same classification principle as in IAS 17 and distinguish between operating leases and finance leases. IFRS 16 requires lessees and lessors to make more extensive disclosures than under IAS 17. Lessees can choose to apply the standard using either a full retrospective or a modified retrospective approach.

The Group plans to adopt the transitional provisions in IFRS 16 to recognise the cumulative effect of initial adoption as an adjustment to the opening balance of retained earnings at 1 January 2019 and will not restate the comparatives. In addition, the Group plans to apply the new requirements to contracts that were previously identified as leases applying IAS 17 and measure the lease liability at the present value of the remaining lease payments, discounted using the Group's incremental borrowings rate at the date of initial application. The right-of-use asset will be measured at the amount of the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to the lease recognised in the statement of financial position immediately before the date of initial application. The Group plans to use the exemptions allowed by the standard on lease contracts whose lease terms end within 12 months as of the date of initial application. During the year ended 31 December 2018, the Group has performed a detailed assessment on the impact of adoption of IFRS16. The expected impacts arising from the adoption of IFRS 16 on the Group are not significant.

2.3 ISSUED BUT NOT YET EFFECTIVE INTERNATIONAL FINANCIAL REPORTING STANDARDS (CONTINUED)

Amendments to IAS 1 and IAS 8 provide a new definition of material. The new definition states that information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements. The amendments clarify that materiality will depend on the nature or magnitude of information. A misstatement of information is material if it could reasonably be expected to influence decisions made by the primary users. The Group expects to adopt the amendments prospectively from 1 January 2020. The amendments are not expected to have any significant impact on the Group's financial statements.

Amendments to IAS 28 clarify that the scope exclusion of IFRS 9 only includes interests in an associate or joint venture to which the equity method is applied and does not include long-term interests that in substance form part of the net investment in the associate or joint venture, to which the equity method has not been applied. Therefore, an entity applies IFRS 9, rather than IAS 28, including the impairment requirements under IFRS 9, in accounting for such long-term interests. IAS 28 is then applied to the net investment, which includes the long-term interests, only in the context of recognising losses of an associate or joint venture and impairment of the net investment in the associate or joint venture. The Group expects to adopt the amendments on 1 January 2019 and will assess its business model for such long-term interests based on the facts and circumstances that exist on 1 January 2019 using the transitional requirements in the amendments. The Group also intends to apply the relief from restating comparative information for prior periods upon adoption of the amendments.

IFRIC 23, addresses the accounting for income taxes (current and deferred) when tax treatments involve uncertainty that affects the application of IAS 12 (often referred to as "uncertain tax positions"). The interpretation does not apply to taxes or levies outside the scope of IAS 12, nor does it specifically include requirements relating to interest and penalties associated with uncertain tax treatments. The interpretation specifically addresses (i) whether an entity considers uncertain tax treatments separately; (ii) the assumptions an entity makes about the examination of tax treatments by taxation authorities; (iii) how an entity determines taxable profits or tax losses, tax bases, unused tax losses, unused tax credits and tax rates; and (iv) how an entity considers changes in facts and circumstances. The interpretation is to be applied retrospectively, either fully retrospectively without the use of hindsight or retrospectively with the cumulative effect of application as an adjustment to the opening equity at the date of initial application, without the restatement of comparative information. The Group expects to adopt the interpretation from 1 January 2019. The interpretation is not expected to have any significant impact on the Group's financial statements.

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 Group's investments in associates and joint ventures are stated in the consolidated statement of financial position at the Group's 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 Group's 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. 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 Group's 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 Group's 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 31 December. 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.

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.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Impairment of non-financial assets (continued)

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

(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.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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.

Cost may also include transfers from equity of any gains or losses on qualifying cash flow hedges of foreign currency purchases of property, plant and equipment.

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 and other comprehensive income 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.

Valuations are performed frequently enough to ensure that the fair value of a revalued asset does not differ materially from its carrying amount. Changes in the values of property, plant and equipment are dealt with as movements in the asset revaluation reserve. If the total of this reserve is insufficient to cover a deficit, on an individual asset basis, the excess of the deficit is charged to the statement of profit or loss and other comprehensive income. Any subsequent revaluation surplus is credited to the statement of profit or loss and other comprehensive income to the extent of the deficit previously charged. An annual transfer from the asset revaluation reserve to retained profits is made for the difference between the depreciation based on the revalued carrying amount of an asset and the depreciation based on the asset's original cost. On disposal of a revalued asset, the relevant portion of the asset revaluation reserve realised in respect of previous valuations is transferred to retained profits as a movement in reserves.

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.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Property, plant and equipment and depreciation (continued)

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 borrowings 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 and beef cattle. Dairy cows include milkable cows, heifers and calves which are raised by the Group for the purposes of producing raw milk. Beef cattle are raised by the Group for sale.

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.

Non-current assets and disposal groups are 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.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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.

Computer software

Computer software is stated at cost less any impairment losses and is amortised on the straight-line basis over its estimated useful life of 5 to 10 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.

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.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Leases (continued)

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 (policies under IFRS 9 applicable from 1 January 2018)

Initial recognition and measurement

Financial assets are classified, at initial recognition, as subsequently measured at amortised cost, fair value through other comprehensive income, and fair value through profit or loss.

The classification of financial assets at initial recognition depends on the financial asset's contractual cash flow characteristics and the Group's business model for managing them. With the exception of trade receivables that do not contain a significant financing component or for which the Group has applied the practical expedient of not adjusting the effect of a significant financing component, the Group initially measures a financial asset at its fair value, plus in the case of a financial asset not at fair value through profit or loss, transaction costs. Trade receivables that do not contain a significant financing component or for which the Group has applied the practical expedient are measured at the transaction price determined under IFRS 15 in accordance with the policies set out for "Revenue recognition (applicable from 1 January 2018)" below.

In order for a financial asset to be classified and measured at amortised cost or fair value through other comprehensive income, it needs to give rise to cash flows that are solely payments of principal and interest ("SPPI") on the principal amount outstanding.

The Group's business model for managing financial assets refers to how it manages its financial assets in order to generate cash flows. The business model determines whether cash flows will result from collecting contractual cash flows, selling the financial assets, or both.

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 (policies under IFRS 9 applicable from 1 January 2018) (continued)

Subsequent measurement

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

Financial assets at amortised cost (debt instruments)

The Group measures financial assets at amortised cost if both of the following conditions are met:

- The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows.
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Financial assets at amortised cost are subsequently measured using the effective interest method and are subject to impairment. Gains and losses are recognised in profit or loss when the asset is derecognised, modified or impaired.

Financial assets at fair value through other comprehensive income (debt instruments)

The Group measures debt investments at fair value through other comprehensive income if both of the following conditions are met:

- The financial asset is held within a business model with the objective of both holding to collect contractual cash flows and selling.
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

For debt investments at fair value through other comprehensive income, interest income, foreign exchange revaluation and impairment losses or reversals are recognised in profit or loss and computed in the same manner as for financial assets measured at amortised cost. The remaining fair value changes are recognised in other comprehensive income. Upon derecognition, the cumulative fair value change recognised in other comprehensive income is recycled to profit or loss.

Financial assets designated at fair value through other comprehensive income (equity investments)

Upon initial recognition, the Group can elect to classify irrevocably its equity investments as equity investments designated at fair value through other comprehensive income when they meet the definition of equity under IAS 32 Financial Instruments: Presentation and are not held for trading. The classification is determined on an instrument-by-instrument basis.

Gains and losses on these financial assets are never recycled to profit or loss. Dividends are recognised as other income in the statement of profit or loss and other comprehensive income when the right of payment has been established, it is probable that the economic benefits associated with the dividend will flow to the Group and the amount of the dividend can be measured reliably, except when the Group benefits from such proceeds as a recovery of part of the cost of the financial asset, in which case, such gains are recorded in other comprehensive income. Equity investments designated at fair value through other comprehensive income are not subject to impairment assessment.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Investments and other financial assets (policies under IFRS 9 applicable from 1 January 2018) (continued)

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading, financial assets designated upon initial recognition at fair value through profit or loss, or financial assets mandatorily required to be measured at fair value. Financial assets are classified as held for trading if they are acquired for the purpose of selling or repurchasing in the near term. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments. Financial assets with cash flows that are not solely payments of principal and interest are classified and measured at fair value through profit or loss, irrespective of the business model. Notwithstanding the criteria for debt instruments to be classified at amortised cost or at fair value through other comprehensive income, as described above, debt instruments may be designated at fair value through profit or loss on initial recognition if doing so eliminates, or significantly reduces, an accounting mismatch.

Financial assets at fair value through profit or loss are carried in the statement of financial position at fair value with net changes in fair value recognised in profit or loss.

This category includes derivative instruments and equity investments which the Group had not irrevocably elected to classify at fair value through other comprehensive income. Dividends on equity investments classified as financial assets at fair value through profit or loss are also recognised as other income in the statement of profit or loss and other comprehensive income when the right of payment has been established, it is probable that the economic benefits associated with the dividend will flow to the Group and the amount of the dividend can be measured reliably.

A derivative embedded in a hybrid contract, with a financial liability or non-financial host, is separated from the host and accounted for as a separate derivative if the economic characteristics and risks are not closely related to the host; a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and the hybrid contract is not measured at fair value through profit or loss. 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.

A derivative embedded within a hybrid contract containing a financial asset host is not accounted for separately. The financial asset host together with the embedded derivative is required to be classified in its entirety as a financial asset at fair value through profit or loss.

Investments and other financial assets (policies under IAS 39 applicable before 1 January 2018)

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 (policies under IAS 39 applicable before 1 January 2018) (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 losses and negative net changes in fair value presented as finance costs in the statement of profit or loss and other comprehensive income. 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 (applicable before 1 January 2018)" 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 losses 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 (policies under IAS 39 applicable before 1 January 2018) (continued)

Subsequent measurement (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 (applicable before 1 January 2018)" 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.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Derecognition of financial assets (policies under IFRS 9 applicable from 1 January 2018 and policies under IAS 39 applicable before 1 January 2018)

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.

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 (policies under IFRS 9 applicable from 1 January 2018)

The Group recognises an allowance for ECLs for all debt instruments not held at fair value through profit or loss. ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Group expects to receive, discounted at an approximation of the original effective interest rate. The expected cash flows will include cash flows from the sale of collateral held or other credit enhancements that are integral to the contractual terms.

General approach

ECLs are recognised in two stages. For credit exposures for which there has not been a significant increase in credit risk since initial recognition, ECLs are provided for credit losses that result from default events that are possible within the next 12-months (a 12-month ECL). For those credit exposures for which there has been a significant increase in credit risk since initial recognition, a loss allowance is required for credit losses expected over the remaining life of the exposure, irrespective of the timing of the default (a lifetime ECL).

At each reporting date, the Group assesses whether the credit risk on a financial instrument has increased significantly since initial recognition. When making the assessment, the Group compares the risk of a default occurring on the financial instrument as at the reporting date with the risk of a default occurring on the financial instrument as at the date of initial recognition and considers reasonable and supportable information that is available without undue cost or effort, including historical and forward-looking information.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Impairment of financial assets (policies under IFRS 9 applicable from 1 January 2018) (continued)

General approach (continued)

For debt investments at fair value through other comprehensive income, the Group applies the low credit risk simplification. At each reporting date, the Group evaluates whether the debt investments are considered to have low credit risk using all reasonable and supportable information that is available without undue cost or effort. In making that evaluation, the Group reassesses the external credit ratings of the debt investments. In addition, the Group considers that there has been a significant increase in credit risk when contractual payments are more than 30 days past due.

