

REPORT OF THE DIRECTORS

To be presented at the Forty-third Annual General Meeting of shareholders to be held at the Langham Hotel, 8 Peking Road, Tsimshatsui, Kowloon, Hong Kong on Tuesday, 11th April 2006 at 2:00pm.

The Directors submit herewith their Annual Report together with the audited financial statements for the year ended 31st December 2005.

PRINCIPAL PLACE OF BUSINESS

San Miguel Brewery Hong Kong Limited (the "Company") is a company incorporated and domiciled in Hong Kong and has its registered office and principal place of business at 9/F., Citimark Building, 28 Yuen Shun Circuit, Siu Lek Yuen, Shatin, New Territories, Hong Kong.

PRINCIPAL ACTIVITIES

The principal activities of the Company and its subsidiaries (the "Group") continue to be the manufacture and distribution of bottled, canned and draught beers.

The analysis of geographical locations of the operations of the Group during the financial year are set out in Note 14 to the financial statements.

As the Group's turnover, profit and loss are almost entirely attributable to these activities, no analysis by activity is provided.

MAJOR CUSTOMERS AND SUPPLIERS

For the year ended 31st December 2005, the percentages of the Group's gross turnover and purchases attributable to major customers and suppliers were as follows:

Gross turnover attributable to:

Largest customer	16.3%
Five largest customers	43.5%

Purchases attributable to:

Largest supplier	11.9%
Five largest suppliers	20.9%

As at 31st December 2005, none of the Directors, their associates, or any shareholder (which to the knowledge of the Directors owned more than 5% of the Company's share capital) had any interest in the above major customers or suppliers.

FINANCIAL STATEMENTS

The loss of the Group for the year ended 31st December 2005 and the state of affairs of the Company and the Group at that date are set out in the financial statements on pages 30 to 75 of this Annual Report.

TRANSFER TO RESERVES

Loss for the year of HK\$66 million (2004: profit (restated) of HK\$12.5 million) have been transferred to reserves. Other movements in reserves are set out in Note 31 to the financial statements.

DIVIDENDS

An interim dividend of 1 cent per share, was paid on 30th September 2005 to shareholders of record on 19th September 2005. The Directors have resolved that no final dividend be declared for the year 2005.

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CHARITABLE AND OTHER DONATIONS

The Group made donations for charitable and other purposes totalling \$17,000 (2004: \$31,000) during the financial year.

FIXED ASSETS

The Group spent \$20.1 million (2004: \$12.4 million) on fixed assets during the year. Particulars of the movements of fixed assets during the year are set out in Note 15 to the financial statements.

SUBSIDIARIES

Particulars of the Company's subsidiaries are set out in Note 18 to the financial statements.

LIQUIDITY AND FINANCIAL RESOURCES

Working capital at the end of the year was \$361 million compared with \$478 million (restated) in 2004.

Cash and bank deposits at year end were \$383 million (2004: \$455 million) and are sufficient to fund working capital requirements and capital expenditure in 2006.

BANK LOANS

The Group has short term credit facilities of \$169 million (2004: \$168 million) of which \$50 million (2004: \$51 million) had been utilised as at 31st December 2005.

Long term loans at year end amounted to \$95 million (2004: \$195 million).

Total borrowings at the year end for the Company were \$95 million (2004: \$195 million) and for the Group \$145 million (2004: \$246 million).

Particulars of bank loans of the Company and the Group are set out in Note 25 to the financial statements.

DIRECTORS

With the exception of Mr. Chong Yoon Fatt, Ms. Minerva Lourdes Bibonia, Ms. Ma. Belen C. Buensuceso, Mr. Ferdinand K. Constantino and Mr. Roberto N. Huang, the Directors of the Company, whose names appear on page 2 of the Annual Report, were Directors for the financial year and as at the date of this Annual Report.

Messrs Benjamin P. Defensor, Jr., Francisco C. Eizmendi, Jr., Ramon A. de la Llana, Thomas R. Mainwaring and Carmelo L. Santiago resigned from the office of Director during the year 2005. Messrs Francis H. Jardeleza, Estelito P. Mendoza and Gabriel L. Villareal resigned from the office of Director on 24th February 2006.

Messrs Ng Wai Sun and Ian F. Wade retire by rotation in accordance with Article 105 of the Company's Articles of Association at the forthcoming Annual General Meeting and, being eligible, offer themselves for re-election.

