玖源生態農業科技(集團)有限公司

Ko Yo Ecological Agrotech (Group) Limited

(incorporated in the Cayman Islands with limited liability)

(Stock code: 8042)

2006
Annual Report

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This report, for which the Directors of Ko Yo Ecological Agrotech (Group) Limited collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the Growth Enterprise Market of the Stock Exchange of Hong Kong Limited for the purpose of giving information with regard to Ko Yo Ecological Agrotech (Group) Limited. The Directors of Ko Yo Ecological Agrotech (Group) Limited, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief: (i) the information contained in this report is accurate and complete in all material respects and not misleading; (ii) there are no other matters the omission of which would make any statement in this report misleading; and (iii) all opinions expressed in this report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

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Corporate Information

DIRECTORS

Executive directors

Mr. Li Weiruo
Mr. Yuan Bai
Ms. Chi Chuan
Ms. Man Au Vivian
Mr. Li Shengdi

Independent non-executive directors

Mr. Hu Xiaoping
Mr. Woo Che-wor, Alex
Mr. Qian Laizhong

COMPANY SECRETARY

Mr. Chung Tin Ming, HKICPA, ACCA

QUALIFIED ACCOUNTANT

Mr. Chung Tin Ming, HKICPA, ACCA

AUDIT COMMITTEE

Mr. Hu Xiaoping
Mr. Woo Che-wor, Alex
Mr. Qian Laizhong

AUTHORIZED REPRESENTATIVES

Mr. Li Weiruo
Ms. Man Au Vivian

COMPLIANCE OFFICER

Ms. Chi Chuan

REGISTERED OFFICE

Cricket Square
Hutchins Drive
P.O. Box 2681
Grand Cayman KY1-1111
Cayman Islands

HEAD OFFICE AND PRINCIPAL PLACE OF BUSINESS IN HONG KONG

Suite No. 02, 31st Floor, Sino Plaza
255-257 Gloucester Road
Causeway Bay
Hong Kong

SHARE REGISTRAR

Union Registrars Limited
Room 1803. Fook Lee Commercial Centre, Town Place, 33 Lockhart Road
Wanchai
Hong Kong

AUDITORS

PricewaterhouseCoopers
Certified Public Accountants
22nd Floor
Prince's Building
Central
Hong Kong

PRINCIPAL BANKERS

Industrial and Commercial Bank of China
-Chengdu City Xindu Branch

Agricultural Bank of China
-Chengdu City Wuhou Branch

Shanghai Pudong Development Bank
-Chengdu Branch

The Bank of East Asia, Limited
-Chengdu Branch

Standard Chartered Bank
-Central Branch

GEM STOCK CODE

8042

WEBSITE

www.koyochem.com

Highlights

— For the year ended 31st December 2006, the profit attributable to shareholders decreased to approximately RMB29 million, which represents a decrease of 39% as compared to year 2005.

— Basic earnings per share was approximately RMB6.0 cents for the year ended 31st December 2006.

— For the year ended 31st December 2006, sale quantities increased by approximately 0.2% and turnover decreased by 2.7% as compared to year 2005.

— The sale quantities of BB Fertilizers and complex fertilizers of the Group increased to 156,571 tonnes, which represents a growth of 12% as compared with year 2005.

— The Directors have proposed to pay a final dividend of HKD0.7 cents per share for the year ended 31st December 2006.

TO SHAREHOLDERS

I am pleased to present the annual report of Ko Yo Agrotech (Group) Limited (the "Company") and its subsidiaries (Collectively the "Group") for the year ended 31st December 2006 for shareholders to peruse and review.

BUSINESS REVIEW

The financial results for the year ended 31st December 2006 were not as good as the management's expectation. The turnover and profit were lower than that of last year. The turnover of the Group was approximately RMB611 million, which represented a decrease of 2.7% as compared to that of last year. The total sales volume of the Group was approximately 472,000 tonnes (2005: 471,000 tonnes), which represented an increase of 0.2%. Audited profit attributable to shareholders of the Group was approximately RMB29 million, representing a decrease of 39% compared to that of last year. Basic earnings per share of the Group was approximately RMB6.0 cents.

One of the main factors affected the turnover and profit during the period under review was that the major manufacturing locations and target market of the Group, Sichuan Province and its peripheries, encountered the most severe drought within the past 50 years in 2006. As hydroelectric power is the main resource of Sichuan Province, power supply was reduced by the drought. Moreover, the increase usage of coal and electricity in winter, the Government limited the electricity supply for the use of industry. Another factor was that the two largest natural gas suppliers, China Petroleum & Chemical Corporation and Petro China Company Limited have spent the longest period over the previous five years, on checking and maintenance of the equipment. It caused the shortage of natural gas supply. The above two reasons led to the standstill of machineries of approximately 11,630 machinery hours and reduction of production of ammonium compound of approximately 8,720 tonnes, which negatively affected the annual production and product sales performance. Moreover, the provision on employees' stock option was approximately RMB4 million which further decrease the profit for the year ended 31st December 2006.

After reviewing the results for the year ended 31st December 2006, the directors of the Company (the "Directors") proposed a final dividend of HKD0.7 cents per share (2005: HKD1.5 cents per share). A total of HKD1.2 cents per share were declared for the year ended 31st December 2006 (2005: HKD2.0 cents per share)..

PROSPECTS

Industry Review

The Industry Continues to be Positive, Demand for Fertilizers Continues to Enlarge

According to the Ministry of Agriculture of the China estimated, in 2006, the production of crops in China continues to increase in three consecutive years. The production volume of crops reaching 490 million tonnes. In the same year, income increment of Chinese peasants rose more than 6% in three consecutive years, which was the first time in the past 21 years.

'Agricultural Development Plan of the Eleventh Five-Year Plan' pointed out that by 2010, the amount of crops production in China shall reach 500 million tonnes, keeping the current sowing areas, which could only be achieved by increasing the production amount per unit by 9% (counted based on the average production amount per unit of last 5 years). The production amounts of crops, cotton, oil, sugar, meat, egg and milk will increase by 3.3%, 19.0%, 4.0%, 27.0%, 8.5%, 4.2% and 46.6% respectively within next a few years. Calculating based on the crops demand per capita raised by Food and Agriculture Organization of the United Nations, which is 400 kg, by year 2010, the crops demand will reach around 550 million tonnes and the crops production per unit shall increase by 20%, which will still drive the increase of demand for fertilizers.