The Group considers a financial asset in default when contractual payments are 90 days past due. However, in certain cases, the Group may also consider a financial asset to be in default when internal or external information indicates that the Group is unlikely to receive the outstanding contractual amounts in full before taking into account any credit enhancements held by the Group. A financial asset is written off when there is no reasonable expectation of recovering the contractual cash flows.

Debt investments at fair value through other comprehensive income and financial assets at amortised cost are subject to impairment under the general approach and they are classified within the following stages for measurement of ECLs except for trade receivables and contract assets which apply the simplified approach as detailed below.

Stage 1 – Financial instruments for which credit risk has not increased significantly since initial recognition and for which the loss allowance is measured at an amount equal to 12-month ECLs

Stage 2 – Financial instruments for which credit risk has increased significantly since initial recognition but that are not credit-impaired financial assets and for which the loss allowance is measured at an amount equal to lifetime ECLs

Stage 3 – Financial assets that are credit-impaired at the reporting date (but that are not purchased or originated credit-impaired) and for which the loss allowance is measured at an amount equal to lifetime ECLs

Simplified approach

For trade receivables and contract assets that do not contain a significant financing component or when the Group applies the practical expedient of not adjusting the effect of a significant financing component, the Group applies the simplified approach in calculating ECLs. Under the simplified approach, the Group does not track changes in credit risk, but instead recognises a loss allowance based on lifetime ECLs at each reporting date. The Group has established a provision matrix that is based on its historical credit loss experience, adjusted for forward-looking factors specific to the debtors and the economic environment.

For trade receivables and contract assets that contain a significant financing component and lease receivables, the Group chooses as its accounting policy to adopt the simplified approach in calculating ECLs with policies as described above.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Impairment of financial assets (policies under IAS 39 applicable before 1 January 2018)

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.

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.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Impairment of financial assets (policies under IAS 39 applicable before 1 January 2018) (continued)

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 and other comprehensive income. 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 and other comprehensive income 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 and other comprehensive income.

Financial liabilities (policies under IFRS 9 applicable from 1 January 2018 and IAS 39 applicable before 1 January 2018)

Initial recognition and measurement

Financial liabilities are classified, at initial recognition, as financial liabilities at fair value through profit or loss, loans and borrowings, payables, 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 and payables, net of directly attributable transaction costs.

The Group's financial liabilities include trade and other payables, an amount due to the ultimate holding company, derivative financial instruments and interest-bearing bank and other borrowings.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Financial liabilities (policies under IFRS 9 applicable from 1 January 2018 and IAS 39 applicable before 1 January 2018) (continued)

Subsequent measurement

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

Financial liabilities at fair value through profit or loss (policies under IFRS 9 applicable from 1 January 2018)

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 incurred for the purpose of repurchasing in the near term. This category also includes derivative financial instruments entered into by the Group that are not designated as hedging instruments in hedge relationships as defined by IFRS 9. 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 initial date of recognition, and only if the criteria in IFRS 9 are satisfied. Gains or losses on liabilities designated at fair value through profit or loss are recognised in profit or loss, except for the gains or losses arising from the Group's own credit risk which are presented in other comprehensive income with no subsequent reclassification to profit or loss. The net fair value gain or loss recognised in profit or loss not include any interest charged on these financial liabilities.

Financial liabilities at fair value through profit or loss (policies under IAS 39 applicable before 1 January 2018)

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.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Impairment of financial assets (policies under IAS 39 applicable before 1 January 2018) (continued)

Financial guarantee contracts (policies under IFRS 9 applicable from 1 January 2018)

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 contracts at the higher of: (i) the ECL allowance determined in accordance with the policy as set out in "Impairment of financial assets (policies under IFRS 9 applicable from 1 January 2018)"; and (ii) the amount initially recognised less, when appropriate, the cumulative amount of income recognised.

Financial guarantee contracts (policies under IAS 39 applicable before 1 January 2018)

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.

Derecognition of financial liabilities (policies under IFRS 9 applicable from 1 January 2018 and IAS 39 applicable before 1 January 2018)

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 (policies under IFRS 9 applicable from 1 January 2018 and IAS 39 applicable before 1 January 2018)

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.

Derivative financial instruments (policies under IFRS 9 applicable from 1 January 2018 and IAS 39 applicable before 1 January 2018)

Initial recognition and subsequent measurement

Derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

Any gains or losses arising from changes in fair value of derivatives are taken directly to profit or loss, except for the effective portion of cash flow hedges, which is recognised in other comprehensive income and later reclassified to profit or loss when the hedged item affects profit or loss.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 consolidated 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, less bank overdrafts which are repayable on demand and form an integral part of the Group's cash management.

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.

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.

Provision for product warranties granted by the Group on certain products are recognized 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.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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.

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 and only if the Group has a legally enforceable right to set off current tax assets and current tax liabilities and the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities which intend either to settle current tax liabilities and assets on a net basis, or to realise the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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.

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.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Revenue recognition (applicable from 1 January 2018)

Revenue from contracts with customers

Revenue from contracts with customers is recognised when control of goods or services is transferred to the customers at an amount that reflects the consideration to which the Group expects to be entitled in exchange for those goods or services.

When the consideration in a contract includes a variable amount, the amount of consideration is estimated to which the Group will be entitled in exchange for transferring the goods or services to the customer. The variable consideration is estimated at contract inception and constrained until it is highly probable that a significant revenue reversal in the amount of cumulative revenue recognised will not occur when the associated uncertainty with the variable consideration is subsequently resolved.

When the contract contains a financing component which provides the customer a significant benefit of financing the transfer of goods or services to the customer for more than one year, revenue is measured at the present value of the amount receivable, discounted using the discount rate that would be reflected in a separate financing transaction between the Group and the customer at contract inception. When the contract contains a financing component which provides the Group a significant financial benefit for more than one year, revenue recognised under the contract includes the interest expense accreted on the contract liability under the effective interest method. For a contract where the period between the payment by the customer and the transfer of the promised goods or services is one year or less, the transaction price is not adjusted for the effects of a significant financing component, using the practical expedient in IFRS 15.

Sale of goods

Revenue from the sale of goods is recognised at the point in time when control of the asset is transferred to the customer, generally on delivery of the goods.

Revenue from other sources

Rental income is recognised on a time proportion basis over the lease terms.

Other income

Interest income is recognised 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.

Dividend income is recognised when the shareholders' right to receive payment has been established, it is probable that the economic benefits associated with the dividend will flow to the Group and the amount of the dividend can be measured reliably.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Revenue recognition (applicable before 1 January 2018)

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) from the rendering of services, on the percentage of completion basis, as further explained in the accounting policy for "Contracts for services (applicable before 1 January 2018)" below;

c) rental income, on a time proportion basis over the lease terms;

d) 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;

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

Contract assets (applicable from 1 January 2018)

A contract asset is the right to consideration in exchange for goods or services transferred to the customer. If the Group performs by transferring goods or services to a customer before the customer pays consideration or before payment is due, a contract asset is recognised for the earned consideration that is conditional.

Contract liabilities (applicable from 1 January 2018)

A contract liability is the obligation to transfer goods or services to a customer for which the Group has received a consideration (or an amount of consideration that is due) from the customer. If a customer pays the consideration before the Group transfers goods or services to the customer, a contract liability is recognised when the payment is made or the payment is due (whichever is earlier). Contract liabilities are recognised as revenue when the Group performs under the contract.

Contracts for services (applicable before 1 January 2018)

Contract revenue on the rendering of services comprises the agreed contract amount. Costs of rendering services comprise labour and other costs of personnel directly engaged in providing the services and attributable overheads.

Revenue from the rendering of services is recognised based on the percentage of completion of the transaction, provided that the revenue, the costs incurred and the estimated costs to completion can be measured reliably. The percentage of completion is established by reference to the costs incurred to date as compared to the total costs to be incurred under the transaction. Where the outcome of a contract cannot be measured reliably, revenue is recognised only to the extent that the expenses incurred are eligible to be recovered.

Provision is made for foreseeable losses as soon as they are anticipated by management. Where contract costs incurred to date plus recognised profits less recognised losses exceed progress billings, the surplus is treated as an amount due from contract customers. Where progress billings exceed contract costs incurred to date plus recognised profits less recognised losses, the surplus is treated as an amount due to contract customers.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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.

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.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Other employee benefits

Pension scheme

The employees of the Group's 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.

Borrowings costs

Borrowings 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 borrowings 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 borrowings costs capitalised. All other borrowings costs are expensed in the period in which they are incurred. Borrowings costs consist of interest and other costs that an entity incurs in connection with the borrowings 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. Proposed final dividends are disclosed in the notes to the financial statements.

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.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Foreign currencies (continued)

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).

In determining the exchange rate on initial recognition of the related asset, expense or income on the derecognition of a non-monetary asset or non-monetary liability relating to an advance consideration, the date of initial transaction is the date on which the Group initially recognises the non-monetary asset or non-monetary liability arising from the advance consideration. If there are multiple payments or receipts in advance, the Group determines the transaction date for each payment or receipt of the advance consideration.

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.

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.

2.5 CORRECTION OF PRIOR PERIOD ERRORS

During the year, the Group identified guarantees issued by the Group in previous years which had not been disclosed or accounted for in its financial statements The guarantees were issued for bank facilities granted by banks to the Group's distributors and associated companies.

1. During the year ended 31 December 2017, the Group provided joint guarantees to banks for the bank loans of RMB180,000,000 granted to its distributors.

2. On 28 August 2017, the Group provided guarantees to the bank for the bank loans of RMB92,600,000 granted to Bayannur Shengmu High-tech Ecological Forage Co., Ltd. ("Shengmu Forage "), an associated company of the Group and a key supplier to the Group.

3. Since 20 September 2016, the Group has provided a guarantee to the bank for the one-year bank loan of RMB30,000,000 of Shengmu Forage. The guarantee period was extended upon the renewal of the bank loan during the year ended 31 December 2017. The guarantee expired upon the repayment of the bank loan on 10 February 2019.

4. On 13 October 2017, the Group provided a joint guarantee to the bank for the bank loans of RMB130,000,000 granted to Shengmu Forage, along with Mr. Tongshan Yao, a shareholder and a director of the Company.

5. Since 21 October 2016, the Group has provided guarantees to the bank for the three-year revolving loan facility with a cap amounting to RMB133,000,000 granted to Food Union Shengmu Dairy Co., Ltd. ("Food Union Shengmu"), an associated company of the Group. As at 31 December 2017, the utilised balance of the bank loan was RMB102,880,000.

The Group has quantified the financial impact of the guarantees on its financial statements and their impact on the Company's consolidated financial statements as at 31 December 2017 and 1 January 2017 are provided in the tables below.

