Management Discussion and Analysis

Our turnover surged by 14.9% to HK$512 million and profit attributable to equity holders of the Company by 15.5% to HK$117 million

Results

The Board of Directors ("Directors") of Dynasty Fine Wines Group Limited ("the Company") is pleased to report a steady growth in the unaudited results of the Company and its subsidiaries ("the Group") for the first half of 2005. These interim results have been reviewed by the Company's Audit Committee and the Company's auditors, PricewaterhouseCoopers. All of the Audit Committee members are independent non-executive Directors, including the Chairman of the Audit Committee.

Our turnover was HK$512 million (2004 — HK$445 million), increased by 14.9% and our profit attributable to equity holders of the Company was HK$117 million (2004 — HK$101 million), increased by 15.5% during the period under review.

Earnings per share of the Company ("Share") was HK9.8 cents per Share based on the weighted average number of 1,195,856,354 Shares in issue during the period (2004 — HK11.2 cents per Share on a pro forma basis as if 900,000,000 Shares were outstanding since 1 January 2004). As there was no dilutive potential ordinary Share outstanding as at 30 June 2005, dilutive earnings per Share are not presented.

The satisfactory financial results in the first half of 2005 were mainly attributable to the growth in sales volume and the relatively stable distribution costs and general and administrative expenses. As a reflection of the good performance and generally positive outlook, the Directors have resolved to pay an interim dividend of HK3.7 cents per Share.

Financial review

Turnover

Turnover for the six months ended 30 June 2005 increased by 14.9% to HK$512 million, from HK$445 million in the first half of 2004 as a result of increase in sales volume. This increase was attributable to the sales and marketing effort and the organic growth of the overall grape wine market in the PRC.

The Group's average ex-factory sales prices during the period under review for red and white wine products had been relatively stable compared to 2004 yearly average price of HK$20.8 per bottle (750ml). The average ex-factory sales prices of the Group's red wine products are, however, in general higher than the Group's white wine products. Based on consumers in the PRC having a prevalent preference in favour of red wine products, the Group is able to set higher prices for its red wine products.

Cost of sales

The following table sets forth the major components of our cost of sales for the period under review:

	For the six months ended 30 June	
	2005	2004
	%	%
Cost of raw materials		
• Grapes and grape juice	**38.4**	35.1
• Yeast and additives	**1.8**	1.5
• Packaging materials	**27.4**	29.2
• Others	**1.8**	1.8
Total cost of raw materials	**69.4**	67.6
Manufacturing overheads	**10.1**	10.4
Consumption tax	**20.5**	22.0
Total cost of sales	**100.0**	100.0

The major raw materials required by the Group in producing wine products are grapes, grape juice, yeast and additives and packaging materials. During the period under review, the cost of grapes and grape juice accounted for approximately 38.4% of the Group's total cost of sales, an increase of 3.3 percentage points from approximately 35.1% in the corresponding

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period in 2004 and was due to the unfavorable demand and supply situation of grapes or grape juice. The average cost of packaging materials was relatively stable during the period under review as compared with the preceding period.

Manufacturing overheads consist primarily of depreciation or rental of fixed assets, supplies, utilities, repair and maintenance expenses, salaries and related personnel expenses for the production and related departments and other incidental expenses for production. During the period, manufacturing overheads did not fluctuate significantly as a percentage of turnover.

Gross profit margin

During the period under review, the gross margin was calculated based on cost of sales inclusive of consumption tax over gross invoiced sales. Overall gross profit margin reached 51.5% in the first half of 2005, a decline of 3.1 percentage points from 54.6% in the corresponding period in 2004 and was primarily due to higher purchase cost of grape juice as compared to the first half of 2004. The gross margin of red wine products and white wine products were 51.9% and 42.3% respectively (2004 — 55.4.% and 43.4% respectively). The higher gross margin of the red wine products was attributable to their higher sales prices.