National Macro Policy Continue to be Positive and Create Favorable Environment for the Business Growth of the Group in Future

"Communist Party of China Central Committee's Policies and Advices on Development of Modern Agriculture and Promotion of Socialist New Rural Village Construction" (中共中央國務院關於積極發展現代農業扎實推進社會主義新農村建設的若干意見) was announced on 29th January 2007, which was the forth No.1 document about "San Nong" (「三農」) released by Communist Party of China Central Committee since 2004. The document would be the strong motive force for the increase of the production amount and peasant's income, improvement of comprehensive agricultural production capability, healthy agricultural development and long-term rural development.

The Ministry of Agriculture continues to promote the Testing Soil to Prescribe and Apply Suitable Fertilizers in 2007. Since the agricultural (2005) document No. 101 "Temporary Management Measures of the Compensation Fund for Testing Soil to Prescribe and Apply Suitable Fertilizers" was promulgated and implemented by the Ministry of Finance and the Ministry of Agriculture of the China on 11th July 2005, the Ministry of Agriculture did a lot of work. Testing soil to prescribe and apply suitable fertilizers was included in the 16 executed policies for the benefit of peasants by the Ministry of Agriculture in 2007. It was clearly pointed out in the decision of the Ministry of Agriculture: 100 million peasants would be provided with free technology services for testing soil to prescribe and apply suitable fertilizers in 2007, the area coverage of the application of testing soil would be 760 million acreage.

The Directors believe that with the above encouraging policies, rural economy, crops production and peasants income would continue to increase steadily in 2007, which would have a positive impact on the demand for chemical fertilizers.

Forward Objectives and Strategies

Expand Sales Network, Enhance Product Brand

With the increasing productivity, the Group will devote more resources to develop a Ko Yo featured distribution channel, and enhance our brand name and corporate servicing image. In addition to expanding the publicity and promotion strategies, the Group will strengthen management and skills training of our sales persons and agricultural servicing staff, so as to establish a national agricultural servicing network to support the increasing sales and after sales services.

Further Develop Overseas Market, Increase Overseas' Market Share

According to the pledge made by China in joining the World Trade Organization, it will open its wholesale and retail chemical fertilizers market as at 11th December 2006 to the foreign investment. The Group will expand our chemical fertilizers exports, in order to boost our product competitiveness.

Take Advantage of Resources in Western China to Enhance Productivity

According to Dow Jones, Beijing on 28th February 2007 and the official media, Xinhua News Agency, till 2008, if the proved reserves of Puguang Gasfield, the largest natural gasfield in China for the time being, could be doubled, it may be able to alleviate the supply shortage of cleaning energy resources in the forthcoming years. Proved reserves of Puguang Gasfield may reach 500 to 550 billion cubic metres in 2008. Puguang Gasfield is located at Sichuan, China, and was being explored by China Petroleum & Chemical Corporation ("CPCC") in early 2006. CPCC has announced that Puguang Gasfield will commence production in 2008 and expected that its annual production capacity will reach 12 billion cubic metres. It also estimated in December 2006 that proved reserves of Puguang Gasfield will reach 351 to 361 billion cubic metres in late 2006. Directors of the Group believes that exploration and utilization of Puguang Gasfield will effectively lessen the influence of natural gas supply shortage in the coming few years.

In the foreseeable future, energy and productivity will still be our development bottle-neck. Under the circumstances of keen market competition and significant influence of raw materials on industry profit margins, in accordance with the trend of the chemical fertilizers industry of large scale production in regions of energy-oriented, the Directors have made full assessment on the concerned risk and suggested to take advantage of the rich natural gas resources in Sichuan. Allied with other investors, the Group has initiated a project with annual productivity of ammonia compound and urea of approximately 400,000 tonnes and 450,000 tonnes respectively in Dazhou, Sichuan. Meanwhile, preparation work of the project is under smooth progress. The local government has confirmed the required volume of natural gas resources of the Group. The flattening of the site of the plant in Dazhou has been completed about 90% of its construction as at 31st January 2007, and the equipments to be dismantled have completed checking and verification. The Directors expect that implementation of the project will probably bring sustainable growth to our Group's turnover and profits in the coming five years. The Group's productivity of ammonia compound and urea will increase by 286% and 281% respectively.

APPRECIATION

Due to the difficulties and unfavorable factors confronted by the Group in the previous year, the Company fell short of realizing targets set upon by the board of Directors (the "Board"), which could not bring satisfactory returns to the shareholders. I would hence deeply and sincerely express my regret and apology. Nevertheless, I believe those difficulties and obstacles faced by our Group are of short-term. We hope to retain support from our shareholders, and dedicate our utmost to reach a brand new milestone for the Comany in the coming year. The Board, the management and all staff will continue to work diligently to achieve greater success for the Group and to provide shareholders with returns.

Li Weiruo
Chairman

Hong Kong, 28th March 2007

FINANCIAL PERFORMANCE

Results

For the year ended 31st December 2006, the Group remained focused on manufacture and distribution of chemical fertilizers and chemical products, including BB Fertilizers and complex fertilizers, sodium carbonate, urea, ammonium chloride, ammonium bicarbonate and ammonia.

During the year under review, the Group recorded turnover of approximately RMB611 million, a decrease of approximately 2.7% over the previous year. Slight drop in the turnover is mainly contributed to different degrees of deduction in selling price of the Group's products. Compare to last year, selling price of our products decreased approximately 1.7% to 31.4%. Total sales volume of our products slight increase from 471,000 tonnes in 2005 to 472,000 tonnes in 2006. Compare to the same period last year, sales volume of the Group's products increased by approximately 0.2%. The main factor affected the turnover and profit was that the major manufacturing locations of the Group, Sichuan Province and its peripheries, encountered the most severe drought within the past 50 years in 2006. As hydroelectric power is the main resource of Sichuan Province, power supply was reduced by the drought. Moreover, the increase usage of coal and electricity in winter, the Government limited the electricity supply for the use of industry. Another factor was that the two largest natural gas suppliers, China Petroleum & Chemical Corporation and Petro China Company Limited have spent the longest period over the previous five years, on checking and maintenance of the equipment. It caused the shortage of natural gas supply. The above two reasons led to the standstill of machineries of approximately 11,630 machinery hours and reduction of production of ammonium compound of approximately 8,720 tonnes, which negatively affected the annual production and product sales performance. Moreover, the provision on employees' stock option was approximately RMB4 million which further decrease the profit for the year ended 31st December 2006.

The profit attributable to shareholders of the Group amounted to approximately RMB29 million, representing a drop of approximately 39% as compared to last year. The profit before provision of employees' stock option is approximately RMB33 million. Earnings per share amounted to approximately RMB6.0 cents.

Dividends

The Directors proposed a final dividend of HKD0.7 cents per share (2005: HKD1.5 cents per share) for the year ended 31st December 2006. A total of HKD1.2 cents per share were declared for the year ended 31st December 2006 (2005: HKD2.0 cents per share).

