Industry Review

In 2006, the Chinese meat processing industry was confronted by tough challenges from the substantial hog price fluctuations, natural disasters and a series of abrupt public health incidents. Nevertheless, adhering to its brand advantages, flexible pricing policies, nationwide strategic layout and its commitment to product quality, the Group continued to stand out as one of the leading players in the Chinese meat products market during the year.

Business Review

Year 2006 is the first full financial year after the Group's listing. Based on the encouraging performance in the first half of the year, we continued to expand production and optimise production bases during the second half to prepare for the continuous capacity growth and to satisfy the market demand in 2007. At the same time, we stepped up our efforts to new product development, market expansion and marketing initiatives, laying solid foundations for the Group's mid-to-long term competitive edge and sustainable growth.

Sales and Distribution

In 2006, the Group successfully pursued its stated strategy of focusing on medium and high-end products to further boost the sales of chilled pork and Low Temperature Meat Products ("LTMP"). Sales of chilled pork totalled RMB2,128 million, representing an increase of 5.6% from that of the previous year. This represented 42.2% (2005: 42.2%) of the Group's total sales (before inter-segment elimination) and 58.6% (2005: 57.0%) of the Group's turnover in the upstream slaughtering business. Sales of LTMP were RMB1,184 million, an increase of 19.6% as compared with 2005, and represented 23.5% (2005: 20.8%) of the Group's total sales (before inter-segment elimination) and 83.8% (2005: 80.2%) of the Group's turnover in downstream processed meat products.

Benefiting from the consumers' demand for medium and high-end products that are hygienic, tasty and healthy, the Group further diversified its product portfolio by developing high-end products with higher gross margins. The Group also committed to enhancing its marketing effort while expanding product distribution networks. Such products are sold mainly through modern retail channels, primarily hypermarkets and supermarket chains, convenience stores and distributors in prime locations. During the year, the Group expanded sales in some affluent and fast growing small to medium cities, particularly in northern and northeastern China, giving rise to a wider and deeper geographical coverage in the PRC. During the year, our products have revealed presence in new cities in the mainland including Shaoxing, Qinhuangdao and Qiqihar.

In order to further enhance our branding strategy, we gradually consolidated our chilled pork products under our flagship "Yurun" brand during the year. We also selectively increased advertisements in high return mobile media (such as buses and mass transportation system) to strengthen our "Yurun" brand in medium to high-end markets.

Production Facilities and Production Capacity

To better implement its plan of expanding upstream production capacity for the booming market demands, the Group adopted a combination of flexible measures, such as acquisition, upgrading of existing facilities as well as green field projects to expand the production capacity of chilled and frozen pork. Through the acquisition of Yurun Beixu plant in Henan Province during the first half of the year and Shandong Jinan Plant and Hubei Badong Plant in the second half of the year, the Group's annual slaughtering capacity increased by 1.7 million heads. Combining with the upgraded capacities in our existing plants in Suzhou, Kaiyuan and Suihua, the Group's annual slaughtering capacity exceeded 10 million heads as of the end of 2006.

In the downstream, the Group has been focusing on supplementing market coverage, de-bottlenecking and upgrading key production facilities. Annual production capacity of our downstream meat processing business increased by 5,000 tons from the end of 2005 to 168,000 tons as at the end of 2006. The increase was mainly due to completion of a new production facility in Xinjiang and upgrading of production capacities in Nanjing during the year.

We expedited the construction of new capacity in northeastern China and expansion of existing plants in eastern China to pave the way for sustaining capacity growth and to meet the market demand in 2007.

Against a backdrop of increased geographical coverage and rapid sales growth, the Group managed to maintain a rather stable utilization rate amid fast production capacity expansion. The weighted average utilisation rates were 66% for the upstream slaughtering businesses while that of the downstream meat processing businesses increased to 57% in 2006.

Product Quality and R&D

The Group has placed emphasis on quality management since its establishment. Internal quality controls are properly secured at each process of procurement, production, sale and logistics, wining us a good reputation among consumers and in the industry.

Meanwhile, the Group's R&D team comprising over 200 members continued to focus on the research and development ("R&D") of mid-to-high end new products to foster a new meat consumption trend. These products proved to be competitive. Our team had successfully launched 74 new products in 2006 and they were very positively received by the market.

Financial Review

Turnover

By the end of 2006, the Group offered a selection of over 800 types of processed meat products. With the improvement in the living standards and changing life styles of people in the PRC, there is a growing demand for high-end gourmet food products that are delicious, nutritious, hygienic and convenient, with LTMP being trendier in the domestic consumer market. To further strengthen competitiveness and market share, the Group refined its product mix, increased its marketing efforts for high-end LTMP products, strengthened product promotion by working with large scale retail shops and hotels, and explored new marketing channels. Thanks to these efforts, sales of LTMP products recorded satisfactory growth.