Distribution costs

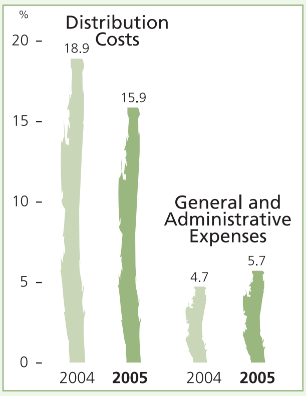
Distribution costs include principally advertising and market promotion expenses, transportation and delivery charges in connection with the sales of wine products, salaries and related personnel expenses for the sales and marketing department and other incidental expenses. During the period under review, distribution costs decreased and accounted for approximately 15.9% (2004 — 18.9%) of the Group's turnover. In particular, advertising and market promotion expenses accounted for approximately 8.6% (2004 — 12.0%) of the Group's turnover. The decrease in percentage reflected that turnover outgrew the effect of incurring more advertising and market promotion expenses during the period. We expect advertising and market promotion expenses to increase in line with the growth in turnover of the Group in the foreseeable future so as to allow the Group to maintain consumer awareness of our brand name — "Dynasty", to increase the market share and also to facilitate the launch of new products.

General and administrative expenses

General and administrative expenses consist primarily of salaries and related personnel expenses for administrative, finance and human resources departments, provision for doubtful debts and write off for obsolete inventories, depreciation and amortisation expense and other incidental administrative expenses.

During the period under review, general and administrative expenses remained relatively stable and accounted for approximately 5.7% (2004 — 4.7%) of the Group's turnover.

Expenses to Turnover (%)
for the six months ended 30 June



Taxation expense

Under the current laws of the Cayman Islands and the British Virgin Islands ("BVI"), neither the Company nor its subsidiaries incorporated in BVI is subject to tax on its income or capital gains. In addition, payment of dividends by them is not subject to withholding tax in those jurisdictions.

Pursuant to the relevant income tax rules and regulations of the PRC, the applicable tax rate for Sino-French Joint-Venture Dynasty Winery Limited, our major operating subsidiary, and for Tianjin Tianyang Grape Extracting Co. Ltd, another subsidiary of the Group, is 24%, being the preferential income tax rate for foreign investment production enterprises established in a coastal economic development zone. The applicable rate for Shandong Yu Huang Grape Wine Co., Ltd., another subsidiary of the Group, is 30%. During the period under review, the effective tax rate of the Group was slightly lowered to approximately 26.6% (2004 — 27.6%).

Cash flow

In the first half of 2005, the Group's source of cash flow was mainly from its financing activities. The Group's cash has principally been applied to pay the consideration for acquisition of Smiling East Resources Limited ("Smiling East"), 2004 special dividends to shareholders and listing expenses.

The decrease in cash inflow from operating activities from HK$102.0 million in 2004 to HK$52.4 million in 2005 was primarily attributable to the effects of the changes in working capital, mainly other payables and accruals.

Net cash used in investing activities was primarily attributable to the acquisition of Smiling East pursuant to the plan disclosed in the prospectus dated 17 January 2005 and amounting to approximately HK$47.0 million (2004 — HK$Nil).

Net cash inflow in financing activities was primarily attributable to the net proceeds from the placing and public offer approximately HK$724 million (2004 — HK$Nil) and offset by the payment of dividends to shareholders of approximately HK$78.7 million (2004 — HK$Nil).

Management Discussion and Analysis

Financial management and treasury policy

As at 30 June 2005, except for the net proceeds from the placing and public offer, the Group's revenues, expenses, assets and liabilities are substantially denominated in RMB. Accordingly, the Group does not anticipate significant exposure to foreign currency fluctuation. The Group has maintained sufficient financial resources and is in a net cash position, thus we are exposed to minimal financial risk on interest rate fluctuation.

As at the date of this report, almost all of our cash and bank balances are denominated either in RMB, Hong Kong dollars or United States dollars. The net proceeds from the placing and public offer that were not already used for the intended purposes have been placed on short term deposits with authorised financial institutions in Hong Kong. The Group has established an investment policy with the objective of monitoring the investments of the Group's uncommitted funds to ensure the achievement of the highest practicable return on the investments with priority on capital preservation and liquidity.