Mr. Chong Yoon Fatt, Ms. Minerva Lourdes Bibonia, Ms. Ma. Belen C. Buensuceso and Mr. Roberto N. Huang appointed to the Board since the last Annual General Meeting, retire from the office of Director in accordance with Article 96 of the Company's Articles of Association, and offer themselves for re-election at the forthcoming Annual General Meeting.

None of the Directors proposed for re-election has a service agreement with the Company or any of its subsidiaries which is not determinable within one year without payment of compensation, other than normal statutory compensation.

DIRECTORS' INTERESTS

As at 31st December 2005, the Directors and their associates had the following beneficial interests in the issued share capital of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) as recorded in the register required under Section 352 of the SFO:

(1) INTERESTS IN ISSUED SHARE CAPITAL

Name of Director	Number of ordinary shares of \$0.50 each in the Company			Approximate percentage of shareholding
	Personal interests	Family interests	Total	
David K.P. Li	300,000	–	300,000	0.08%

Name of Director	Number of shares in San Miguel Corporation			Approximate percentage of shareholding
	Personal interests	Family interests	Total	
<i>Class A (par value of 5 pesos each):</i>				
Ramon S. Ang	6,050	–	6,050	0.000193%
Faustino F. Galang	33,800	–	33,800	0.001076%
Ferdinand K. Constantino	114,224	2,070	116,294	0.003638%
Francis H. Jardeleza	25,001	–	25,001	0.000796%
Estelito P. Mendoza	31,972	–	31,972	0.001018%
Gabriel L. Villareal	24,572	11,550	36,122	0.001152%

<i>Class B (par value of 5 pesos each):</i>				
Faustino F. Galang	50,000	–	50,000	0.001593%
Francis H. Jardeleza	90,000	–	90,000	0.002867%
Gabriel L. Villareal	–	31,900	31,900	0.001017%

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DIRECTORS' INTERESTS (Continued)

(2) INTERESTS IN UNDERLYING SHARES

Certain Directors of the Company have been granted stock options to subscribe for common shares in San Miguel Corporation. Particulars of stock options in San Miguel Corporation held by Directors during the year and as at 31st December 2005 are as follows:

Stock options in San Miguel Corporation							
		Exercise	Exercise	Balance as			Balance
	Date	period	price per	at 1st	Granted	Exercised	Balance
Name of Director	granted	up to	option	January	during	during	as at 31st
			(pesos)	2005	the year	the year	December
							2005
Class A (par value of 5 pesos each):							
Ramon S. Ang	26/06/03	26/06/11	54.50	259,422	–	–	259,422
	01/10/04	01/10/12	57.50	266,854	–	–	266,854
	10/11/05	10/11/13	65.00	–	204,654	–	204,654
Faustino F. Galang	26/06/03	26/06/11	54.50	85,306	–	56,871	28,435
	01/10/04	01/10/12	57.50	87,751	–	–	87,751
	10/11/05	10/11/13	65.00	–	67,090	–	67,090
Chong Yoon Fatt	10/11/05	10/11/13	65.00	–	1,027	–	1,027
Ferdinand K. Constantino	26/06/03	26/06/11	54.50	50,514	–	33,676	16,838
	01/10/04	01/10/12	57.50	56,643	–	–	56,643
	10/11/05	10/11/13	65.00	–	48,391	–	48,391
Francis H. Jardeleza	26/06/03	26/06/11	54.50	52,537	–	35,025	17,512
	01/10/04	01/10/12	57.50	56,476	–	–	56,476
	10/11/05	10/11/13	65.00	–	45,086	–	45,086
Class B (par value of 5 pesos each):							
Ramon S. Ang	26/06/03	26/06/11	62.50	111,181	–	–	111,181
	01/10/04	01/10/12	70.50	114,366	–	–	114,366
	10/11/05	10/11/13	89.50	–	136,436	–	136,436
Faustino F. Galang	26/06/03	26/06/11	62.50	36,560	–	24,374	12,186
	01/10/04	01/10/12	70.50	37,607	–	–	37,607
	10/11/05	10/11/13	89.50	–	44,727	–	44,727
Chong Yoon Fatt	10/11/05	10/11/13	89.50	–	684	–	684
Ferdinand K. Constantino	26/06/03	26/06/11	62.50	21,649	–	14,433	7,216
	01/10/04	01/10/12	70.50	24,275	–	–	24,275
	10/11/05	10/11/13	89.50	–	32,260	–	32,260
Francis H. Jardeleza	26/06/03	26/06/11	62.50	22,516	–	15,011	7,505
	01/10/04	01/10/12	70.50	24,204	–	–	24,204
	10/11/05	10/11/13	89.50	–	30,057	–	30,057

Note:

The only stock options exercised by Directors during the year were those disclosed above.