In 2006, sales of LTMP were RMB1,184 million, an increase of 19.6% compared with RMB991 million in 2005 and represented 83.8% (2005: 80.2%) of the Group's total turnover in processed meat products. Sales of HTMP decreased by 6.0%, from RMB244 million in 2005 to RMB230 million and represented 16.2% (2005: 19.8%) of the Group's total turnover in processed meat products.

In 2006, the Group sold a total of approximately 444,000 tons of chilled and frozen pork, representing an increase of approximately 13.6% compared to that of last year. Total turnover (before inter-segment elimination) in upstream businesses increased by 2.7% to RMB3,629 million, primarily due to our market-based pricing strategy as a result of the declining in the average live hog prices during the year. In 2006, chilled pork accounted for 58.6% (2005: 57.0%) of the total turnover in upstream businesses, with sales volume of approximately 243,000 tons (up 20.7% over 2005) and sales revenue of RMB2,128 million (up 5.6% over 2005). Frozen pork accounted for 41.4% (2005: 43.0%) of the total turnover in upstream businesses, with sales volume of approximately 201,000 tons, up 6.1% over 2005, and sales revenue reached RMB1,501 million.

Gross Profit and Gross Profit Margin

The Group's gross profit increased by 13.6% from RMB639 million in 2005 to RMB726 million in 2006 as a result of the substantial increase in sales during the year. The Group managed to maintain sustainable profit growth amid the hog price fluctuations.

The Group's overall gross profit margin increased by 1.0 percentage point from 14.4% in 2005 to 15.4% in 2006. The increase was due to the Group's focus on sales of higher margin chilled pork and LTMP. In addition, as "Yurun" is a well-known brand, our selling price is relatively stable.

For the processed meat business, the gross profit margin was 26.1% for LTMP and 19.3% for HTMP, an increase of 2.7 and 1.7 percentage points compared with 2005 respectively, primarily due to the relatively reduction in the cost of sales and the Group's efforts to develop and launch out high-end and high margin products in 2006.

In the raw pork segment, the gross profit margin of chilled and frozen pork was 12.4% and 7.5% respectively, similar to the level of 2005. As the Group's pricing power was enhanced and the increase in popularity of chilled pork products in the PRC, we recorded a stable average gross profit margin during the year despite the violent fluctuations of hog prices.

Other Operating Income

Other operating income mainly includes government subsidies and negative goodwill. In 2006, the Group had other operating income of RMB91.40 million (2005: RMB23.37 million), primarily due to the negative goodwill of RMB40 million recorded as a result of the acquisition of Henan Yurun Beixu Meat Food Co., Ltd.

Operating Expenses

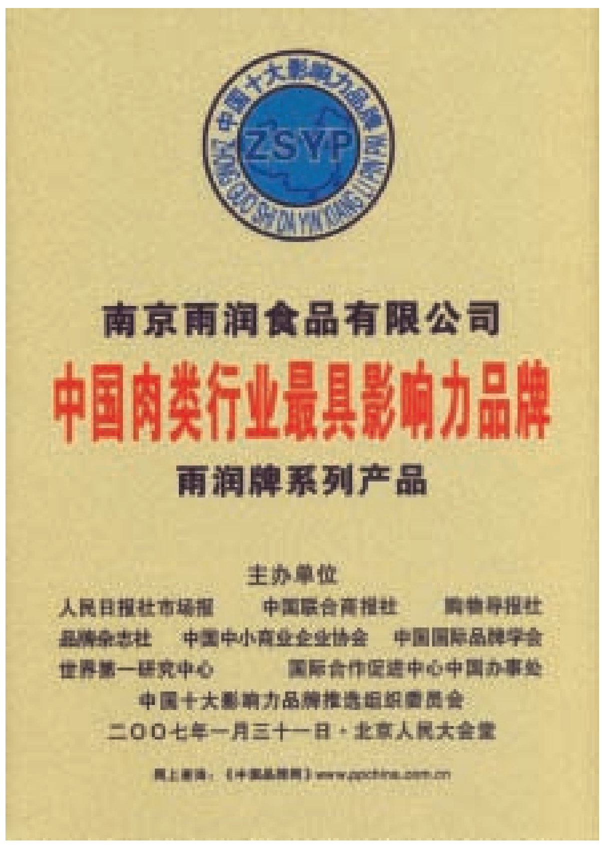
Operating expenses include distribution expenses, administrative expenses and other operating expenses. In 2006, the Group's operating expenses were RMB333 million, an increase of 25.8%, compared to RMB264 million in 2005. Operating expenses represented 7.1% of the Group's turnover, an increase of 1.2 percentage points compared to 5.9% in 2005. The increase in operating expenses was due to an increase in sales volume, promotion costs, salary expenses, research and development expenses and transportation costs as well as an increase in expenses due to the opening of new plants and new sales networks.