Liquidity and financial resources

The Group's cash balances as at 30 June 2005 amounted to HK$853 million and net cash inflow from operating activities are ample enough to satisfy the working capital requirement for the business operations and capital expenditures. No bank debts were recorded and the gearing of the Group was net cash as at 30 June 2005, reflecting the sound capital structure of the Group. New investment will be funded by the Group's internal resources.

Capital structure

Upon the completion of the placing and public offer, the net proceeds from our listing further strengthen our capital structure and we expect our cash to be sufficient for meeting our operating and capital expenditure requirements in the foreseeable future.

The market capitalisation of the Company as at 30 June 2005 was approximately HK$3,424 million.

Capital commitments, contingencies and charges on assets

The Group has made capital expenditure commitments mainly for machineries of approximately HK$144.6 million which are authorised but not contracted for and approximately HK$7.2 million which are contracted but not provided for in the financial statements as at 30 June 2005. These commitments, mainly related to the expansion of the Group's production capacity, are expected to be paid within one year. The funding of such capital commitments will be out of the proceeds of the new issue as stated in the prospectus.

As at 30 June 2005, none of the Group's assets were charged or subject to any encumbrance and the Group had no material contingent liabilities.

Use of proceeds

The Company was successfully listed on the Main Board of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") on 26 January 2005. Upon the completion of the placing and public offer, we issued a total of 345,000,000 new shares, including the shares issued upon the exercise of the over-allotment option. The net proceeds raised from the placing and public offer amounted to approximately HK$724 million. The satisfactory results of the placing and public offer reflected the confidence of investors in the prospects of our business as well as in the grape wine industry of the People's Republic of China (the "PRC"). The planned usage of proceeds was as follows:

Use	Usage as announced HK$ million	Actual progress HK$ million
Expansion of existing production facilities	200	61
Establishment of new production facilities	160	—
Expansion of sales and distribution network	20	—
Acquisition of Smiling East	47	47
Other acquisition opportunities and general working capital	297	1
Total	724	109

To cope with the Group's long term development and to crystallise our business plan as set out in our prospectus dated 17 January 2005, we are planning to build a new production facility in Tianjin to further boost our production capacity. Moreover, we are in discussion with certain companies in complementary wine business, which we consider as possible targets of acquisition in the future. As at the date of this report, no agreement was entered into between the Group and other parties in this regard.

We have placed the unutilised net proceeds in short term bank deposits.

Business review

Sales analysis

During the period under review, the Group experienced satisfactory growth in sales volume. The number of bottles of wine sold increased from approximately 20.8 million in the first half of 2004 to approximately 24.9 million in the first half of 2005, whilst the average ex-factory

Management Discussion and Analysis

sale price remained relatively stable. The primary revenue sources of the Group continued to be red wine product sales which accounted for approximately 95.1% of the Group's turnover for the period (2004 — 94.2%). Dynasty Dry Red, the prototype of our mass market product, remained as the Group's best selling wine product, accounting for approximately 49.6% of the Group's turnover (2004 — 50.4%).

During the period under review, we sold our products in all provinces and autonomous regions and four municipalities directly under the central government of the PRC. Huadong region, or Eastern region of the PRC, still remained as our primary market. In addition to the primary market, we are expanding the sales of our products in other markets, such as Guangdong, Jiangxi, Hunan and Hubei, etc., in the PRC as well as to enhance our marketing and promotion efforts in other coastal provinces in order to increase market share in those markets. Overseas sales remained insignificant at 0.2% (2004 — 0.1%) of our turnover during the period as the domestic market was our primary focus.