Cost and Profit Margin

Cost of sales of the Group amounted to approximately RMB513 million, representing an increase of 3.1% as compared to the figure in 2005. The reasons of increase in cost of sale were increase in unit cost of raw materials.

Gross profit margin of the Group decreased approximately from 20.7% in 2005 to 16.0% in 2006. The overall decrease in gross profit margin was due to the severe drought in Sichuan Province and its peripheries which led to the decrease of selling price.

FINANCIAL PERFORMANCE *(Continued)*

Cost and Profit Margin *(Continued)*

During the year under review, distribution costs decreased approximately by 36% compared with last year as the portion of export increased and the decreased in selling price due to the drought. The distribution costs over sale ratio decreased approximately from 0.055 in 2005 to 0.036 in 2006.

In comparison with last year, there was an increase in administrative expenses of the Group by approximately 6.8% from RMB38.6 million in 2005 to RMB41.3 million in 2006. If exclued the effect of provision on employees' share option, the administrative expenses will be 37.1 million which represented a decrease of approximately 4% as compare to last year.

Starting from the year under review, the Group accrued provision of Enterprise Income Tax amounting to approximately RMB5.7 million. Details of tax schemes are set out in note 23 to consolidated financial statements.

PRODUCTS

BB Fertilizers and Complex Fertilizers

Net sales of BB Fertilizers and complex fertilizers of the Group amounted to approximately RMB250 million, representing a growth of approximately 4% as compared to last year, and accounted for approximately 40.9% of the Group's aggregate net sales.

Sodium Carbonate and Ammonium Chloride

The net sales of sodium carbonate and ammonium chloride amounted to approximately RMB98 million and RMB42 million, which decreased approximately by 6% and 28% respectively as compared to previous year, which accounted for approximately 16.0% and 6.8% of the Group's aggregate net sales respectively.

Urea

The net sales of urea increased by 2% to RMB202 million in 2006 as compared to last year, which accounted for approximately 33.2% of the Group's aggregate net sales.

Ammonia and Ammonium Bicarbonate

The net sales of ammonia decreased approximately by 3.6% to RMB10 million in 2006 as compared to last year, which accounted for 1.7% of the Group's aggregate net sales. The net sales of ammonium bicarbonate decreased by 82% to RMB3 million of sales as compared to last year, which accounted for approximately 0.5% of the Group's aggregate net sales. The reason for the decrease is the shifting of production from ammonium bicarbonate to urea which has higher gross profit margin.

PRODUCTS *(Continued)*

Others

The net sales of other products including foliar fertilizer, highly water soluble fertilizer and others was approximately RMB6 million, which accounted for approximately 0.9% of the Group's aggregate net sales.

Enhance Productivity/Improve Production Facilities

In order to boost the production capability, turnover and profit , the Group had carried out technique reconstruction, equipment renovation and repair projects by existed internal resources.

Completion of the technique reconstruction project of transforming the "little granule urea" production line to "large granule urea" production line in Xin Du District, Chengdu City, Sichuan in April 2006.	The Group invested approximately RMB5 million in this project. The production line will achieve an annual production capacity of 80,000 tonnes. It not only can satisfy the raw material demand of BB Fertilizers of our Group, but also further reduce the production cost.
Constructions of the 300,000-tonne BB Fertilizers production line project in Qingdao City, Shandong Province, China has basically been completed and is awaiting verification for operation.	The project is expected to be verified and commence operation in the first half of 2007. It will enhance production capacity of our Group's BB Fertilizers to 700,000 tonnes, and create favourable conditions for the sustainable growth of our sales and profits.
Implementation of the cyclic catalytic regenerative reforming (CCR) technique reconstruction project of ammonia compound production line in Xin Du District, Sichuan Province in July 2006.	Completed and commenced operation on 1st February 2007. It greatly reduces the usage of electricity and natural gas and enhances the competitive edge in production cost. The technique reconstruction will not only reduce production cost of ammonia compound by approximately RMB12,000,000, but also increase the production capacity of urea by 10,000 tonnes, or sodium carbonate by 10,000 tonnes and ammonium chloride by 12,000 tonnes.

BRAND NAME AND MARKETS

The brand of "Testing Soil for Formulated Fertilization of Ko Yo" (玖源測方) of our Group has been selected by China Co-operation Times, China Agricultural Means of Production Magazine (《中國農資》雜志社) and China National Agricultural Means of Production Circulation Association as "The Most Valuable Brand in the Chinese Agriculture Industry 2006" in October 2006.

After spending nearly half year on internet voting and election by the assessment committee, "Testing Soil for Formulated Fertilization of Ko Yo BB Fertilizers 玖源測方 BB 肥)" of Chengdu Ko Yo Compound Fertilizer Co., Limited ("Chengdu Ko Yo Compound") was awarded the "Top Ten Influential Brand in China's Compound Fertilizer Industry" at the "Third Annual China Influential Brands Forum", which was held in Beijing's Great Hall of the People on 31st January 2007.

Following the "First Forum on the Development of BB Fertilizers Industry" successfully co-organized by the Group in 2005, we have organized the "Second Forum on the Development of BB Fertilizers Industry" with China Co-operation Times in Beijing on 7th July 2006. Leaders of the concerned government departments including National Development and Reform Committee, All China Federation of Supply and Marketing Cooperatives, Ministry for Agriculture, General Administration of Quality Supervision, Inspection and Quarantine of the China, State Administration For Industry & Commerce, China Phosphate Fertilizer Industry Association etc., professionals and scholars, as well as major manufacturers of BB Fertilizers in China, representatives of BB Fertilizers suppliers, corporate representatives of BB Fertilizers manufacturers, have attended the forum."To take responsibility at the same fertile field" was the theme of the forum, which mainly study and forecast the development, scientific formula, operation mode and market prospect of BB Fertilizers in China.

In order to strengthen the cooperative relationship between the agricultural departments of different local governments, and proactively carry out the soil testing prescription project and establish formula fertilizers demonstrative area, the Group has formally launched "Testing Soil for Formulated Fertilization Action of Ko Yo, Zeng Xiang Hua" (曾祥華 • 玖源測土配方施肥行動) in August 2006. The campaign signifies the beginning of exploration on soil testing for prescription and application of suitable fertilizers, through cooperation with advanced peasants.

RESEARCH AND DEVELOPMENT

In order to diversify its product mix to lower market risk, the Group has been undergoing the preliminary market research on a number of products including foliar fertilizer, fertilizer with high water solubility and high/medium/low concentration (25-50%) complex fertilizers.

During the year under review, our Group has been appointed to manufacture and trial sale of foliar fertilizer and highly water soluble fertilizer of 18 tonnes and 144 tonnes respectively, in order to have further product mix optimization of BB Fertilizers. Trial sales volume and sales amount of complex fertilizers reached approximately 29,715 tonnes and RMB46,125,600 respectively. Markets of the new products were well received.