All interests in the share and underlying shares of the Company and its associated corporations are long positions.

None of the Directors or their associates had any interests in the issued share capital or in stock options of the Company or any of its associated corporations other than those disclosed above.

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SUBSTANTIAL INTERESTS IN THE SHARE CAPITAL OF THE COMPANY

As at 31st December 2005 according to the register required under Section 336 of the SFO, the Company was notified that the following shareholders had an interest of 5% or more of its issued share capital:–

Name	Number of shares of \$0.50 each Ordinary shares held	Percentage of total issued shares
Neptunia Corporation Limited (<i>note 1</i>)	245,720,800	65.78%
HKSCC Nominees Limited	66,707,356	17.86%
Conroy Assets Limited (<i>note 2</i>)	13,624,600	3.65%
Hamstar Profits Limited (<i>note 2</i>)	10,078,400	2.70%

Notes:

1. San Miguel Corporation ("SMC"), San Miguel International Limited ("SMIL"), San Miguel Holdings Limited ("SMHL") and San Miguel Brewing International Limited ("SMBIL") are all deemed to hold the above disclosed interest of Neptunia Corporation Limited ("Neptunia") in the Company because SMC has a controlling interest in SMIL, SMIL has a controlling interest in SMHL, SMHL has a controlling interest in SMBIL and SMBIL has a controlling interest in Neptunia.
2. Mr. Li Ka-Shing, Cheung Kong (Holdings) Limited, Li Ka-Shing Unity Trustee Company Limited, Li Ka-Shing Unity Trustee Corporation Limited and Li Ka-Shing Unity Trustcorp Limited are all deemed to hold the above disclosed interest of Conroy Assets Limited ("Conroy") and Hamstar Profits Limited ("Hamstar") in the Company. The aggregate interest of Conroy and Hamstar exceeding 5% of the issued share capital of the Company constitutes a duty of disclosure under the SFO.

All interests in the share of the Company are long positions.

Apart from the foregoing, no other interests required to be recorded in the register kept under Section 336 of the SFO have been notified to the Company.

SUFFICIENCY OF PUBLIC FLOAT

Based on the information that is publicly available to the Company and within the knowledge of the Directors of the Company as at the date of this annual report, the Company has maintained the prescribed public float under the Listing Rules.

DIRECTORS' INTERESTS IN CONTRACTS

Pursuant to an Agreement dated 12th June 1963, Neptunia Corporation Limited provides technical and advisory services to the Company and may be paid a General Managers' Commission. Messrs Ramon S. Ang, Faustino F. Galang, Chong Yoon Fatt, Ferdinand K. Constantino, Francis H. Jardeleza, Estelito P. Mendoza and Gabriel L. Villareal are interested parties to this contract to the extent that they either have equity interests in or are directors of San Miguel Corporation, the ultimate holding company of Neptunia Corporation Limited. General Managers' Commission has not been paid by the Company or charged by Neptunia Corporation Limited since the 1995 financial year.

Save as disclosed above, during the financial year and at the end of the year, no Director of the Company has had a material interest in any significant contract to which the Company or any related company (the holding company, subsidiaries or fellow subsidiaries) was also a party.

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CONNECTED TRANSACTIONS

In order to comply with the Listing Rules, the Company entered into an agreement (the "Agreement") with San Miguel Corporation ("SMC"), the ultimate holding company of the Company, on 11th March 2005 to govern the terms upon which the continuing connected transactions will be carried out between members of the Group and members of the SMC Group. The Agreement will expire on 31st December 2007. Under the Agreement, the Group entered into the following continuing connected transactions during the year. Each of the continuing connected transactions is not expected to exceed the following Caps.

The Agreement was approved by independent shareholders at the Extraordinary General Meeting of the Company held on 7th April 2005.

in Hong Kong dollar thousands

	2005 Actual	2005 Cap	2006 Cap	2007 Cap
Purchase of packaging materials (comprising cans, bottles, crown seals and crates) by the Group from the SMC Group	33,255	47,800	92,600	105,700
Purchase of packaged beer by the Group from the SMC Group	2,716	4,300	4,700	5,000
Sales of packaged beer by the Group to the SMC Group	40,490	46,100	53,600	60,700
Payment of commission by the Group to the SMC Group in respect of sales of packaged beer by the Group directly to customers in certain countries (other than Hong Kong, Macau and the PRC)	1,037	1,100	1,300	1,600

The on-going transactions had been reviewed by the Independent Non-Executive Directors of the Company who had confirmed that the on-going transactions were entered into:

- (1) in the ordinary and usual course of business of the Group;
- (2) on normal commercial terms and on terms in accordance with the Agreement that were fair and reasonable so far as the shareholders of the Company were concerned; and
- (3) the aggregate amount of the on-going transactions did not exceed the limit as set out in the announcement dated 11th March 2005.