We produce over 50 products under the "Dynasty" brand name to meet different consumer demands in the PRC grape wine market and focus on medium to high end segments. With a diversified and high quality product portfolio, we believe we will be able to attract higher end consumers by introducing premium higher end products. During the period under review, sales of premium wine products, such as *Dynasty Dry Red Wine-Aged in Oak Barrels* and *Dry Red and Dry White Wine-Seven-Year Reserve* that were launched in 2003, saw encouraging growth. Although sales of these products made up an insignificant contribution to our turnover during the period, we believe these products will become an increasingly significant source of our future growth.

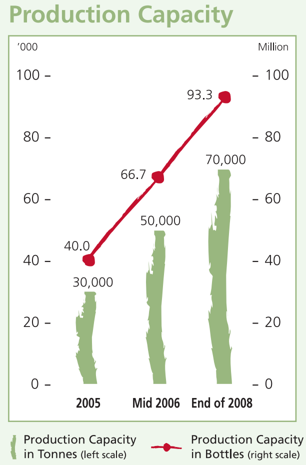
Supplies of grapes or grape juice

The production and quality of wine products is highly dependent upon sufficient supply of quality grapes or grape juice. We currently have over 10 major grape juice suppliers, mainly located in Tianjin, Shandong, Hebei and Ningxia, with whom we have had long term relationships. To ensure reliable and solid supplies of quality grapes and grape juice to meet the needs of the growing business and our expected increasing demand generated from the production capacity expansion plan, we are working with our grape growing partners on enlarging their vineyards to increase harvests and also identify new suppliers who can meet our quality requirements. Such measures will enable us to secure grape supplies and lower the risk of our production being interrupted by effects of weather, affecting the quality of our grapes or grape juice. We will also explore opportunities of acquiring grape juice suppliers in the PRC or overseas.

Production capacity

The progress of production capacity expansion from 30,000 tonnes (equivalent to approximately 40.0 million bottles) to 50,000 tonnes (equivalent to approximately 66.7 million bottles) per annum is in accordance with our schedule and is expected to be completed around mid-2006. The management will put all its

Production Capacity



efforts into ensuring the timely, or even early, completion of the plan. During the period, we commenced a feasibility study on the establishment of a new production facility and identified an appropriate site in Tianjin for that purpose. The new production facility, expected to be completed by the end of 2008, will further increase our production capacity to 70,000 tonnes (equivalent to approximately 93.3 million bottles) per annum.

Employees

The Group employed 386 staff (including Directors) in Hong Kong and the PRC. The increase in manpower occurred mainly due to the acquisition of Smiling East. Total salaries and related costs incurred for the six months ended 30 June 2005 amounted to HK$26.2 million. The Group offers competitive remuneration packages commensurate with industry level and provides various fringe benefits, including trainings, medical, insurance coverage as well as retirement benefits to all employees in Hong Kong and in the PRC.

The Company also adopted a share option scheme on 6 December 2004 for the purposes of providing incentives and rewards to eligible participants who have contributed to the success of our operations. As at 30 June 2005, 23,100,000 share options were granted under the scheme.

Prospects

Successful listing on the Main Board in January 2005 was a historical milestone of the Group. Our financial position have since benefited significantly, laying the foundation for our further growth in the industry. Looking ahead, we will continue to capitalise on the robust market demand of grape wine products in the PRC in order to maximise business growth in the future. By leveraging the advantages of the Group in a wide range of areas, such as our reputable brand name, comprehensive product and market knowledge and extensive distribution network, further upgrading our product mix and pursuing appropriate capacity expansion strategies, we will further consolidate and strengthen our leading position in the PRC and generate greater value for our shareholders in the years ahead.

Interim Dividend

The Directors are pleased to declare an interim dividend of HK3.7 cents per Share. The interim dividend will be paid to shareholders whose names appear on the Register of Members on Wednesday, 19 October 2005. The interim dividend will be paid on Wednesday, 2 November 2005.

Closure of Register of Members

The Register of Members of the Company will be closed from Monday, 17 October 2005 to Wednesday, 19 October 2005, both days inclusive, during which period no share transfer will be effected. In order to qualify for the interim dividend, all transfers accompanied by the relevant share certificates must be lodged with the Company's branch share registrar in Hong

Kong, Tricor Investor Services Limited, Ground Floor, Bank of East Asia Harbour View Centre, 56 Gloucester Road, Wanchai, Hong Kong, for registration of not later than 4:30 pm on Friday, 14 October 2005.