AWARDS & RECOGNITIONS

Chengdu Ko Yo Chemical Industry Company Limited ("Chengdu Ko Yo Chemical") was awarded one of "15 Advanced Organizations in Sichuan Province Petroleum Industry" by Sichuan Province Economy Committee.

Moreover, the brand of "Testing Soil for Formulated Fertilization of Ko Yo" (玖源測方) of the Chengdu Ko Yo Compound has been selected by China Co-operation Times, China Agricultural Means of Production Magazine (《中國農資》雜志社) and China National Agricultural Means of Production Circulation Association as "The Most Valuable Brand in the Chinese Agriculture Industry 2006" in October 2006.

To echo Premier Wen Jiabao's appeal of "Rapid Development of National Brand", People's Daily (Market Post), China United Business, Purchasing Newspaper Office (購物導報社), Brand Magazine, China International Brand Academy, World First Research Centre, International Cooperation Promoting Center (China Office), etc., jointly hosted the community activity of the "Third (2006) China Top Ten Influential Brands". Further, on 31st January 2007, the "Third Annual China Influential Brands Forum" was held in Beijing's Great Hall of the People. After spending nearly half year on internet voting and election by the assessment committee, "Testing Soil for Formulated Fertilization of Ko Yo BB Fertilizers (玖源測方BB肥)" of Chengdu Ko Yo Compound was awarded the "Top Ten Influential Brand in China Compound Fertilizer Industry". Mr. Li Weiruo, Executive President of Chengdu Ko Yo Compound was selected as the "Top Ten Outstanding Entrepreneurs in China's Brand Building".

LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE

As at 31st December 2006, the Group had net current liabilities of approximately RMB52,033,000. Current assets as at 31st December 2006 comprised cash and bank deposits of approximately RMB12,839,000, pledged bank deposits of approximately RMB20,801,000, inventories of approximately RMB76,804,000, trade receivables of approximately RMB13,961,000 and prepayments and other current assets of approximately RMB50,417,000. Current liabilities as at 31st December 2006 comprised short-term bank loans of approximately RMB134,276,000, trade and notes payables of approximately RMB42,450,000, deposits from customers of approximately RMB29,582,000 and accrued charges and other payables of approximately 20,547,000. Details of the Group's adoption of going concern basis in preparing the consolidated financial statements is set out in note 2.1 to the consolidated financial statements.

CAPITAL COMMITMENTS

As at 31st December 2006, the Group had outstanding capital commitments of approximately RMB264,478,000. Details of the Group's capital commitments and its plan of financing such capital commitments are set out in note 30 and note 32, respectively, to the consolidated financial statements.

FINANCIAL RESOURCES

As at 31st December 2006, the Group had cash and bank deposits of approximately RMB12,839,000 and pledged bank deposits of approximately RMB20,801,000. The Company intends to finance the Group's future operations, capital expenditure and other capital requirements with the existing bank balances.

As at 31st December 2006, the total bank loans and notes payable balances of the Group amounted to RMB146,276,000.

GEARING RATIO

The Group's gearing ratios were approximately 44.1% and 58.5% as at 31st December 2006 and 31st December 2005 respectively. The gearing ratios were calculated based on total liabilities over total assets as at the respective balance sheet dates.

CONTINGENT LIABILITIES

The Group had no significant contingent liabilities as at 31st December 2006.

MATERIAL ACQUISITION/DISPOSAL

Other than the major transaction on the acquisition of production facilities as per announcement dated 5th October 2006 and as disclosed in note 32 to the consolidated financial statements, there was no other material acquisition in the year 2006 which would have been required to be disclosed under the Rules Governing the Listing of Securities on Growth Enterprise Market of the Stock Exchange ("GEM Listing Rules").

SEGMENTAL INFORMATION

The Group activities are primarily conducted in the PRC. In the year under review the total sales of export was approximately RMB51,745,000, which represents 8.5% of the total sales.

DETAILS OF FUTURE PLANS FOR MATERIAL INVESTMENT OR CAPITAL ASSETS

The Directors do not have any future plans for material investment or capital assets.

EXPOSURE ON EXCHANGE RATE FLUCTUATION

Since most of the income and expenditure of the Group were received and paid in RMB, the local currency of the place where the Group primarily operates in, the Directors do not consider that the Group was significantly exposed to any foreign currency exchange risk.

CHARGES ON THE GROUP'S ASSETS

As at 31st December 2006, certain land use rights and buildings with a total net book value of approximately RMB83,390,000 (2005: RMB85,537,000), plant and machinery with a total net book value of approximately RMB24,296,000 (2005: RMB25,092,000) and bank deposits approximately RMB20,801,000 (2005: RMB77,800,000) were pledged as collateral for the Group's bank loans and notes payable.

DIVIDEND

The Directors recommend the payment of a final dividend of HKD0.7 cents per share to the shareholders whose names appear on the register of members of the Company as at the close of business on 26th April 2007. The dividend will be payable on 24th May 2007. The register of members of the Company will be closed from 23rd April 2007 to 26th April 2007, both days inclusive, during which period no share transfer shall be effected. In order to qualify for the final dividend, all instruments of transfers accompanied by the relevant share certificates must be lodged with the Company's share registrar, Union Registrars Limited, Room 1803, Fook Lee Commercial Centre, Town Place, 33 Lockhart Road, Wanchai, Hong Kong for registration by no later than 4:00 p.m. on 20th April 2007.

NUMBER OF EMPLOYEES

As at 31st December 2006, the Group had 1,822 (2005: 2,016) employees, comprising 6 (2005: 6) in management, 168 (2005: 115) in finance and administration, 1,555 (2005: 1,779) in production, 87 (2005: 107) in sales and marketing and 6 (2005: 9) in research and development. 1,816 (2005: 2,010) of these employees were located in the PRC and 6 (2005: 6) were located in Hong Kong.

Pension schemes of the Group are set out in note 2.14(b) to consolidated financial statements.

EXECUTIVE DIRECTORS

Mr. Li Weiruo, aged 53, is the Chairman of the Board, Executive President and the founder of the Group. He graduated from Sichuan Institute of Finance and Economics with a certificate in economics in 1985. Mr. Li has over 20 years' experience in corporate management in the PRC. He was awarded a certificate for "Chief Economists of Large-to-Medium Sized Enterprises in the PRC" after completing "The Study Course for Chief Economists of Large-to-Medium Sized Enterprises" commissioned by the State Economics Commission at the Southwest University of Finance and Economics in 1986. He is one of the authors of "Modern Corporate Management" which was published by the Sichuan Education Publisher. Mr. Li was the former Vice-director of China Nonferrous Metal Corporation in Chengdu. Mr. Li moved to Hong Kong in 1994 and became a permanent resident of Hong Kong in 2001. He was appointed as an invited member of the Chinese People's Political Consultative Conference of Sichuan Province in 2003. Mr. Li is responsible for the overall management, strategic planning and business development of the Group.