Operating Profit

In 2006, the Group's operating profit was RMB485 million, an increase of 21.8% from RMB398 million in 2005.

Net Financing Cost

The Group's net financing cost for 2005 was RMB31 million where there was a net financing income of RMB9.89 million in 2006. This was mainly because after the listing of the Company's shares on the Stock Exchange ("IPO"), all convertible instruments were converted into equity and the Group no longer incurred the corresponding amortisation of discounts and transaction costs of the convertible instruments in 2006. In addition, interest income also increased in 2006 because the unused proceeds from the IPO were deposited as short-term deposits in banks. Interest expenses also declined as a result of lower balance of bank loans.



Taxation

For the year ended 31 December 2006, the income tax was RMB5.62 million with an effective tax rate of 1.1%, representing a decrease of 26.8% in income taxes and 1.0 percentage point in effective tax rate, respectively, compared with a total of RMB7.69 million income tax and an effective tax rate of 2.1% in 2005. The reason is that most of the Group's subsidiaries were able to enjoy preferential tax treatment after the reorganisation for IPO.

Net profit

Taking all the above factors into account, the Group's net profit for 2006 increased by 36.3% to RMB489 million, from RMB359 million in 2005. Net profit margin for 2006 was 10.4%, representing an increase of 2.3 percentage points compared with 8.1% in 2005.

Financial Resources

The Group's major financial resources were the proceeds from the IPO in 2005 and cash inflow from operating activities during the year. Cash inflow from operating activities during the year amounted to RMB411 million, with cash balance of RMB844 million as of 31 December 2006, representing a decrease of RMB512 million compared with that of 31 December 2005. The money was applied for the Group's investments in strategic acquisitions and production facilities during the year as well as to prepare for the sustainable production capacity growth in 2007 in order to meet the market demand for the Group's products.

The Group had RMB43 million outstanding bank loans as of 31 December 2006. It is expected that the amount will be repaid in 2007.

During the year, the Group used capital for strategic acquisition and investment in production facilities, while maintaining stable financial management and adequate liquidity for daily operations and other capital needs.

Assets and Liabilities

As of 31 December 2006, the Group's total assets and total liabilities were RMB3,151 million and RMB690 million, an increase of RMB294 million and RMB75 million compared with 31 December 2005 respectively.

As of 31 December 2006, the Group's equity attributable to equity holders of the Company was RMB2,449 million. Total equity including minority interests was RMB2,461 million, representing an increase of RMB219 million compared with RMB2,242 million as of 31 December 2005.

As of 31 December 2006, the Group's gearing ratio (total debt represented by the sum of bank loans and finance lease liabilities divided by the sum of total debt and equity) was 8.6%, a significant improvement when compared with that of 12.1% as of 31 December 2005.

Capital Commitments

Details of the Group's capital commitment as of 31 December 2006 are set out in note 36 to the financial statements.

Foreign Exchange Risk

Most of the Group's income and expenses are denominated in Renminbi. For the year ended 31 December 2006, the Group did not experience any material difficulties or negative effects on its operations or liquidity due to currency exchange rate fluctuations.

Human Resources

As of 31 December 2006, the Group employed 11,519 (2005: 9,286) employees in the PRC and Hong Kong. Total staff costs for the year were RMB171 million, accounting for 3.6% of the Group's turnover (2005: RMB112 million, accounting for 2.5% of turnover).

The Group offered competitive remuneration as incentive to staff for innovation and improvements, which was in line with industry practice. We offered performance-based bonuses to staff. The Group provided other employee benefits including contributions to social security scheme such as retirement benefit schemes. The Company has a share option scheme in place as a mean to encourage and reward the qualified employees' (including directors') contributions to the Group's results and business development based on their individual performance. On 10 November 2006, the Company for the first time granted 40,250,000 share options in total to 65 eligible employees, senior management and executive directors. In addition, the Group invested in continuing education and training for management and employees to help improve their skills and knowledge continuously.

With reinforced quality control, our products are warm welcomed by customers for the taste and hygiene