Share Option Scheme

Details of the Company's Share Option Scheme are set out in the published annual report of the Company for the year ended 31 December 2004. Share options are granted to Directors, other than the independent non-executive directors, and employees of the Group to provide incentive and/or reward for their contribution to, and continuing efforts to promote the interest of the Group. Details of the share options granted, exercised, lapsed and cancelled under the Scheme during the period and outstanding as at 30 June 2005 are as follows:

	Granted	Exercised	Lapsed/ Cancelled	Outstanding options held at 30 June 2005	Approximate percentage of issued share capital of the Company
Executive directors:					
Mr. He Xiuheng	2,300,000	—	—	2,300,000	0.19%
Mr. Gao Xiaode	2,100,000	—	—	2,100,000	0.17%
Mr. Nie Jiansheng	1,950,000	—	—	1,950,000	0.16%
Mr. Bai Zhisheng	1,100,000	—	—	1,100,000	0.09%
Mr. Chen Naiming	1,950,000	—	—	1,950,000	0.16%
Non-executive directors:					
Mr. Heriard-Dubreuil Francois	1,200,000	—	—	1,200,000	0.10%
Mr. Wang Guanghao	900,000	—	—	900,000	0.07%
Mr. Cheung Wai Ying, Benny	900,000	—	—	900,000	0.07%
Mr. Zhang Wenlin	900,000	—	—	900,000	0.07%
Mr. Wong Ching Chung	900,000	—	—	900,000	0.07%
Mr. Robert Luc	900,000	—	—	900,000	0.07%
Other employees	8,000,000	—	—	8,000,000	0.64%
Total	23,100,000	—	—	23,100,000	1.86%

All of the above share options were granted on 27 January 2005, with an exercise price of HK$3.00 and are exercisable from 17 August 2005 to 26 January 2015.

Directors' Interests and Short Positions in the Shares, Underlying Shares and Debentures of the Company

As at 30 June 2005, the interests and short positions of the Directors, chief executives and their respective associates of the Company in the shares, underlying shares and debentures of the Company or its associated corporation (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) which require notification pursuant to Divisions 7 and 8 of Part XV of the SFO or which were required to be recorded in the register required to be kept under Section 352 of SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies, were as follows:

(a) Long position in Shares

Name	Capacity	Number of Shares interested	Approximate percentage of issued share capital of the Company
Mr. Cheung Wai Ying, Benny	Corporate interest	45,000,000 (Note)	3.6%

Note: Inttra Limited directly owns 45,000,000 Shares or 3.6% of the issued share capital of the Company. The entire issued share capital of Inttra Limited is owned by Mr. Cheung Wai Ying, Benny and his spouse. By virtue of the SFO, Mr. Cheung Wai Ying, Benny is deemed to be interested in the Shares held by Inttra Limited.

(b) Rights to acquire Shares

The interests of the Directors in the share options of the Company as beneficial owner are set out in the section headed "Share Option Scheme" above.

Except as set out above, as at 30 June 2005, none of the Directors and chief executives and their respective associates has any interest or short positions in the shares, underlying shares and debentures of the Company or its associated corporation (within the meaning of Part XV of the SFO) which require notification pursuant to Divisions 7 and 8 of Part XV of the SFO or which were required to be recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed companies.