Mr. Yuan Bai, aged 48, is the Executive Vice President of the Group. Mr. Yuan is responsible for the cost management and general operations and research and development of the Group. Mr. Yuan graduated from Northeast Institute of Technology with a bachelor degree in engineering in 1982 and obtained a certificate as Senior Engineer in 1992. Mr. Yuan studied economy management in Qinghua University from September 1995 to March 1996. Prior to joining the Group in August 1999, Mr. Yuan was the Deputy General Manager of Chongqing Sanjiu Industrial Co., Ltd., which focused on the manufacture and trading of non-ferrous metal. Mr. Yuan was elected as a people's delegate of the first session of the People's Congress of Chongqing in 1997.

Ms. Chi Chuan, aged 51, is the Compliance Officer and Executive Vice President of the Group. She graduated from Sichuan Normal College with a bachelor degree in science in 1982. Ms. Chi has over 10 years' experience in finance and accounting. Prior to joining the Group in July 1999, Ms. Chi was the finance manager of Leshan Economic and Trade General Company, a trading company in the PRC. Ms. Chi is primarily responsible for the financial management and general operations of the Group since she joined the Group in July 1999.

Ms. Man Au Vivian, aged 43, is responsible for business development and investment activities of the Group. Ms. Man graduated from the University of International Business and Economics with a bachelor degree in economics in 1986. Ms. Man has over 15 years' experience in international trade. She formerly worked for China National Light Industrial Products Import and Export Corporation of MOFTEC. She joined the Group in January 1997.

Mr. Li Shengdi, aged 54, is a director of Chengdu Ko Yo Chemical and Chengdu Ko Yo Compound respectively. He graduated from Chinese Communist Party School with a degree majoring economics and was entitled as an economist. Prior to joining the Group, he was the deputy manager of China Nonferrous Huludao Zinc Corporation, from 1983 to 1993, general manager of Hainan Hui Yuantang Medicine Co., Ltd. from 1996 to 1999 and general manager of Shanghai Haos Water Rectified Co., Ltd., a Sino-US joint venture from 2000 to 2002. Mr. Li joined the Group in October 2002 and was appointed as a Director of the Company on 29th April 2004. He is currently responsible for the administration and production operations of the Group.

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Hu Xiaoping, aged 56, is an independent non-executive director. He obtained a bachelor degree in Economics from Sichuan Institute of Finance and Economics in 1982 and a master degree in Economics from Southwest University of Finance and Economics in 1987. Mr. Hu is currently the head of the Economics Research Centre of the Southwest University of Finance and Economics. Mr. Hu has been involved in various research projects at both the provincial and state level and has published numerous articles in financial and economics publications in the PRC. He was appointed as an independent non-executive director in June 2003.

Mr. Woo Che-wor, Alex, aged 54, is an independent non-executive director. Mr. Woo has been the Chairman and Chief Executive Director of STI Certified Products Inc., a private company in California, U.S.A. since February 1988. From January 1976 to December 1988, Mr. Woo was the corporate treasurer of Fairchild Semiconductor Corporation, a multi-national semiconductor company with its headquarters in California, U.S.A.. Mr. Woo is qualified as Certified Management Accountant from Chartered Institute of Management Accountants of England and obtained an M.B.A. from San Jose State University of the U.S.A. in 1987. He was appointed as an independent non-executive director in June 2003.

Mr. Qian Laizhong, aged 64, is an independent non-executive director. Mr. Qian graduated from Sichuan Fine Arts Institute in 1968. Over the past 20 years, Mr. Qian actively participated in cultural and economical researches and publishes in Sichuan province, the PRC. Currently, Mr. Qian is a member of Sichuan Provincial Committee of Chinese Peoples Political Consultative Conference. He was appointed as an independent non-executive director on 16th August 2004.

SENIOR MANAGEMENT

Mr. Zhu Changhou, aged 68, is the deputy general manager and chief engineer of Chengdu Ko Yo Chemical. He obtained a certificate of chemistry in Luzhou Chemical College and has over 18 years' experience in developing and analyzing chemical products. Mr. Zhu is also a director of Sichuan Chemical Association and the PRC Chemical Association. Prior to joining the Group, Mr. Zhu was the deputy chief engineer of Luzhou Natural Gas Chemical Corporation, which focused on the manufacture of chemical products. Mr. Zhu is primarily responsible for Chengdu Ko Yo Chemical's production and product research and development. He joined the Group in 1999.

Mr. Mai Zixun, aged 59, is the general manager of Chengdu Ko Yo Compound. He graduated from Sichuan Broadcasting and Television University. Mr. Mai was formerly the General Manager of Zhuhai Gree Magneto-Electronic Co., Ltd., which focused on the manufacture of electronics products. He joined the Group in June 2001 and is responsible for the sales and marketing activities of Chengdu Ko Yo Compound.

Mr. Chung Tin Ming, aged 36, is the financial controller of the Group and is responsible for financial management of the Group. He graduated from Chinese University of Hong Kong with a bachelor degree in science and City University of Hong Kong with a master degree in financial engineering. He is an associate member of each of the Hong Kong Institute of Certified Public Accountants and Association of Chartered Certified Accountants. Prior to joining the Group in January 2006, he was a director of Keen Ocean Industrial Limited in Hong Kong.

The Directors have the pleasure of presenting their report together with the audited financial statements of the Company and its subsidiaries for the year ended 31st December 2006.

GENERAL INFORMATION

The Company was incorporated in the Cayman Islands on 11th February 2002 as an exempted company with limited liability under the Companies Law Cap. 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands.

The Group reorganized its structure on 10th June 2003 in preparation for the listing of the Company's shares on Growth Enterprise Market ("GEM") of the Stock Exchange of Hong Kong. The Company became the holding company of the companies now comprising the Group. Details of the reorganization are set out in the prospectus of the Company dated 30th June 2003. The shares of the Company were listed on GEM of the Stock Exchange on 10th July 2003.

PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding. Its subsidiaries are principally engaged in the research and development, manufacture, marketing and distribution of chemical products, chemical fertilizers and BB Fertilizers.

RESULTS AND APPROPRIATIONS

Details of the Group's profits for the year ended 31st December 2006 are set out in the consolidated income statement.

The Directors recommend the payment of a final dividend of HKD0.7 cents per share, totalling approximately RMB3,541,000 for the year ended 31st December 2006 (2005: RMB6,580,000).