The Company has received from the auditors a letter reporting that the on-going transactions:

- (1) have received the approval of the Board of Directors of the Company;
- (2) were entered into in accordance with the pricing policies of the Company;
- (3) have been entered into in accordance with the Agreement dated 11th March 2005; and
- (4) have not exceeded the relevant caps as set out in the announcement dated 11th March 2005.

RETIREMENT AND PENSION PLANS, PERSONNEL AND PAYROLL

The Company and its subsidiaries in Hong Kong have sponsored a non-contributory defined benefit scheme, The San Miguel Brewery Hong Kong Limited Retirement Fund (the "Fund"), covering local permanent employees, which was registered in September 1995 under the Occupational Retirement Schemes Ordinance. The Fund is formally established under trust and the assets are separately held in an independently administered fund. The members' benefits are determined based on the employees' final remuneration and length of service. Contributions to the Fund are made in accordance with the recommendations of independent actuaries who value the retirement scheme at regular intervals, usually triennially.

The Fund was granted exemption from Mandatory Provident Fund regulations by the Mandatory Provident Fund Scheme Authority on 24th July 2000, following modifications to the Fund benefits which comply with Mandatory Provident Fund regulations.

Pursuant to Government legislation, Allianz Global Investors Hong Kong Limited was selected by the Company as an alternative Mandatory Provident Fund ("MPF") service provider for employees of the Company who do not wish to remain in or join the Company Fund. The MPF scheme is a defined contribution retirement scheme administered by independent trustees. Under the MPF scheme, the employer and its employees are each required to make contributions to the scheme at 5% of the employees' relevant income, subject to a cap of monthly relevant income of \$20,000. Contributions to the MPF scheme vest in employee members immediately.

Employees in the subsidiaries in the People's Republic of China are members of the Central Pension Scheme operated by the Chinese government. The subsidiaries are required to contribute a certain percentage of their covered payroll to the Central Pension Scheme to fund the benefits. Contributions to the Central Pension Scheme vest in employee members immediately. The only obligation for the subsidiaries with respect to the Central Pension Scheme is the associated required contribution under the Central Pension Scheme.

A formal actuarial assessment of the San Miguel Brewery Hong Kong Limited Retirement Fund was carried out as at 31st December 2005 and the results were as follows:

- (A) The actuary of the Fund is Mr. A. Wong, Fellow of the Canadian Institute of Actuaries and Fellow of the Society of Actuaries. In the actuarial valuation, the attained age method was used. Other major assumptions used in the valuation were: Investment return 7% per annum; Long term salary escalation 3% per annum; Mortality Rates 2001 Hong Kong Life Tables; Normal retirement age 60; Early retirement rates allowed between ages 55 to 60.
- (B) The unaudited market value of the Fund assets was \$81.4 million as at 31st December 2005.
- (C) The minimum level of funding as recommended by the Fund actuary was 16% of salary for 2006, 19% for 2007 and 20% for 2008.
- (D) The solvency deficit was \$24.9 million, i.e. the obligation under this Fund was 77% covered by the Fund's assets, at 31st December 2005.

For the purposes of preparing the financial statements, an independent actuarial valuation was also carried at 31st December 2005 following the methodology set out in Hong Kong Accounting Standard 19, Employee benefits. Details of this valuation is set out in Note 29 to the financial statements.

Particulars of the number of personnel and payroll expenses of the Group are set out on page 3 of this Annual Report.

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PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SHARES

During the year ended 31st December 2005, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of its listed shares.

FIVE YEAR SUMMARY

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on page 77 of this Annual Report.

CODE OF BEST PRACTICE

Principal corporate governance practices adopted by the Company are set out in the Corporate Governance section on pages 17 to 22.

CONFIRMATION OF INDEPENDENCE

The Company has received from each of the Independent Non-Executive Directors an annual confirmation of independence pursuant to Rule 3.13 of the Listing Rules and considers all the Independent Non-Executive Directors to be independent.

AUDITORS

A resolution for the re-appointment of KPMG as auditors of the Company is to be proposed at the forthcoming Annual General Meeting.



Ramon S. Ang
Chairman

Hong Kong, 24th February 2006