2.5 CORRECTION OF PRIOR PERIOD ERRORS (CONTINUED)

A summary of the effect of the restatement on the applicable line items within the Company's consolidated statement of financial position as of 31 December 2017 and 1 January 2017 were as follows:

	Consolidated Statement of Financial Position As at 31 December 2017		
	As Reported	Adjustments for guarantees	Restated
	RMB'000	RMB'000	RMB'000
Other payables and accruals	441,718	40,669	482,387
Total current liabilities	4,300,883	40,669	4,341,552
Reserves	4,356,281	(40,669)	4,315,612
Total equity	5,415,782	(40,669)	5,375,113

	Consolidated Statement of Financial Position As at 1 January 2017		
	As Reported	Adjustments for guarantees	Restated
	RMB'000	RMB'000	RMB'000
Other payables and accruals	438,550	11,192	449,742
Total current liabilities	2,292,318	11,192	2,303,510
Reserves	5,338,989	(11,192)	5,327,797
Total equity	6,347,127	(11,192)	6,335,935

2.5 CORRECTION OF PRIOR PERIOD ERRORS (CONTINUED)

A summary of the effect of the restatement on the applicable line items within the Company's consolidated statement of profit or loss and other comprehensive income for the year ended 31 December 2017 were as follows:

	As Reported	Adjustments	Restated-Group	Restated-Continuing operations
	RMB'000	RMB'001	RMB'000	RMB'000
Cost of sales	(1,622,474)	(1,358)	(1,623,832)	(792,295)
Other income and gains/(losses)	(732,855)	8,843	(724,012)	(13,550)
Selling and distribution expenses	(317,400)	(36,962)	(354,362)	(34,907)
(Loss)/profit before tax	(831,853)	(29,477)	(861,330)	199,368
(Loss)/profit for the year	(824,313)	(29,477)	(853,790)	199,345
Total comprehensive income/(loss) for the year	(821,232)	(29,477)	(850,709)	202,426
(Loss)/profit attributable to owners of the parent	(985,789)	(29,477)	(1,015,266)	37,869
Total comprehensive income/(loss) attributable to owners of the parent	(982,708)	(29,477)	(1,012,185)	40,950
Basic (loss)/profit per share attributable to ordinary equity holders of the parent	(0.155)	(0.005)	(0.160)	0.006
Diluted (loss)/profit per share attributable to ordinary equity holders of the parent	(0.155)	(0.005)	(0.160)	0.006

The correction of prior period errors did not have impact on the Group's operating, investing and financing cash flows.

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 judgement, apart from those involving estimations, which has the most significant effect on the amounts recognised in the financial statements:

Withholding tax arising from the distributions 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 31 December 2018, the deferred tax liabilities arising thereon amounted to nil (2017: Nil).

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 biological assets

The Group's biological assets are valued at fair value less costs to sell. The fair value of biological assets 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 characteristics and/or stages of growth of biological assets; or the present value of expected net cash flows from the biological assets 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 biological assets significantly. The independent qualified professional valuer and management review the assumptions and estimates periodically to identify any significant change in fair value of biological assets. Further details are given in note 18 to the financial statements.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (CONTINUED)

Estimation uncertainty (continued)

Provision for expected credit losses on trade receivables and contract assets

The Group sets up its expected credit loss provision estimation policy based on their historical experience, expected risk estimation and comparative data analysis of industries.

The Group uses a provision matrix to calculate ECLs for trade receivables and contract assets. The provision rates are based on days past due for groupings of various customer segments that have similar loss patterns (i.e., by geography, product type, customer type and rating, and coverage by letters of credit and other forms of credit insurance).

The provision matrix is initially based on the Group's historical observed default rates. The Group will calibrate the matrix to adjust the historical credit loss experience with forward-looking information. For instance, if forecast economic conditions (i.e., gross domestic products) are expected to deteriorate over the next year which can lead to an increased number of defaults in the manufacturing sector, the historical default rates are adjusted. At each reporting date, the historical observed default rates are updated and changes in the forward-looking estimates are analysed.

The assessment of the correlation among historical observed default rates, forecast economic conditions and ECLs is a significant estimate. The amount of ECLs is sensitive to changes in circumstances and forecast economic conditions. The Group's historical credit loss experience and forecast of economic conditions may also not be representative of the customers actual default in the future. The information about the ECLs on the Group's trade receivables and financial assets included in prepayments, other receivables and other assets is disclosed in notes 20 and 24 to the financial statements, respectively.

Fair value of financial guarantee contracts and provision for expected credit losses on financial guarantee contracts

The Group's financial guarantee contracts are recognised initially as a liability at their fair value, adjusted for transaction costs that are directly attributable to the issuance of the guarantees. Subsequent to initial recognition, the Group measures the financial guarantee contracts at the higher of: (i) the ECL allowance determined in accordance with the policy as set out in "Impairment of financial assets (policies under IFRS 9 applicable from 1 January 2018)"; and (ii) the amount initially recognised less, when appropriate, the cumulative amount of income recognised. The fair value of the financial guarantee contracts are determined based on the valuation method which take into account the credit rating of guarantees, maturity date of the guarantee contracts, default rates, credit loss ratio, discount rate, risk free interest rate etc. Any changes in the estimates may affect the fair value of the financial guarantee contracts significantly. The independent qualified professional valuer and management review the assumptions and estimates periodically to identify any significant change in fair value of financial guarantee contracts. At each reporting date, the historical observed default rates are updated and changes in the forward-looking estimates are analysed. The assessment of the correlation among the credit rating of guarantees, historical observed default rates, credit loss ratio, forecast economic conditions and ECLs is a significant estimate. The amount of ECLs is sensitive to changes in the assumption, circumstances and forecast economic conditions. The Group's historical credit loss experience and forecast of economic conditions may also not be representative of the guarantee's actual default in the future. Further details are given in note 27 to the financial statements.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (CONTINUED)

Estimation uncertainty (continued)

Impairment of raw materials

Management estimates the net realisable value of raw materials based on the estimated selling prices 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.

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.

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.

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. Further details are contained in note 19 to the financial statements.

Fair value of unlisted equity investments

The unlisted equity investments have been valued based on a market-based valuation technique as detailed in note 39 to the financial statements. The valuation requires the Group to determine the comparable public companies (peers) and select the price multiple. In addition, the Group makes estimates about the discount for illiquidity and size differences. The Group classifies the fair value of these investments as Level 3. The fair value of the unlisted equity investments at 31 December 2018 was nil (2017: Nil). Further details are included in note 10 to the financial statements.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (CONTINUED)

Estimation uncertainty (continued)

Impairment of available-for-sale financial assets

Before 1 January 2018, the Group classified certain assets as available for sale and recognised movements of their fair values in equity. When the fair value declined, management made assumptions about the decline in value to determine whether there was an impairment that should be recognised in the statement of profit or loss and other comprehensive income. At 31 December 2017, no impairment losses have had been recognised for available-for-sale assets. Further details are included in note 17 to the financial statements.

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

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

	2018 RMB'000	2017 RMB'000
Revenue from contracts with customers		
Sales of goods	2,164,449	1,860,722
Other income and gains/(losses)		
Government grants	11,382	261
Bank interest income	6,855	8,387
Foreign exchange differences, net	4,502	(27,968)
Loss on disposal of items of property, plant and equipment from continuing operations	(1,074)	(2,396)
Impairment loss of financial guarantee contracts	—	(1,201)
Fair value losses, net:		
Derivative financial instruments	(6,539)	—
Others	(2,550)	9,367
	12,576	(13,550)

5. (LOSS)/PROFIT BEFORE TAX

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

	2018 RMB'000	2017 RMB'000
Cost of inventories sold	1,468,427	792,295
Loss arising from changes in fair value less costs to sell of biological assets	1,321,554	595,479
Depreciation of items of property, plant and equipment from continuing operations	151,168	139,417
Amortisation of prepaid land lease payments from continuing operations	1,431	2,055
Amortisation of other intangible assets from continuing operations	1,274	1,109
Research and development costs	5,156	6,554
Minimum lease payments under operating leases	1,200	1,200
Auditor's remuneration	4,283	2,318
Impairment losses on financial and contract assets	91,345	—
Employee benefit expense (including directors' and chief executive's remuneration (note 7):		
Wages, salaries, bonuses and allowances	211,395	204,562
Other social insurances and benefits	11,955	14,937
Pension scheme contributions	11,318	9,531
	234,668	229,030

6. FINANCE COSTS

	2018 RMB'000	2017 RMB'000
Interest on bank loans and other loans	59,836	60,233
Interest on short-term notes	6,133	14,300
Interest on corporate bonds	77,234	77,052
Interest on long term payables	3,868	5,040
Less: interest capitalised	(2,076)	(10,610)
	`144,995	146,015

The capitalisation rates used to determine the amount of borrowing costs eligible for capitalisation for the year ended 31 December 2018 ranged between 1.55% and 12.97% (2017: between 1.55% and 6.98%).

7. 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:

	2018 RMB'000	2017 RMB'000
Fees	480	580
Other emoluments:		
Salaries, allowances and benefits in kind	1,329	1,278
Pension scheme contributions	36	44
	1,365	1,322
	1,845	1,902

(a) Independent non-executive directors

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

	2018 RMB'000	2017 RMB'000
Mr. LI Changqing	50	100
Ms.GE Xiaoping	50	100
Mr. YUAN Qing	—	50
Mr. WONG Kun Kau	—	50
Mr. WANG Liyan	100	50
Mr. LI Xuan	100	50
Mr. Fu Wenge	100	100
	400	500

7. DIRECTORS' AND CHIEF EXECUTIVE'S REMUNERATION (CONTINUED)

There were no other emoluments payable to the independent non-executive directors during the year (2017: nil).

(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
2018				
Executive directors:				
Mr. YAO Tongshan^	20	320	—	340
Mr. WU Jianye	20	346	12	378
Ms. GAO Lingfeng*	20	346	12	378
Mr. CUI Ruicheng**	20	317	12	349
Mr. WANG Yuehua#	—	—	—	—
	80	1,329	36	1,445
Non-executive directors:				
Mr. WEN Yongping	—	—	—	—
Mr. FAN Xiang	—	—	—	—
Mr. CUI Guiyong	—	—	—	—
Mr. SUN Qian	—	—	—	—
Mr. SHAO Genhuo	—	—	—	—
Mr. ZHANG Jiawang	—	—	—	—
	80	1,329	36	1,445
2017				
Executive directors:				
Mr. YAO Tongshan	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. WEN Yongping	—	—	—	—
Mr. DONG Xianli	—	—	—	—
Mr. FAN Xiang	—	—	—	—
Mr. CUI Guiyong	—	—	—	—
Mr. SUN Qian	—	—	—	—
Mr. SHAO Genhuo	—	—	—	—
Mr. ZHANG Jiawang	—	—	—	—
	80	1,278	44	1,402

7. DIRECTORS' AND CHIEF EXECUTIVE'S REMUNERATION (CONTINUED)

^ As Mr. YAO Tongshan has already reached the statutory retirement age in January 2018. He did not make pension scheme contribution during the year ended 31 December 2018.

* Since 29 June 2018, Ms. GAO Lingfeng has ceased to be an executive director of the Group. Although she was not an executive director as at 31 December 2018, Ms. GAO Lingfeng has been an executive vice-president of the Group. Therefore, remuneration paid to Ms. GAO Lingfeng after 29 June 2018 was included in directors' remuneration.