SHARE CAPITAL

Details of movements in share capital of the Company are set out in note 15(a) to the consolidated financial statements.

RESERVES

Movements in the reserves of the Group and of the Company during the year are set out in note 16 to the consolidated financial statements.

DISTRIBUTABLE RESERVES

Distributable reserves of the Company as at 31st December 2006 amounted to approximately RMB114,975,000 (2005: RMB66,034,000).

RIGHTS OF DIRECTORS AND EMPLOYEES TO ACQUIRE SHARES OR DEBENTURES

On 10th June 2003, the Company adopted a share option scheme and amended at an extraordinary general meeting on 28th July 2004 (the "Share Option Scheme"). A summary of the principle terms and conditions of the Share Option Scheme is set out under the section headed "Share Option Scheme" in Appendix IV of the prospectus of the Company dated 30th June 2003. The amendments of the Share Option Scheme are explained in the announcement and circular of the Company dated 12th July 2004.

PRE-EMPTIVE RIGHTS

There is no provision for pre-emptive rights under the Company's articles of association and there is no restriction against such rights under the Company Law (Law 3 of 1961, as consolidated and revised) of the Cayman Islands, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

FIVE YEAR FINANCIAL SUMMARY

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out in page 85.

PROPERTY, PLANT AND EQUIPMENT

Details of movements in fixed assets of the Group during the year are set out in note 6 to the consolidated financial statements.

DIRECTORS AND DIRECTORS' SERVICE CONTRACTS

The Directors who held office during the year ended 31st December 2006 and up to the date of this report are:

Executive directors

Mr. Li Weiruo
Mr. Yuan Bai
Ms. Chi Chuan
Ms. Man Au Vivian
Mr. Li Shengdi

Independent non-executive directors

Mr. Hu Xiaoping
Mr. Woo Che-wor, Alex
Mr. Qian Laizhong

DIRECTORS AND DIRECTORS' SERVICE CONTRACTS *(Continued)*

In accordance with Article 87 of the articles of association of the Company, at each annual general meeting, one-third of directors for the time being shall retire from office by rotation and, will be eligible for re-election. Chairman of the Board will not be subject to retirement by rotation. As Ms. Chi Chuan and Ms. Man Au Vivian have been longest in office, Ms. Chi Chuan and Ms. Man Au Vivian will retire by rotation and, being eligible, will offer themselves for re-election at the forthcoming annual general meeting.

Each of the executive directors has entered into a service contract with the Company for initial fixed term of three years, and will continue thereafter for successive terms of one year until terminated by not less than three months' notice in writing served by either party on the other. Each of the executive directors is entitled to a basic salary and director's fee subject to an annual review by the Board. In addition, the executive directors are also entitled to a discretionary bonus, which may not exceed 3% of the audited consolidated net profit of the Group attributable to shareholders in respect of that financial year of the Company. The percentage rate of discretionary bonus is subject to annual review by the Board.

The independent non-executive directors of the Company are appointed with specific terms inside the letter of appointment for initial fixed terms of two years.

None of the directors who are proposed for re-election at the forthcoming annual general meeting has a service contract with the company which is not determinable within one year without payment of compensation, other than statutory compensation.

SHARE OPTIONS

Share options are granted to directors, employees and consultants of the Company or its subsidiaries under the Share Option Scheme approved by written resolutions of shareholders of the Company on 10th June 2003 and amended at an extraordinary general meeting on 28th July 2004. The purpose of the Share Option Scheme is to recognize the contribution of employees and consultants to the Company and its subsidiaries, and to provide a performance related incentive to them. Currently under the Share Option Scheme the maximum number of shares which may fall to be issued pursuant to the exercise of all the share options granted and to be granted is 42,000,000 shares, representing 10% of the total number of issued shares upon listing on 10th July 2003. Unless approved by shareholders, the total number of shares issued and which may fall to be issued upon the exercise of the options granted to each participant may not exceed 4,200,000, such options being exercisable for 10 years from the date of grant of such option. Participants are required to pay an option price of HKD10 for each acceptance of option offer. The subscription price shall be at least the highest of (i) the closing price of a share on the option offer date, (ii) the average closing price of a share for the five business days immediately preceding the option offer date and (iii) the nominal value of a share. The Share Option Scheme will remain valid for a period of ten years commencing from 10th June 2003.

SHARE OPTIONS *(Continued)*

Under the Share Option Scheme, no share options were exercised or cancelled, 11,740,000 share options were granted and 800,000 share options were lapsed during the year ended 31st December 2006. The details of option outstanding and movements are disclosed in the following table:

	Number of options							Number of options	
	Held at 1 January 2006	Grant during period	Exercised during period	Lapsed during period	Held at 31 December 2006	Grant date	Exercise price HK$	Exercisable from grant date until 22 September 2013	Exercisable from grant date until 10 April 2016
Directors									
Li Weiruo	—	420,000	—	—	420,000	16 May 2006	0.75	—	420,000
Yuen Bai	—	400,000	—	—	400,000	16 May 2006	0.75	—	400,000
Chi Chuan	4,200,000	—	—	—	4,200,000	23 September 2003	0.62	4,200,000	—
Man Au Vivian	3,800,000	—	—	—	3,800,000	23 September 2003	0.62	3,800,000	—
Li Shengdi	4,200,000	—	—	—	4,200,000	23 September 2003	0.62	4,200,000	—
Hu Xiaoping	400,000	—	—	—	400,000	23 September 2003	0.62	400,000	—
Woo Che-wor Alex	400,000	—	—	—	400,000	23 September 2003	0.62	400,000	—
Qian Laizhong	—	420,000	—	—	420,000	16 May 2006	0.75		420,000
Employees	12,200,000	—	—	800,000	11,400,000	23 September 2003	0.62	11,400,000	
		10,500,000	—	—	10,500,000	11 April 2006	0.75		10,500,000
Total	25,200,000	11,740,000	—	800,000	36,140,000			24,400,000	11,740,000

The weighted average fair value of 11,740,000 option, granted during the year determined using the Black-Scholes valuation was HKD0.36 (RMB0.36) per option and the total fair value of those options was HKD4,188,000 (RMB4,188,000), which was recognised as administrative expenses and a corresponding increase in reserve. The parameters input into the model were the share prices at the grant date, the volatility of the share price return, expected life of options, expected dividend paid out rate and annual risk-free interest rate. The fair values calculated are inherently subjective and uncertain due to the assumptions made and the limitations of the model used. The value of an option varies with different variables of certain subjective assumptions. Any change in variables so adopted may materially affect the estimation of the fair value of an option.