Substantial Shareholders' Interests and Short Positions in the Shares and Underlying Shares of the Company

As at 30 June 2005, so far as was known to the Directors or chief executive of the Company, the interests or short positions of every person, other than a Director or chief executive of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, in the shares and underlying shares of the Company as recorded in the register required to be kept by the Company under Section 336 of the SFO are as follows:

Long position in shares

Name	Nature of interest	Number of Shares held	Approximate percentage of the Company's issued share capital
Famous Ever Group Limited	Beneficial owner	558,000,000	44.82%
Tianjin Development Holdings Limited (Note 1)	Interest of a controlled corporation	558,000,000	44.82%
Tianjin Investment Holdings Limited (Note 2)	Interest of a controlled corporation	558,000,000	44.82%
Tsinlien Group Company Limited (Note 3)	Interest of a controlled corporation	558,000,000	44.82%
Remy Pacifique Limited	Beneficial owner	297,000,000	23.86%
Remy Concord Limited (Note 4)	Interest of a controlled corporation	297,000,000	23.86%
Remy Cointreau S.A. (Note 4)	Interest of a controlled corporation	297,000,000	23.86%
Orpar S.A. (Note 4)	Interest of a controlled corporation	297,000,000	23.86%
Andromede S.A. (Note 4)	Interest of a controlled corporation	297,000,000	23.86%

Notes:

(1) Famous Ever Group Limited is a wholly owned subsidiary of Tianjin Development Holdings Limited ("Tianjin Development"). By virtue of the SFO, Tianjin Development is deemed to be interested in the Shares held by Famous Ever Group Limited.

(2) Tianjin Investment Holdings Limited ("Tianjin Investment") owns 63.86% shareholdings in Tianjin Development. By virtue of the SFO, Tianjin Investment is deemed to be interested in the Shares held by Tianjin Development.

(3) Tianjin Investment is a wholly owned subsidiary of Tsinlien Group Company Limited, the ultimate holding company of Tianjin Development. By virtue of the SFO, Tsinlien Group Company Limited is deemed to be interested in the Shares held by Tianjin Investment.

(4) Remy Pacifique Limited is a wholly owned subsidiary of Remy Concord Limited, which is wholly owned by Remy Cointreau S.A.. Orpar S.A. owns approximately 50.87% of the shareholding in Remy Cointreau S.A. and Andromede S.A. owns approximately 84.83% of the shareholding in Orpar S.A. By virtue of Part XV of the SFO, each of Remy Concord Limited, Remy Cointreau S.A., Orpar S.A. and Andromede S.A. is deemed to be interested in the Shares held by Remy Pacifique Limited.

Saved as disclosed above, as at 30 June 2005, no person, not being a Director or chief executive of the Company, had interests or short positions in the shares and underlying shares of the Company as record in the register required to be kept by the Company under Section 336 of the SFO.

Purchase, Sale or Redemption of Shares of the Company

Pursuant to the international underwriting agreement dated 21 January 2005, the Company granted an option ("Over-allotment Option") to the international placing underwriters exercisable by ABN AMRO Rothschild, to require the Company to allot and issue up to an aggregate of 45,000,000 additional Shares to cover over-allocation in the international placing. The exercise price per Share for the Over-allotment Option is HK$2.25. On 1 February 2005, the Over-allotment Option was fully exercised and, as a result, the Company issued 45,000,000 additional Shares.

Except for as disclosed above, since the listing of the Company's Shares on the Stock Exchange on 26 January 2005 and up to 30 June 2005, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's Shares.

Compliance with the Model Code for Securities Transactions by Directors

The Company has adopted procedures governing Directors' securities transactions in compliance with the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 of the Listing Rules. Upon enquiry by the Company, all Directors had confirmed that they had complied with the required standards set out in the Model Code throughout the six months ended 30 June 2005.

Corporate Governance

The Company recognises its responsibilities to shareholders and aims to protect and enhance shareholder value through solid corporate governance. Considerable efforts are devoted to identify and formalise best practices. The Group is committed to ensuring even greater transparency and quality of disclosures. The Board has been and will continue to uphold the appropriate standards of corporate governance within the Group, thereby ensuring that all business is conducted in an honest, ethical and responsible manner.

The Company had complied throughout the half-year ended 30 June 2005 with the Code Provisions set out in the Code on Corporate Governance Practices contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

By order of the Board
Mr. He Xiuheng
Chairman

Hong Kong, 13 September 2005