** Since 29 June 2018, Mr. CUI Ruicheng has ceased to be an executive director of the Group.

Mr. Wang Yuehua was appointed as an executive director of the Group on 29 June 2018. As Mr. Wang Yuehua has been remunerated by Beijing Dabeinong Technology Group Co.,Ltd, one of the Group's shareholders, Mr. Wang Yuehua agreed to waive any remuneration in the Group.

Save as disclosed above, there was no arrangement under which a director or the chief executive officer waived or agreed to waive any remuneration during the year.

8. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the year included two executive directors (2017: four), details of whose remuneration are set out in note 7 above. Details of the remuneration for the year of the remaining three (2017: one) highest paid employee, who are neither a director nor chief executive of the Company are as follows:

	2018 RMB'000	2017 RMB'000
Pension scheme contributions	46	11
Salaries, allowances and benefits in kind	1,132	427
	1,178	438

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	
	2018	2017
Nil to HK$1,000,000	3	1

9. INCOME TAX

	2018 RMB'000	2017 RMB'000
Current - PRC	130	23
Deferred (note 19)	(410)	—
Total tax charge/(credit) for the year from continuing operations	(280)	23
Current - PRC	(3,791)	—
Deferred (note 19)	31,980	(7,563)
Total tax charge/(credit) for the year from a discontinued operation (note 10)	28,189	(7,563)
	27,909	(7,540)

A reconciliation of the tax credit applicable to loss 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:

	2018 RMB'000	2017 RMB'000
(Loss)/profit before tax from continuing operations	(1,047,497)	199,368
Loss before tax from a discontinued operation	(1,235,811)	(1,060,698)
	(2,283,308)	(861,330)
Tax at the statutory tax rate (note (i))	(570,827)	(215,333)
Lower tax rate for specific provinces or enacted by local authority (note (iii))	25,413	51,585
Prior year adjustment	3,667	—
Loss/(income) not subject to tax (note (ii))	268,288	(18,179)
Expenses not deductible for tax (note (iv))	291,572	168,170
Tax losses not recognised	9,796	6,217
Tax charge/(credit) at the group's effective rate	27,909	(7,540)
Tax charge/(credit) from continuing operations at the effective rate	(280)	23
Tax charge/(credit) from a discontinued operation at the effective rate	28,189	(7,563)

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 31 December 2018 (2017: 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 the 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 ECLs/impairment losses of trade receivables and other receivables, share of losses of associates and staff welfares exceeding the tax limit.

10. DISCONTINUED OPERATION

On 23 December 2018, the Company announced the decision of its board of directors to dispose of 51% of the equity interests of Inner Mongolia Shengmu High-tech Dairy Co.,Ltd. ("Shengmu Dairy") and Hohhot Shengmu High-tech Dairy Co.,Ltd. ("Hohhot Dairy") to Inner Mongolia Mengniu Dairy (Group) Co., Ltd. ("Inner Mongolia Mengniu"), a subsidiary of China Mengniu Dairy Limited ("China Mengniu"). Shengmu Dairy and Hohhot Dairy engage in producing and distributing liquid milk products. The disposal of Shengmu Dairy and Hohhot Dairy is due to be completed in 2019. As at 31 December 2018, final negotiation for the transaction was in progress and Shengmu Dairy and Hohhot Dairy were classified as a disposal group held for sale and as a discontinued operation.

With Shengmu Dairy and Hohhot Dairy, which comprised the majority of liquid milk business, being classified as a discontinued operation, presentation of operating segment information is no longer required as the Group only has the dairy farming business retained upon the disposal of the liquid milk business.

The results of Shengmu Dairy and Hohhot Dairy for the year are presented below:

	2018 RMB'000	2017 RMB'000
Revenue	722,718	846,120
Cost of sales	(479,159)	(831,537)
Gross profit from the discontinued operation	243,559	14,583
Other income and losses	14,692	(710,462)
Selling and distribution expenses	(277,361)	(319,455)
Administrative expenses	(32,395)	(26,316)
Finance costs	(10,760)	(4,516)
Other expenses	(60,822)	(10,595)
Share of losses of associates	(469)	(3,937)
Impairment losses on financial and contract assets*	(1,112,255)	—
Loss before tax from the discontinued operation	(1,235,811)	(1,060,698)
Income tax (expense)/credit (note 9)	(28,189)	7,563
Loss for the year from the discontinued operation	(1,264,000)	(1,053,135)

* Included in impairment losses on financial and contract assets were expected credit losses provided for trade and other receivables of RMB1,096,288,000 for the year ended 31 December 2018 (2017: RMB656,054,000 included in other income and losses).

10. DISCONTINUED OPERATION (CONTINUED)

The major classes of assets and liabilities of Shengmu Dairy and Hohhot Dairy classified as held for sale as at 31 December are as follows:

	2018 RMB'000	2017 RMB'000
Assets		
Property, plant and equipment (note 13)	588,815	—
Prepaid land lease payments (note 14)	17,965	—
Other intangible assets (note 15)	4,975	—
Investments in associates	184	—
Deferred tax assets (note 19)	217	—
Inventories	32,888	—
Trade and bills receivables	97,434	—
Prepayments, other receivables and other assets	86,208	—
Pledged deposits	146,438	—
Cash and bank balances	3,231	—
Assets classified as held for sale	978,355	—
Liabilities		
Trade payables and bills payables	459,221	—
Other payables and accruals	228,945	—
Interest-bearing bank and other borrowings	101,840	—
Liabilities directly associated with the assets classified as held for sale	790,006	—
Net assets directly associated with the disposal group	188,349	—

At 31 December 2018, certain machinery and equipment with a net carrying amount of RMB30,000,000 (2017: nil) of the discontinued operation were pledged to secure other borrowings granted to the discontinued operation.

The net cash flows incurred by Shengmu Dairy and Hohhot Dairy are as follows:

	2018 RMB'000	2017 RMB'000
Operating activities	25,721	(286,546)
Investing activities	(126,713)	(80,227)
Financing activities	81,564	377,229
Net cash (outflows)/inflows	(19,428)	10,456
Loss per share:		
Basic, from the discontinued operation	(RMB0.199)	(RMB0.166)
Diluted, from the discontinued operation	(RMB0.199)	(RMB0.166)

10. DISCONTINUED OPERATION (CONTINUED)

The calculations of basic and diluted loss per share from the discontinued operation are based on:

	2018 RMB'000	2017 RMB'000
Loss attributable to ordinary equity holders of the parent from the discontinued operation	1,264,000,000	1,053,135,000
Weighted average number of ordinary shares in issue during the year used in the basic earnings per share calculation (note 12)	6,354,400,000	6,354,400,000
Weighted average number of ordinary shares used in the diluted earnings per share calculation (note 12)	6,354,400,000	6,354,400,000

11. DIVIDENDS

The Directors do not recommend the payment of any dividend for the year ended 31 December 2018 (2017: nil).

12. (LOSS)/EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT

The basic (loss)/earnings per share amount is calculated by dividing the (loss)/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 (2017: 6,354,400,000) in issue during the year.

The diluted (loss)/earnings per share amount is calculated by dividing the (loss)/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 (loss)/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.

The Group had no potentially dilutive ordinary shares in issue during the year ended 31 December 2018 (2017:nil).

	Number of shares	
	2018	2017
Weighted average number of ordinary shares in issue during the year used in the basic loss per share calculation	6,354,400,000	6,354,400,000
Weighted average number of ordinary shares in issue during the year used in the diluted loss per share calculation	6,354,400,000	6,354,400,000

13. PROPERTY, PLANT AND EQUIPMENT

	Buildings RMB'000	Machinery and equipment RMB'000	Office and other equipment RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
31 December 2018						
At 31 December 2017 and at 1 January 2018						
Cost	2,068,256	976,304	50,571	9,908	225,635	3,330,674
Accumulated depreciation	(244,723)	(260,826)	(21,289)	(5,508)	—	(532,346)
Net carrying amount	1,823,533	715,478	29,282	4,400	225,635	2,798,328
At 1 January 2018,net of accumulated depreciation	1,823,533	715,478	29,282	4,400	225,635	2,798,328
Additions	9,912	10,282	1,128	348	68,980	90,650
Reclassification	48	—	(48)	—	—	—
Transfers	94,802	36,769	808	—	(132,379)	—
Disposals	—	(560)	(824)	(136)	—	(1,520)
Assets included in a discontinued operation (note 10)	(203,746)	(362,796)	(7,351)	(534)	(14,388)	(588,815)
Depreciation provided during the year	(99,367)	(102,610)	(8,246)	(1,375)	—	(211,598)
At 31 December 2018, net of accumulated depreciation	1,625,182	296,563	14,749	2,703	147,848	2,087,045
At 31 December 2018						
Cost	1,939,985	503,744	37,271	8,459	147,848	2,637,307
Accumulated depreciation	(314,803)	(207,181)	(22,522)	(5,756)	—	(550,262)
Net carrying amount	1,625,182	296,563	14,749	2,703	147,848	2,087,045

13. 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
31 December 2017						
At 1 January 2017	1,721,851	834,018	56,828	9,067	435,492	3,057,256
Cost	(157,253)	(169,951)	(14,916)	(4,768)	—	(346,888)
Accumulated depreciation	1,564,598	664,067	41,912	4,299	435,492	2,710,368
Net carrying amount	1,564,598	664,067	41,912	4,299	435,492	2,710,368
At 1 January 2017, net of accumulated depreciation						
Additions	24	32,483	4,448	1,351	238,239	276,545
Reclassification	2,201	15,380	(17,581)	—	—	—
Transfers	344,185	96,146	7,265	500	(448,096)	—
Disposals	(4)	(917)	(161)	(253)	—	(1,335)
Depreciation provided during the year	(87,471)	(91,681)	(6,601)	(1,497)	—	(187,250)
At 31 December 2017, net of accumulated depreciation	1,823,533	715,478	29,282	4,400	225,635	2,798,328
At 31 December 2017						
Cost	2,068,256	976,304	50,571	9,908	225,635	3,330,674
Accumulated depreciation	(244,723)	(260,826)	(21,289)	(5,508)	—	(532,346)
Net carrying amount	1,823,533	715,478	29,282	4,400	225,635	2,798,328

14. PREPAID LAND LEASE PAYMENTS

	2018 RMB'000	2017 RMB'000
Carrying amount at 1 January	38,058	38,822
Additions	1,891	1,487
Prepaid land lease payments included in a discontinued operation (note 10)	(17,965)	—
Current portion included in prepayments, other receivables and other assets included in a discontinued operation	(195)	—
Recognised during the year	(1,626)	(2,251)
Carrying amount at 31 December	20,163	38,058
Current portion included in prepayments, other receivables and other assets	(1,318)	(1,508)
Non-current portion	18,845	36,550