DIRECTORS' INTERESTS IN SHARES

As at 31st December 2006, the interests and short positions of the Directors and chief executives in the shares, underlying shares or debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")), which are required (a) to be 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 are taken or deemed to have under such provisions of the SFO); or (b) to be recorded in the register required to be kept under section 352 of the SFO; or (c) to be notified to the Company and the Stock Exchange pursuant to the minimum standards of dealings by directors referred to in Rule 5.46 of the GEM Listing Rules were as follows:

(i) Long positions in the shares and the underlying shares of the Company

Directors	Personal long position in shares (beneficial owner)	Personal long position in share options (beneficial owner)	Aggregate long position in shares and underlying shares	Total interests in the issued share capital
Li Weiruo	206,440,000	420,000	206,860,000	40.90%
Yuan Bai	35,448,000	400,000	35,848,000	7.09%
Chi Chuan	12,528,000	4,200,000	16,728,000	3.31%
Man Au Vivian	6,264,000	3,800,000	10,064,000	1.99%
Li Shengdi	—	4,200,000	4,200,000	0.83%
Hu Xiaoping	—	400,000	400,000	0.08%
Woo Che-wor, Alex	—	400,000	400,000	0.08%
Qian Laizhong	—	420,000	420,000	0.08%

(ii) Interests in shares of an associated corporation of the Company

Name of Director	Name of company	Number of non-voting deferred shares	Capacity	Type of interest	Approximate interests in holding
Li Weiruo	Ko Yo Hong Kong	2,100,000	Beneficial Owner	Personal	70%
Yuan Bai	Ko Yo Hong Kong	420,000	Beneficial Owner	Personal	14%
Chi Chuan	Ko Yo Hong Kong	120,000	Beneficial Owner	Personal	4%
Man Au Vivian	Ko Yo Hong Kong	60,000	Beneficial Owner	Personal	2%

Note: a wholly-owned subsidiary of the Company

DIRECTORS' INTERESTS IN SHARES *(Continued)*

(iii) Short positions in the shares of an associated corporation of the Company

Name of Director	Name of company	Number of non-voting deferred shares	Capacity	Type of interest	Approximate interests in holding of such class
Li Weiruo	Ko Yo Hong Kong	2,100,000	Beneficial Owner	Personal	70%
Yuan Bai	Ko Yo Hong Kong	420,000	Beneficial Owner	Personal	14%
Chi Chuan	Ko Yo Hong Kong	120,000	Beneficial Owner	Personal	4%
Man Au Vivian	Ko Yo Hong Kong	60,000	Beneficial Owner	Personal	2%

SUBSTANTIAL SHAREHOLDERS

As at 31st December 2006, there was no substantial shareholder (not being a director or a chief executive of the Company) who had any interests or short positions in the shares or underlying shares of the Company which are required to be notified to the Company and the Stock Exchange under Divisions 2 and 3 of Part XV of the SFO and recorded in the register required to be kept under section 336 of the SFO, and who were directly or indirectly deemed to be interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of the Company.

INTEREST OF OTHER PERSONS IN THE COMPANY

(i) Long positions in the shares of the Company

As at 31st December 2006, so far as is known to any Director or chief executive of the Company, the following person had an interest or short positions in the shares or underlying shares of the Company which are required to be notified to the Company and the Stock Exchange under Divisions 2 and 3 of Part XV of the SFO and recorded in the register required to be kept under section 336 of the SFO, and who were directly or indirectly 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 the Company.

Name	Capacity	Number of shares	Interests in issued share capital of the Company
Fidelity International Limited	Beneficial Owner	34,055,000	6.73%

Save as disclosed above, as at 31st December 2006, the Directors are not aware of any other person (other than the Directors and chief executives of the Company) who had interests or short positions in the shares or underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO.

INTEREST OF OTHER PERSONS IN THE COMPANY *(Continued)*

(ii) Long position in the underlying shares of the Company

No long positions of other persons in the underlying shares of equity derivatives of the Company were recorded in the register

(iii) Interests in shares of an associated corporation of the Company

Name	Name of company	Number and description of shares	Capacity	Type of interest	Approximate percentage of holding
Tang Shiguo *(Note)*	Ko Yo Hong Kong	300,000 non-voting deferred shares	Beneficial owner	Personal	10

Note: Mr. Tang Shiguo ceased to be a director of the Company with effect from 29th April 2004.

(iv) Short positions in the shares of an associated corporation of the Company

Name	Capacity	Name of company	Number and description of shares
Tang Shiguo	Beneficial owner	Ko Yo Hong Kong	300,000 non-voting deferred shares

SUFFICIENCY OF PUBLIC FLOAT

Based on the public information available to the and within the knowledge of the Directors, it is confirmed that there is sufficient public float of more than 25% of the Company's issued shares at 27th March 2007.

DIRECTORS' INTEREST IN COMPETING BUSINESS

None of the Directors or the management shareholders of the Company and their respective associates (as defined under the GEM Listing Rules) had any interest in a business which competes or may compete, directly or indirectly with the business of the Company during the year under review.

DIRECTORS' INTERESTS IN CONTRACTS

No contract of significance in relation to the Group's business to which the Company or its subsidiaries was a party and in which any of the Company's Directors or members of its management had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

MANAGEMENT CONTRACTS

No contract 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 year.

AUDIT COMMITTEE

The Company established an audit committee on 10th June 2003 with written terms of reference pursuant to the GEM Listing Rules. The primary duties of the audit committee are to review and supervise the financial reporting process and internal control system of the Company and provide advice and comments to the Directors. The audit committee has three members comprising the three independent non-executive directors, namely, Mr. Hu Xiaoping, Mr. Woo Che-wor, Alex and Mr. Qian Laizhong.

The audit committee has reviewed with management the accounting principles and practices adopted by the Company and the Group and discussed internal controls and financial reporting matters including a review of the audited financial statements of the Company and the Group for the year ended 31st December 2006.

PURCHASE, SALE OR REDEMPTION OF SHARES

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed shares during the year under review.

SHARE PLACING

On 3rd May 2006, 84,000,000 existing ordinary shares of HKD0.10 each in the share capital of the Company (the "Shares") were placed at HKD0.78 per share (the "Placing Price") through the share placement (the "Share Placement") and on 17th May 2006, the Company issued 84,000,000 new Shares with the aggregate nominal value of HKD8,400,000 (the "New Shares"). The placees were professional, institutional and private investors who were independent of and not connected with the directors, chief executive, management shareholders or substantial shareholders of the Company or any of its subsidiaries. The Placing Price represent a discount of approximately 1.27% to the closing price of HKD0.79 per Share as quoted on the Stock Exchange on 3rd May 2006. The New Shares represented approximately 19.9% of the issued Shares prior to the Share Placement. A net proceed of approximately HKD63.8 million in aggregate after expenses and commissions was received and the net price for New Shares was approximately HKD0.76. Such proceeds was applied to the acquisition of production facilities with annual production capacity of 400,000 tonnes of ammonia compound and 450,000 tonnes of urea as per announcement dated 5th October 2006.