15. OTHER INTANGIBLE ASSETS

	Technical know-how RMB'000	Computer software RMB'000	Total RMB'000
31 December 2018			
Cost at 1 January 2018, net of accumulated amortisation	10,129	3,482	13,611
Additions	—	4,516	4,516
Assets included in a discontinued operation (note 10)	—	(4,975)	(4,975)
Amortisation provided during the year	(750)	(939)	(1,689)
At 31 December 2018	9,379	2,084	11,463
At 31 December 2018			
Cost	15,004	3,885	18,889
Accumulated amortisation	(5,625)	(1,801)	(7,426)
Net carrying amount	9,379	2,084	11,463
At 31 December 2017			
Cost	15,004	5,945	20,949
Accumulated amortisation	(4,875)	(2,463)	(7,338)
Net carrying amount	10,129	3,482	13,611

15. OTHER INTANGIBLE ASSETS (CONTINUED)

	Technical know-how RMB'000	Computer software RMB'000	Total RMB'000
31 December 2017			
Cost at 1 January 2017, net of accumulated amortisation	10,879	3,968	14,847
Additions	—	159	159
Amortisation provided during the year	(750)	(645)	(1,395)
At 31 December 2017	10,129	3,482	13,611
At 31 December 2017			
Cost	15,004	5,945	20,949
Accumulated amortisation	(4,875)	(2,463)	(7,338)
Net carrying amount	10,129	3,482	13,611
At 31 December 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

16. INVESTMENTS IN ASSOCIATES

	2018 RMB'000	2017 RMB'000
Share of net assets	90,328	105,784

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

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	USD 76,847,333	PRC/ Mainland China	15.03%	Dairy processing

16. INVESTMENTS IN ASSOCIATES (CONTINUED)

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 31 December 2018, Shengmu Forage has been accounted for as an associate of the Group as the Group has had more than 20% of 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	2018 RMB'000	2017 RMB'000
Current assets	716,071	645,570
Non-current assets	677,779	690,134
Current liabilities	(945,897)	(913,269)
Net assets	447,953	422,435
Net assets attribute to owners of the parent	442,449	416,078
Reconciliation to the Group's interest in the associate:		
Proportion of the Group's ownership	9.12%	9.12%
Group's share of net assets of the associate, excluding goodwill	40,351	37,947
Goodwill included in the investment	947	947
Adjustments	(1,019)	(999)
Carrying amount of the investment	40,279	37,895
Revenue	318,944	562,870
Profit for the year	25,319	30,098
Total comprehensive income for the year	25,319	30,098
Dividend received	—	—

16. INVESTMENTS IN ASSOCIATES (CONTINUED)

Food Union Shengmu	2018 RMB'000	2017 RMB'000
Current assets	181,134	168,580
Non-current assets	754,352	674,869
Current liabilities	(104,779)	(46,724)
Non-current liabilities	(570,143)	(459,117)
Net assets	260,564	337,608
Reconciliation to the Group's interest in the associate:		
Unpaid capital contribution of other shareholders	72,430	—
Proportion of the Group's ownership	15.03%	20.00%
Group's share of net assets of the associate, excluding goodwill	50,049	67,522
Carrying amount of the investment	50,049	67,522
Revenue	13,109	—
Loss for the year	(128,906)	(24,737)
Total comprehensive loss for the year	(128,906)	(24,737)
Dividend received	—	—

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

	2018 RMB'000	2017 RMB'000
Share of the associates' loss for the year	(93)	(4,672)
Share of the associates' total comprehensive loss	(93)	(4,672)
Aggregate carrying amount of the Group's investments in the associates	—	367

The Group's shareholdings in the associates comprise all the 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 total unrecognised share of losses of these associates for the current year and cumulatively were RMB87,713,000 (2017: RMB272,748,000) and RMB457,748,000 (2017: RMB370,035,000), respectively. Unrecognised share of losses of these associates from continuing operations for the current year and cumulatively were RMB1,387,000 (2017:nil), and RMB1,387,000 (2017: nil), respectively.

17. AVAILABLE-FOR-SALE INVESTMENTS

	2018 RMB'000	2017 RMB'000
Available-for-sale investments		
Non-current:		
Unlisted equity investments, at cost (note (i))	—	2,007

Note:

(i) As at 31 December 2017, certain unlisted equity investments with a carrying amount of RMB2,007,000 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 value cannot be measured reliably.

18. BIOLOGICAL ASSETS

(A) Nature of activities

The biological assets of the Group comprise primarily dairy cows held to produce raw milk and beef cattle raised for sale.

The quantity of biological assets owned by the Group as at 31 December 2018 and 31 December 2017 is shown below. The Group's biological assets include heifers and calves, milkable cows and beef cattle. Heifers and calves are dairy cows that have not had their first calves. The Group's beef cattle are raised for sale.

	2018 Head	2017 Head
Heifers and calves	38,453	51,383
Milkable cows	72,773	72,959
Beef cattle	1,379	7,675
Total	112,605	132,017

18. BIOLOGICAL ASSETS (CONTINUED)

(A) Nature of activities (continued)

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 dry period of approximately 60 days. The male calves which are newly born will be sold while the female calves will be bred for six months and then transferred to the group of heifers. Beef cattle will be bred for three to six months and then sold for profits. The sale of biological assets is not one of the Group's principal activities and the proceeds are not included as revenue.

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 which aimed at complying 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 which 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 derivatives or other contracts which the Group can enter into to manage the risk of a decline in the price of the dairy products.

18. BIOLOGICAL ASSETS (CONTINUED)

(B) Value of biological assets

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

	Heifers and calves RMB'000	Milkable cows RMB'000	Beef cattle RMB'000	Total RMB'000
31 December 2018				
At 1 January 2018	1,146,523	2,720,866	33,511	3,900,900
Increase	1,358	—	—	1,358
Increase due to raising (feeding costs and others)	438,573	—	163,062	601,635
Transfer	(731,034)	731,034	—	—
Decrease due to sales	(48,808)	(287,288)	(171,324)	(507,420)
Loss arising from changes in fair value less costs to sell	(164,521)	(1,139,276)	(17,757)	(1,321,554)
At 31 December 2018	642,091	2,025,336	7,492	2,674,919

	Heifers and calves RMB'000	Milkable cows RMB'000	Beef cattle RMB'000	Total RMB'000
31 December 2017				
At 1 January 2017	1,252,248	2,632,009	—	3,884,257
Increase	198,644	—	—	198,644
Increase due to raising (feeding costs and others)	746,317	—	90,295	836,612
Transfer	(720,535)	720,535	—	—
Decrease due to sales	(123,348)	(267,210)	(32,576)	(423,134)
Loss arising from changes in fair value less costs to sell	(206,803)	(364,468)	(24,208)	(595,479)
At 31 December 2017	1,146,523	2,720,866	33,511	3,900,900

At 31 December 2018, certain biological assets of the Group with fair value of approximately RMB1,069,794,000 (2017: Nil) were pledged to the entrusted loans of the Group amounting to RMB1,300,000,000 (note 29).

Increases of the Group's biological assets included an increase due to purchase and increase due to replacement, of which the increase due to replacement was nil during the year ended 31 December 2018 (2017: RMB127 million).

The Group's biological assets 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.

18. BIOLOGICAL ASSETS (CONTINUED)

(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 RMB'000	Level 2 RMB'000	Level 3 RMB'000	Total RMB'000
As at 31 December 2018	—	—	2,674,919	2,674,919
As at 31 December 2017	—	—	3,900,900	3,900,900

(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	Inter-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.	Average market price of the heifers of 14 months of age: RMB18,500 to RMB19,000 for the year ended 31 December 2018 (2017: RMB18,905 to RMB19,700).	The estimated fair value increases when the market price increases.

18. BIOLOGICAL ASSETS (CONTINUED)

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

Type	Valuation approach	Key unobservable inputs	Inter-relationship between key unobservable inputs and fair value measurements
	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.		
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.

18. BIOLOGICAL ASSETS (CONTINUED)

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

Type	Valuation approach	Key unobservable inputs	Inter-relationship between key unobservable inputs and fair value measurements
	The calving interval (including the 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 the lactation period ranged from 9.7 tonnes to 11.5 tonnes for the year ended 31 December 2018 (2017: 9.9 tonnes to 11.3 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 ended 31 December 2018 ranged from RMB1.92 to RMB2.60 (2017: RMB1.84 to RMB2.22)	The estimated fair value decreases when the estimated feed costs per kilogram of raw milk increases.
		The estimated future local market prices for raw milk per tonne for the year ended 31 December 2018 ranged from RMB3,750 to RMB4,850 per tonne (2017: RMB3,700 to RMB4,700 per tonne).	The estimated fair value increases when the estimated future local market price for raw milk increases.
		The discount rate was 14.00% for the year ended 31 December 2018 (2017: 14.00%), calculated by using the capital asset pricing model.	The estimated fair value decreases when the discount rate increases.

18. BIOLOGICAL ASSETS (CONTINUED)

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

	2018 Tonne	2017 Tonne
Raw milk	673,238	609,185

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

	2018 Tonne	2017 Tonne
Raw milk	2,358,610	2,467,324

19. DEFERRED TAX

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

Deferred tax assets:

	Accrued expenses RMB'000	Unused tax credits RMB'000	Unrealized internal profits RMB'000	Total RMB'000
At 1 January 2018	1,594	12,887	17,716	32,197
Deferred tax charged to the statement of profit or loss during the year (note 9)	(1,594)	(12,887)	(17,089)	(31,570)
Gross deferred tax assets at 31 December 2018	—	—	627	627
Deferred tax assets included in the discontinued operation (note 10)	—	—	627	217
Deferred tax assets in respect of continuing operations	—	—	627	410

19. DEFERRED TAX (CONTINUED)

Deferred tax assets

	Impairment RMB'000	Accrued expenses RMB'000	Unused tax credits RMB'000	Unrealized internal profits RMB'000	Total RMB'000
At 1 January 2017	3,535	1,473	—	19,626	24,634
Deferred tax credited/(charged) to profit or loss during the year (note 9)	(3,535)	121	12,887	(1,910)	7,563
Gross deferred tax assets at 31 December 2017	—	1,594	12,887	17,716	32,197

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 1 January 2008 and applies to earnings after 31 December 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 1 January 2008.

At 31 December 2018, no (2017: 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 RMB897,171,000 at 31 December 2018 (2017: RMB2,404,183,000).

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

The Group also has tax losses arising in Mainland China of RMB210,953,000 (2017: RMB122,164,000) that will expire in one to five years for offsetting against future taxable profits.

The carrying value of deferred tax assets relating to recognised unused tax credits at 31 December 2018 was nil (2017: RMB12,887,000).

Deferred tax assets have not been recognised in respect of the losses of RMB125,041,000 (2017: RMB36,252,000) as they have arisen in subsidiaries that have been loss-making for some time and it is not considered probable that taxable profits will be available against which the tax losses can be utilised.

20. PREPAYMENTS, OTHER RECEIVABLES AND OTHER ASSETS

	2018 RMB'000	2017 RMB'000
Prepayments	557,301	518,516
Deposits and other receivables	30,140	327,774
Prepaid expenses	12,665	58,756
	600,106	905,046
Non-current prepayments	(1,014)	(6,209)
Current portion	599,092	898,837

Deposits and other receivables mainly represent receivables from sales of biological assets, employee loans and financial support to distributors. Where applicable, an impairment analysis is performed at each reporting date by considering the probability of default of comparable companies with published credit ratings. After applying IFRS 9, an impairment analysis is performed at each reporting date using a provision matrix to measure ECLs, ECLs are estimated by applying a loss rate approach with reference to the historical loss record of the Group. The loss rate is adjusted to reflect the current conditions and forecasts of future economic conditions, as appropriate. A reconciliation between the carrying amounts under IAS 39 and under IFRS 9 as at 1 January 2018 is disclosed in note 2.2(b).

21. LONG TERM RECEIVABLES

	Contract amounts of long term receivables		Present value of long term receivables	
	2018 RMB'000	2017 RMB'000	2018 RMB'000	2017 RMB'000
Within 1 year	3,200	3,200	2,519	2,402
1 to 2 years	3,200	3,200	2,643	2,519
2 to 5 years	9,600	9,600	8,873	8,323
Over 5 years	—	3,200	—	3,217
	16,000	19,200	14,035	16,461
Less: Unearned finance income	(1,965)	(2,739)	—	—
Present value of long term receivables	14,035	16,461	14,035	16,461
Portion classified as current assets under other receivables	(2,519)	(2,402)	(2,519)	(2,402)
Non-current portion	11,516	14,059	11,516	14,059

22. OTHER NON-CURRENT ASSETS

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

23. INVENTORIES

	2018 RMB'000	2017 RMB'000
Consumables	34,495	38,430
Finished goods	423	32,995
Raw materials	569,142	789,403
	604,060	860,828

24. TRADE AND BILLS RECEIVABLES

	2018 RMB'000	2017 RMB'000
Bills receivable	1,433	25,707
Trade receivables	245,282	1,814,785
	246,715	1,840,492
Impairment	—	(740,486)
	246,715	1,100,006

The Group's trading terms with its customers are mainly on credit. In 2018, the credit period is generally one month, extending up to three months for major customers. However, the Group normally allows a credit limit or offer to its customers credit terms which are adjustable in certain circumstances in 2017 and closely monitors overdue balances.

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 ageing analysis of the trade and bills receivables as at the end of the reporting period, based on the invoice date and net of loss allowance, is as follows:

	2018 RMB'000	2017 RMB'000
Within 3 months	239,821	550,907
4 to 6 months	3,446	269,445
7 months to 1 year	2,424	272,596
Over 1 year	1,024	7,058
	246,715	1,100,006

24. TRADE AND BILLS RECEIVABLES (CONTINUED)

Impairment under IFRS 9 for the year ended 31 December 2018

An impairment analysis is performed at each reporting date using a provision matrix to measure ECLs. For special cases, management will consider the corresponding expected credit loss separately. The provision rates are based on days past due for groupings of various customer segments with similar loss patterns (i.e., by product type, customer type and rating, and coverage by letters of credit or other forms of credit insurance). The calculation reflects the probability-weighted outcome, the time value of money and reasonable and supportable information that is available at the reporting date about past events, current conditions and forecasts of future economic conditions.

Set out below is the information about the credit risk exposure on the Group's trade receivables using a provision matrix:

As at 31 December 2018

		Past Due					
	Within 3 months	4 to 6 months	7 to 12 months	1 to 2 years	2 to 3 years	Over 3 years	Total
Expected credit loss rate	0%	0%	5%	10%	50%	100%	0%
Gross carrying amount without special cases (RMB'000)	239,721	2,113	—	—	—	—	241,834
Expected credit losses (RMB'000)	—	—	—	—	—	—	—

Impairment under IAS 39 for the year ended 31 December 2017

Included in the above provision for impairment of trade receivables, which was measured based on incurred credit losses under IAS 39, as at 31 December 2017 was a provision for individually impaired trade receivables of RMB740,486,000 with a carrying amount before provision of RMB1,814,785,000.

The individually impaired trade receivables as at 31 December 2017 related to customers that were in financial difficulties or were in default in interest and/or principal payments and only a portion of the receivables is expected to be recovered.

The ageing analysis of the trade receivables as at 31 December 2017 that were not individually nor collectively considered to be impaired under IAS 39 is as follows:

	2017 RMB'000
Neither past due nor impaired	861,648
Past due within 3 months	238,358
	1,100,006

24. TRADE AND BILLS RECEIVABLES (CONTINUED)

Receivables that were neither past due nor impaired related to a large number of diversified customers for whom there was no recent history of default.

Receivables that were past due but not impaired related to a number of independent customers that had a good track record with the Group. Based on past experience, the directors of the Company were of the opinion that no provision for impairment under IAS 39 was necessary in respect of these balances as there had not been a significant change in credit quality and the balances were still considered fully recoverable.

25. CASH AND BANK BALANCES AND PLEDGED DEPOSITS

	2018 RMB'000	2017 RMB'000
Cash and cash equivalents	73,852	297,672
Time deposits with original maturity of more than three months	200	284,611
Pledged deposits	150,617	128,884
	224,669	711,167
Less: Pledged deposits	(150,617)	(128,884)
Cash and bank balances	74,052	582,283

As at 31 December 2018, deposits of RMB80,000,000 were pledged to secure bank loans of RMB75,710,000 of the Group (2017: nil) (note 29 (vi)).

As at 31 December 2018, deposits of RMB30,617,000 (2017: RMB30,000,000) were pledged to provide guarantees for the bank loans of RMB15,000,000 of Shengmu Forage (2017: RMB15,000,000).

	2017 RMB'000	2016 RMB'000
Euro	327	4,468
United States dollars	567	174,930
Hong Kong dollars	6,656	5,375
RMB	66,502	397,510
	74,052	582,283

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 utilised 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.

26. TRADE AND BILLS PAYABLES

An ageing analysis of the trade payables of the Group, based on the invoice date, is as follows:

	2018 RMB'000	2017 RMB'000
1 to 3 months	789,020	967,986
4 to 6 months	109,151	138,930
7 to 12 months	65,068	69,365
1 to 2 years	27,110	12,255
2 to 3 years	6,449	351
Over 3 years	287	77
	997,085	1,188,964

The trade payables are non-interest-bearing and are normally settled within 90-day terms.

27. OTHER PAYABLES AND ACCRUALS

	Notes	2018 RMB'000	2017 RMB'000
Payables for purchases of dairy cows	(a)	940	3,472
Payables for taxes other than corporate income tax	(a)	770	984
Payables for third parties' deposits	(a)	26,642	40,067
Long term payables due within one year		26,301	25,071
Salary and welfare payables	(a)	61,489	43,225
Payables for purchases of transportation services	(a)	27,105	80,017
Payables for acquisition of items of property, plant and equipment	(a)	139,631	207,916
Contract liabilities	(b)	119,680	—
Financial guarantee contracts	(c)	43,203	40,669
Others	(a)	40,474	40,966
		486,235	482,387

(a) These payables are non-interest-bearing and have an average term of 90 days.

(b) Details of contract liabilities as at 31 December 2018 and 1 January 2018 are as follows:

27. OTHER PAYABLES AND ACCRUALS(CONTINUED)

	31 December 2018 RMB'000	1 January 2018 RMB'000
Short-term advances received from customers		
Sale of goods	119,680	14,700

Contract liabilities include short-term advances received to deliver raw milk and liquid milk. The increase in contract liabilities as at 31 December 2018 was mainly due to the increase in short-term advances received from customers in relation to the supply of raw milk in the following year.

(c) The financial guarantee contracts represent guarantees given to banks in connection with facilities granted to associates and external distributors. As at 31 December 2018, the associates' banking facilities granted by the banks were RMB499,000,000 (2017: RMB679,000,000), out of which RMB300,480,000 (2017: RMB535,480,000) was utilised by the associates and external distributors.

The Group does not provide financial guarantees except for limited circumstances. All guarantees are approved by the chief executive.

The financial guarantee contracts are measured at the higher of the ECL allowance and the amount initially recognised less the cumulative amount of income recognised. The ECL allowance is measured by estimating the cash shortfalls, which are based on the expected payments to reimburse the holders (i.e., the banks) for a credit loss that it incurs less any amounts that the Group expects to receive from the debtor (i.e., the associates, and external distributors).

The amount initially recognised representing the fair value at initial recognition of the financial guarantees has been restated at RMB40,669,000 as at 31 December 2017, as further detailed in note 2.5 to the financial statements. Upon transition to IFRS 9, the carrying amount of the financial guarantees was remeasured at RMB40,669,000 as at 1 January 2018 as further detailed in note 2.2 to the financial statements.

The credit exposure of the financial guarantee contracts is classified as stage 1. During the year, there were no transfers between stages.

During the year, an ECL allowance of RMB121,703,000 was reversed as the loans on which the guarantees were executed by the Group were defaulted and the defaulted amounts have already been paid by the Group for the purpose of fulfilling the guarantees.

28. DERIVATIVE FINANCIAL INSTRUMENTS

	2018 Derivative financial liabilities RMB'000
Subscription right of warrants	81,238

On 23 December 2018, the Company entered into agreements with Start Great Holdings Limited, a wholly-owned subsidiary of China Mengniu, and Greenbelt Global Limited, two independent investors, for the issuance of warrants. In accordance with the agreements, the two investors would be entitled to subscribe the warrants after certain precedent conditions were met. As at 31 December 2018, the warrants have not been issued but the subscription rights of warrants were considered as derivative financial instruments and were measured at fair value through profit and loss. Changes in the fair value of the subscription rights of warrants amounting to RMB6,251,000 were charged into profit or loss during the year.

29. INTEREST-BEARING BANK AND OTHER BORROWINGS

	2017			2016		
	Effective interest rate (%)	Maturity	RMB'000	Effective interest rate (%)	Maturity	RMB'000
Current						
Bank loans – unsecured	4.79-6.97	2019	200,000	2.50-5.66	2018	1,066,141
Bank loans – secured	5.66-12.97	2019	1,390,266	5.66	2018	180,000
Domestic corporate bonds – unsecured	5.01	2019	599,209	4.74	2018	997,619
Current portion of long term bank and other borrowings – unsecured	1.55-5.23	2019	29,389	1.55	2018	11,486
Super short-term notes – unsecured			—	6.98	2018	398,800
			2,218,864			2,654,046
Non-current						
Bank loans – unsecured	1.55	2020-2024	49,518	1.55-5.23	2019-2024	122,544
Domestic corporate bonds – unsecured			—	5.01	2019	597,657
			49,518			720,201
			2,268,382			3,374,247

29. INTEREST-BEARING BANK AND OTHER BORROWINGS (CONTINUED)

	2018 RMB'000	2017 RMB'000
Analysed into:		
Bank loans repayable:		
Within one year or on demand	1,619,655	1,257,627
In the second year	—	59,000
Beyond five years	49,518	63,544
	1,669,173	1,380,171
Other borrowings repayable:		
Within one year	599,209	1,396,419
In the second year	—	597,657
	599,209	1,994,076
	2,268,382	3,374,247

Notes:

(i) As at 31 December 2018, substantially all of the Group's bank and other borrowings were denominated in RMB except for the interest-bearing bank loans of RMB60,907,000 (2017: RMB322,850,000) 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 29 December 2015 as approved by the China Securities Regulatory Commission. As at 31 December 2018, the domestic corporate bonds have been fully repaid.

The domestic corporate bonds with an aggregate nominal amount of RMB600,000,000 were issued by the Issuer to qualified investors on 30 May 2016 as approved by the China Securities Regulatory Commission. The domestic corporate bonds bear interest at an annual interest rate of 4.75 % and have a term of 3 years with extension options granted to the bond holders for two more years at the end of the third year. As at 31 December 2018, the domestic corporate bonds were classified as a non-current liability due within one year in the consolidated financial statements of the Group, as the Issuer did not have an unconditional right to defer settlement of the liability for at least twelve months after 31 December 2018.

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) The super short – term notes with an aggregate nominal amount of RMB400,000,000 were issued by the Issuer on 22 June 2017 in the Inter-bank Bond Market in the PRC according to the approval by National Association of Financial Market Institutional Investors. The super short-term notes bore interest at an annual interest rate of 6.50% and were repayable in 270 days. As at 31 December 2018, the super short-term notes has been fully repaid.

(iv) As at 31 December 2018, two directors of the Company provided guarantees for the bank loans of the Group amounting to RMB 80,000,000 (2017: RMB180,000,000).

29. INTEREST-BEARING BANK AND OTHER BORROWINGS (CONTINUED)

Notes: (continued)

(v) On 10 December 2018 and 23 December 2018, the Company and Inner Mongolia Mengniu, a subsidiary of China Mengniu, entered into two entrusted loan agreements, where half-year term loan of RMB300,000,000 and one-year term loan of RMB1,000,000,000 were granted by Inner Mongolia Mengniu to the Group, respectively. Included in the loan facilities were the subscription rights of fair-valued warrants at RMB67,093,000 on 23 December 2018, which were classified to derivative financial instruments, as disclosed in note 28 to the financial statements.

The loan facility of RMB300,000,000 was secured by the pledged biological assets of Shengmu High-tech and Shengmu Holding with fair value of approximately RMB729,757,000 in total as at 31 December 2018 and a corporate guarantee provided by the Company. The loan facility of RMB1,000,000,000 was secured by the pledged biological assets of Shengmu High-tech and Shengmu Holding with fair value of approximately RMB340,037,000 in total and the pledged equity interests in fourteen subsidiaries of the Group with net assets amounting to RMB2,311,889,000 in total as at 31 December 2018.

(vi) At 31 December 2018, the Group's bank loans amounting to RMB75,710,000 (2017: Nil) were secured by the pledged deposits of RMB80,000,000.

30. LONG TERM PAYABLES

	Contract amounts of long term payments		Present value of long term payments	
	2018 RMB'000	2017 RMB'000	2018 RMB'000	2017 RMB'000
Within 1 year	28,940	28,940	26,301	25,071
1 to 2 years	28,940	28,940	27,588	26,300
2 to 5 years	28,940	57,880	28,940	56,529
	86,820	115,760	82,829	107,900
Future finance charges	(3,991)	(7,860)	—	—
Present value of long term payables	82,829	107,900	82,829	107,900
Portion classified as current liabilities included in other payables	(26,301)	(25,071)	(26,301)	(25,071)
Non-current portion	56,528	82,829	56,528	82,829

31. SHARE CAPITAL

Shares

	2018 RMB'000	2017 RMB'000
Authorised:		
30,000,000,000 ordinary shares of HK$0.00001 each (2017: 30,000,000,000 ordinary shares HK$0.00001 each)	236	236
Issued and fully paid:		
6,354,400,000 (2017: 6,354,400,000) ordinary shares	50	50

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 asset 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 SUBSIDIARY WITH MATERIAL NON-CONTROLLING INTERESTS

Details of the Group's subsidiary that has material non-controlling interests are set out below:

Shengmu Pangu	2018	2017
Percentage of equity interest held by non-controlling interests	45%	45%
Profit for the year allocated to non-controlling interests	5,528	40,935
Accumulated balances of non-controlling interests at the end of the reporting period	241,298	235,770

The following tables illustrate the summarised financial information of Shengmu Pangu. The amounts disclosed are before any inter-company eliminations:

	2018 RMB'000	2017 RMB'000
Revenue	221,261	237,714
(Loss)/profit for the year	(2,284)	84,281
Total comprehensive income for the year	(2,284)	84,281
Current assets	233,456	182,421
Biological assets	247,235	321,045
Other non-current assets	121,919	125,217
Current liabilities	(64,521)	(51,310)
Non-current liabilities	—	(37,000)
Net cash flows from operating activities	102,640	75,641
Net cash flows used in investing activities	(4,546)	(49,102)
Net cash flows used in financing activities	(92,223)	(33,724)
Net increase/(decrease) in cash and cash equivalents	5,871	(7,185)

34. NOTE TO THE CONSOLIDATED STATEMENT OF CASH FLOWS

Changes in liabilities arising from financing activities:

	Bank and other loans RMB'000	Domestic corporate bonds RMB'000	Super short-term notes RMB'000	Derivative financial instruments RMB'000
At 1 January 2018	1,380,171	1,595,276	398,800	—
Changes from financing cash flows	390,842	(1,000,000)	(398,800)	67,093
Foreign exchange movement	—	—	—	(287)
Fair value loss	—	—	—	6,539
Consideration receivable	—	—	—	7,893
Interest expense	—	3,933	—	—
At 31 December 2018 (notes 28, 29 and 30)	1,771,013	599,209	—	81,238

	Bank and other loans RMB'000	Domestic corporate bonds RMB'000	Super short-term notes RMB'000	Derivative financial instruments RMB'000
At 1 January 2017	1,078,831	1,591,523	—	—
Changes from financing cash flows	301,340	—	398,800	—
Interest expenses	—	3,753	—	—
At 31 December 2017	1,380,171	1,595,276	398,800	—

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:

	2018 RMB'000	2017 RMB'000
Within one year	1,200	1,319
In the second to fifth years, inclusive	—	15
	1,200	1,334

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:

	Notes	2018 RMB'000	2017 RMB'000
Contracted, but not provided for:			
Plant and machinery		57,821	117,951
Land and buildings		49,436	96,614
Capital contribution payable to Inner Mongolia Shengmu Sand and Grass Industry Co., Ltd. ("Shengmu Sand & Grass") and associates	(i)	311,000	11,000
		418,257	225,565

Note:

(i) On 21 December 2018, the Group has subscribed capital contribution of RMB300,000,000 to acquire the non-controlling interests of Shengmu Sand and Grass but has not made capital injection.

As at 31 December 2018, the Group has subscribed capital contribution of RMB11,000,000 (2017: RMB11,000,000) into certain associates but has not made capital injection. As these associates had net liabilities and accumulated losses at the year end, the maximum amount of the Group's unrecognised share of accumulated losses of these associates would be RMB11,000,000 (2017: RMB6,748,000) based on the investment commitment of these associates.

37. RELATED PARTY DISCLOSURES

(A) The Group had the following significant transactions with related parties:

	Notes	2018 RMB'000	2017 RMB'000
Associates:			
Sales of products	(i)	166,692	599,158
Purchases of raw materials	(i)	330,006	583,606
Sales of raw materials	(i)	30,663	18,982
Affiliates of a substantial shareholder:			
Purchases of raw materials	(i)	45,630	—

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 ended and as of 31 December 2018, the Group provided guarantees to banks in respect of the bank loans of the following related parties:

	During the year ended 31 December	
	2018 RMB'000	2017 RMB'000
Shengmu Forage	140,000	252,600
Food Union Shengmu	20,539	45,400
Associates distributors	—	154,000

	As at 31 December	
	2018 RMB'000	2017 RMB'000
Shengmu Forage	155,000	252,600
Food Union Shengmu	123,419	102,880
Associates distributors	20,820	154,000

During the year ended 31 December 2018, the Group has paid RMB35,526,000 and RMB78,330,000 for the purpose of fulfilling the guarantees for the associate distributors and Shengmu Forage, respectively (2017: nil). Details of the guarantees granted were disclosed in note 2.5 and note 27 to the financial statements.

During the year ended and as at 31 December 2018, two directors of the Company provided guarantees for the bank loans of the Group amounting to RMB80,000,000 (2017: RMB180,000,000).

As at 31 December 2018, deposits of RMB30,617,000 (2017: RMB30,000,000) was pledged to provide guarantees for the bank loans of RMB15,000,000 of Shengmu Forage (2017: RMB15,000,000).

37. RELATED PARTY DISCLOSURES (CONTINUED)

(C) Compensation of key management personnel of the Group:

	2018 RMB'000	2017 RMB'000
Short term employee benefits	1,810	1,858
Pension scheme contributions	35	44
	1,845	1,902

Further details of directors' and the chief executive's emoluments are included in note 8 to the financial statements.

(D) Outstanding balances with related parties

	2018 RMB'000	2017 RMB'000
Amounts owed by/(owed to) associates included in:		
Trade and bills receivables	22,847	524,216
Trade and bills payables	(38,796)	(1,001)
Prepayments, other receivables and other assets	507,444	700,258
Contract liabilities	(190)	—
Other payables and accruals	(1,472)	(1,416)

As at 31 December 2018, included in the Group's prepayments, deposits and other receivables were the prepayment to Shengmu Forage for the purchase of raw materials of RMB507,444,000 (2017: RMB464,382,000) and the amounts due from the Group's associates of RMB242,216,000 (2017: RMB235,876,000) for the working capital financing provided to these associates. ECLs arising from the working capital financing provided to associates distributors have been fully provided as at 31 December 2018.

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 instruments as at the end of the reporting period are as follows:

2018

Financial assets

	Financial assets at amortised cost RMB'000
Long term receivables	11,516
Financial assets included in prepayments, other receivables and other assets	30,140
Pledged deposits	150,617
Cash and bank balances	74,052
Trade and bills receivables	246,715
	513,040

Financial liabilities

	Financial liabilities at fair value through profit and loss RMB'000	Financial liabilities at amortised cost RMB'000	Total RMB'000
Long term payables	—	56,528	56,528
Financial liabilities included in other payables and accruals	—	261,092	261,092
Trade and bills payables	—	997,085	997,085
Interest-bearing bank and other borrowings	—	2,268,382	2,268,382
Financial guarantee contracts	43,203	—	43,203
Derivative financial instruments	81,238	—	81,238
	124,441	3,583,087	3,707,528

38. FINANCIAL INSTRUMENTS BY CATEGORY (CONTINUED)

2017

Financial assets

	Financial assets at amortised cost RMB'000
Long term receivables	14,059
Financial assets included in prepayments, other receivables and other assets	327,774
Pledged deposits	128,884
Cash and bank balances	582,283
Trade and bills receivables	1,100,006
Available-for-sale investments	2,007
	2,155,013

Financial liabilities

	Financial liabilities at fair value through profit and loss RMB'000	Financial liabilities at amortised cost RMB'000	Total RMB'000
Long term payables	—	82,829	82,829
Financial liabilities included in other payables and accruals	—	397,509	397,509
Trade and bills payables	—	1,188,964	1,188,964
Financial guarantee contracts	40,669	—	40,669
Interest-bearing bank and other borrowings	—	3,374,247	3,374,247
	40,669	5,043,549	5,084,218

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 31 December		Fair values As at 31 December	
	2018 RMB'000	2017 RMB'000	2018 RMB'000	2017 RMB'000
Financial liabilities				
Interest-bearing bank and other borrowings	2,268,382	3,374,247	2,256,035	3,324,471

Management has assessed that the fair values of cash and cash equivalents, pledged deposits, trade and bills receivables, trade and bills payables, financial assets included in prepayments, other receivables and other assets, and 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 the non-current portion of long term receivables, the non-current portion of interest-bearing bank loans and long term payables 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 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)	
	2018 RMB'000	2017 RMB'000
Interest-bearing bank and other borrowings	2,256,035	3,324,471

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 bank 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.

It is, and has been throughout the year under review, the Group's policy that no trading in financial instruments shall be undertaken.

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's exposure to the risk of changes in market interest rates relates primarily to the Group's long term debt obligations with a floating interest rate.

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 significant interest rate exposure should the need arise. The Group's interest rate profile is set out in note 29.

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the Group's (loss)/profit before tax through the impact on floating rate borrowings and the Group's equity.

	Increase/(decrease) in basis points	Increase/(decrease) in profit/(loss) before tax RMB'000	Increase/(decrease) in equity* RMB'000
2018			
RMB	50	(796)	(796)
RMB	(50)	796	796
2017			
RMB	50	(2,574)	(2,574)
RMB	(50)	2,574	2,574

* Excluding retained profits

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

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 31 December 2018, cash and bank balances of approximately RMB327,000 (2017: RMB4,468,000), RMB567,000 (2017: RMB174,930,000) and RMB6,656,000 (2017: RMB5,375,000) were denominated in Euro ("EUR"), United States dollars ("USD") and Hong Kong dollars ("HK$"), respectively, and the interest-bearing bank and other borrowings of approximately RMB60,907,000 (2017: RMB322,848,000) were denominated in EUR. 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 EUR exchange rate (2017: EUR exchange rate) with all other variables held constant, of the Group's profit/(loss) before tax (due to changes in the fair value of monetary assets and liabilities):

	Increase/(decrease) in rate %	Increase/(decrease) in profit/(loss) before tax RMB'000
2018	5	39,029
	(5)	(39,029)
2017	5	20,621
	(5)	(20,621)

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.

Maximum exposure and year-end staging as at 31 December 2018

The table below shows the credit quality and the maximum exposure to credit risk based on the Group's credit policy, which is mainly based on past due information unless other information is available without undue cost or effort, and year-end staging classification as at 31 December 2018. For listed debt investments, the Group also monitors them by using external credit ratings. The amounts presented are gross carrying amounts for financial assets and the exposure to credit risk for the financial guarantee contracts.

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

Maximum exposure and year-end staging as at 31 December 2018 (continued)

	12-month ECLs	Lifetime ECLs			
	Stage 1 RMB'000	Stage 2 RMB'000	Stage 3 RMB'000	simplified approach RMB'000	RMB'000
Trade and bills receivables*	—	—	—	246,715	246,715
Long term receivables**					
– Normal**	11,516	—	—	—	11,516
– Doubtful**	—	—	—	—	—
Financial assets included in prepayments, other receivables and other assets*					
– Normal*	—	—	—	30,140	30,140
– Doubtful*	—	—	—	—	—
Pledged deposits					
– Not yet past due	150,617	—	—	—	150,617
Cash and cash equivalents					
– Not yet past due	74,052	—	—	—	74,052
Guarantees given to banks in connection with facilities granted to associates and external distributors	—	—	—	—	—
– Not yet past due	263,421				263,421
– Less than 1 month past due	22,070	—	—	—	22,070
– 1 to 3 months past due	14,989	—	—	—	14,989
– More than 3 months past due	536,665	—	—	276,855	813,520

* For trade and bills receivables to which the Group applies the simplified approach for impairment, information based on the provision matrix is disclosed in notes 20 and 24 to the financial statements.

** The credit quality of long term receivables and the financial assets included in prepayments, other receivables and other assets are considered to be "normal" when they are not past due and there is no information indicating that the financial assets had a significant increase in credit risk since initial recognition. Otherwise, the credit quality of the financial assets is considered to be "doubtful".

40. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

Maximum exposure and year-end staging as at 31 December 2017

The credit risk of the Group's other financial assets, which comprise cash and bank balances, pledged deposits, other receivables and long term 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. Concentrations of credit risk are managed by customer/counterparty, by geographical region and by industry sector. 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 31 December 2018 and 2017.

Further quantitative data in respect of the Group's exposure to credit risk arising from trade and bills receivables are disclosed in note 24 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 RMB'000	Less than 1 year RMB'000	1 to 5 years RMB'000	Total RMB'000
2018				
Long term payables	—	—	57,880	57,880
Financial liabilities included in other payables and accruals	232,152	28,940	—	261,092
Trade and bills payables	997,085	—	—	997,085
Interest-bearing bank and other borrowings	—	2,288,188	66,381	2,354,569
Derivative financial instruments	81,238	—	—	81,238
Guarantees given to banks in connection with facilities granted to associates and external distribution	37,059	263,421	—	300,480
	1,374,534	2,580,549	124,261	4,052,344
2017				
Long term payables	—	—	86,820	86,820
Financial liabilities included in other payables and accruals	368,569	28,940	—	397,509
Trade and bills payables	1,188,964	—	—	1,188,964
Interest-bearing bank and other borrowings	—	1,686,083	1,831,373	3,517,456
Guarantees given to banks in connection with facilities granted to an associate	—	535,480	—	535,480
	1,557,533	2,250,503	1,918,193	5,726,229

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 characteristics 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:

	2018 RMB'000	2017 RMB'000
Interest-bearing bank and other borrowings	2,268,382	3,374,247
Total equity	2,878,887	5,375,113
Gearing ratio	78.8%	62.8%

41. EVENTS AFTER THE REPORTING PERIOD

(a) On 24 January 2019, the issuance of 1,080,248,000 and 127,088,000 warrants to Start Great Holdings Limited and Greenbelt Global Limited, respectively, was approved by the shareholders' meeting of the Group. The warrants may be exercised at HKD0.33 per warrant share, in whole or in part, at the discretion of the relevant warrant holder at any time during the eighteen-month period commencing from the date of issuance of the respective warrants. Upon issue of the warrants, a maximum of 1,207,336,000 new shares will fall to be issued, which represent approximately 15.97% of the total number of shares in issue as at that date.

(b) On 21 December 2018, the Company and Shengmu High-tech entered into an equity transfer framework agreement with twelve individual shareholders of Shengmu Sand and Grass (the "Individual Shareholders") to acquire the equity interests held by the Individual Shareholders in Shengmu Sand and Grass at a cash consideration of RMB300,000,000 by installs from March 2019 to November 2019. As not all of the conditions precedent to the equity transfer framework agreement have been fulfilled before 28 February 2019, a supplementary agreement was entered into by the contract parties on 8 March 2019 to amend the payment terms. Pursuant to the supplementary agreement, the Company and Shengmu High-tech shall pay the cash consideration amounting to RMB300,000,000 in full to the Individual Shareholders by installs from the month in which all the conditions precedent to the equity transfer framework agreement are fulfilled and before 30 November 2019.

Subsequent to 31 December 2018, six subsidiaries of the Company declared a special dividend amounting to RMB87,903,500 to Shengmu Sand and Grass.

42. COMPARATIVE AMOUNTS

The comparative statement of profit or loss has been re-presented as if the operation discontinued during the current year had been discontinued at the beginning of the comparative period (note 10).

As further explained in note 2.2 and note 2.5 to the financial statements, due to the adoption of the new and revised IFRSs during the current year and the correction of prior period errors, respectively, the accounting treatment and presentation of certain items and balances in the financial statements have been revised to comply with the new requirements. Accordingly, certain prior year adjustments have been made, and certain comparative amounts have been reclassified and restated to conform with the current year's presentation and accounting treatment, and a third statement of financial position as at 1 January 2017 has been presented.

43. 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:

	31 December 2018 RMB'000	31 December 2017 RMB'000
NON-CURRENT ASSETS		
Investments in subsidiaries	294,563	205,834
Due from subsidiaries	3,088,522	3,174,929
Total non-current assets	3,383,085	3,380,763
CURRENT ASSETS		
Prepayments, other receivables and other assets	6,928	1,579
Cash and cash equivalents	1,128	6,885
Due from subsidiaries	74,375	116,351
Total current assets	82,431	124,815
CURRENT LIABILITIES		
Interest-bearing bank borrowings	11,389	259,306
Derivative financial instruments	81,238	—
Other payables and accruals	8,545	2,516
Total current liabilities	101,172	261,822
NET CURRENT ASSETS	(18,741)	(137,007)
TOTAL ASSETS LESS CURRENT LIABILITIES	3,364,344	3,243,756
NON-CURRENT LIABILITIES		
Interest-bearing bank borrowings	49,518	63,542
Total non-current liabilities	49,518	63,542
Net assets	3,314,826	3,180,214
EQUITY		
Share capital	50	50
Reserves (note 32)	3,314,776	3,180,164
Total equity	3,314,826	3,180,214

43. STATEMENT OF FINANCIAL POSITION OF THE COMPANY (CONTINUED)

Note:

A summary of the Company's reserves is as follows:

	Share premium account RMB'000	Share option reserve RMB'000	Accumulated losses RMB'000	Exchange fluctuation reserve RMB'000	Total RMB'000
At 1 January 2017	3,024,937	57,265	(10,401)	386,946	3,458,747
Loss for the year	—	—	(58,856)	—	(58,856)
Other comprehensive loss	—	—	—	(219,727)	(219,727)
Total comprehensive loss for the year	—	—	(58,856)	(219,727)	(278,583)
At 31 December 2017	3,024,937	57,265	(69,257)	167,219	3,180,164
Loss for the year	—	—	(14,843)	—	(14,843)
Other comprehensive income	—	—	—	149,455	149,455
Total comprehensive income for the year	—	—	(14,843)	149,455	134,612
At 31 December 2018	3,024,937	57,265	(84,100)	316,674	3,314,776

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 accumulated losses should the related options expire or be forfeited.

44. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 28 March 2019.

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,				
	2018	2017 (Restated)*	2016	2015	2014
Revenue	2,887,167	2,706,842	3,466,544	3,100,711	2,132,428
(Loss)/profit for the year	(2,311,217)	(853,790)	956,808	1,083,222	883,808
Of which: (loss)/profits attributable to the owners of the parent	(2,225,200)	(1,015,266)	680,615	800,652	711,228
(Loss)/earnings per share attributable to ordinary equity holders of the parent:					
Basic	(RMB0.350)	(RMB0.160)	RMB0.107	RMB0.126	RMB 0.118
Diluted	(RMB0.350)	(RMB0.160)	RMB0.106	RMB0.124	RMB 0.116

	As at December 31,				
	2018	2017 (Restated)*	2016 (Restated)*	2015	2014
Total assets	7,558,361	10,519,695	10,499,295	9,459,793	6,491,244
Total liabilities	4,679,474	5,144,582	4,163,360	4,092,568	2,236,145
Net assets	2,878,887	5,375,113	6,335,935	5,367,225	4,255,099
Of which: equity attributable to the owner of the parent:	2,017,913	4,315,662	5,327,847	4,551,655	3,721,898

* Certain amounts shown here do not correspond to the 2017 financial statements and reflect adjustments made. Refer to note 2.5 to the consolidated financial statements.