CUSTOMERS AND SUPPLIERS

For the year ended 31st December 2006, the five largest customers accounted for approximately 14.8% of the Group's total turnover and the five largest suppliers of the Group accounted for approximately 43.2% of the Group's total purchases. The largest customer of the Group accounted for approximately 3.9% of the Group's total turnover and the largest supplier accounted for approximately 13.8% of the Group's total purchases.

None of the Directors, their associates, or any shareholders (which, to the knowledge of the Directors, owned more than 5% of the Company's share capital) had a beneficial interest in the Group's five largest customers and suppliers.

SUBSEQUENT EVENTS

Details of subsequent events of the Company are set out in note 33 to the consolidated financial statement.

CORPORATE GOVERNANCE

A report on the corporate governance practices adopted by the Company is set out on pages 26 to 30 of the annual report.

AUDITORS

The financial statements have been audited by PricewaterhouseCoopers who shall retire and, being eligible, will offer themselves for re-appointment at the forthcoming annual general meeting.

On behalf of the Board,

Li Weiruo
Chairman

28th March 2007

CORPORATE GOVERNANCE PRACTICES

The Board of directors believes that by adopting high standard of corporate governance practices can improve the transparency and accountability of the Company, and instill confidence of shareholders and the public in the Group. The board had adopted the Code on Corporate Governance Practices (the "Code") as set out in Appendix 15 of the GEM Listing Rules since 1st January 2005. Throughout the year under review, save as disclosed in page 27 with heading of the Chairman and Chief Executive Officer, the Company had complied with the Code.

THE BOARD OF DIRECTORS

Board Composition

The Board of directors currently comprises eight directors of which five are executive directors and three are independent non-executive directors. The detail is as follow:

Executive directors

Mr. Li Weiruo (Chairman)
Mr. Yuan Bai
Ms. Chi Chuan
Ms. Man Au Vivian
Mr. Li Shengdi

Independent non-executive directors

Mr. Hu Xiaoping
Mr. Woo Che-wor, Alex
Mr. Qian Laizhong

The independent non-executive directors represent over one-third of the Board. Among the three independent non-executive directors, at least one has appropriate professional qualifications or accounting or related financial management expertise which satisfies the requirement under the rule 5.05(1) and (2) of the GEM Listing Rules. An annual confirmation of the independence of each independent non-executive director had been received in accordance with each and every guideline set out in rule 5.09 of the GEM Listing Rules. No independent non-executive director has served the Group for more than nine years. All independent non-executive directors are identified as such in all corporate communications that disclose the names of the directors. There is no family or other material relationship among members of the Board.

The Board is responsible for the strategic development of the Group's business. Daily operations and execution of strategic plans are delegated to management. The Audit Committee, Remuneration Committee and the Nomination Committee have specific terms of reference clearly defining the powers and responsibilities of the respective committees. All committees are required to report to the Board in relation to their decisions and recommendations for seeking the Board's approval.

THE BOARD OF DIRECTORS *(Continued)*

Board Meeting

The Board meets regularly and board meetings are held at least four times a year. The board meetings involved the active participation in persons or through other electronic means of communication. At least 14 days notice of all board meetings were given to all directors to ensure all directors, who were given an opportunity to attend and include matters in the agenda for discussion. Agenda and accompanying board papers are sent to all directors at least one day prior to the meeting. Draft and final versions of minutes of board meetings were sent within a reasonable time to all directors for comment and record. All the committee meetings follow the applicable practices and procedures used in board meetings.

In the financial year ended 31st December 2006, eight board meetings were held and the attendance record for the meetings by each director is as follow:

Attendants	Number of meetings attended/Total	Attendance percentage
Executive Directors		
Mr. Li Weiruo	8/8	100%
Mr. Yuan Bai	8/8	100%
Ms. Chi Chuan	8/8	100%
Ms. Man Au Vivian	8/8	100%
Mr. Li Shengdi	8/8	100%
Independent Non-Executive Directors		
Mr. Hu Xiaoping	7/8	87.5%
Mr. Woo Che-wor, Alex	7/8	87.5%
Mr. Qian Laizhong	7/8	87.5%

Chairman and Chief Executive Officer

The Chairman and Chief Executive Officer of the Group is Mr. Li Weiruo. This structure is not complied with the Code. The Chairman of the Group is primarily responsible for the management of the Board and ensuring the Board functions effectively, smoothly and following a good corporate governance practices. Mr. Li Weiruo, the Chairman and Chief Executive Officer of the Group together with the other four executive directors are responsible for monitoring the day to day operation of the Group. Segregation of duties is among the executive directors and each executive director has specific area to focus on. Mr. Li Weiruo and Mr. Yuen Bai are responsible for the development and marketing of the Group. Mr. Li Shengdi is responsible for the operational and human resources matters of the Group. Ms. Chi Chuan is responsible for the financial matters of the Group. Ms. Man Au Vivian is responsible for the affairs and administration of the office in Hong Kong. The Board believes that the segregation of duties among the chairman and executive directors is a sufficient safeguard procedure of the Group before the role of Chairman and Chief Executive Officer are performed by different individuals.

DIRECTORS' SECURITIES TRANSACTION

The Group adopted a code of conduct of regarding directors' securities transactions as the required standard of dealings set out in rules 5.48 to 5.67 of the GEM Listing Rules. Specific enquiry had been made to all directors and each director confirmed that during the year under review, he had fully complied with the required standard of the dealings and there was no event of non-compliance with the required standard of dealings.

REMUNERATION OF DIRECTORS

Remuneration Committee was established in January 2005 and one meeting was held during the financial year under review. The members of the committee and the attendance record are as follow:

Attendants	**Number of meetings attended/Total**	**Attendance percentage**
Independent Non-Executive Directors		
Mr. Hu Xiaoping (Chairman)	1/1	100%
Mr. Qian Laizhong	1/1	100%
Executive Directors		
Ms. Chi Chuan	1/1	100%

The majority of the members of the remuneration committee are independent non-executive directors.

The Remuneration Committee is responsible for the reviewing and recommending the Board for the remuneration policy of the directors and assessing performance of executive directors. The remuneration terms and policies recommended by the Remuneration Committee were reported to the Board for approval. The Remuneration Committee is provided with sufficient resources for discharging its duties.

NOMINATION OF DIRECTORS

Nomination Committee was established in January 2005 and one meeting was held during the financial year under review. The members of the committee and the attendance record are as follow:

Attendants	**Number of meetings attended/Total**	**Attendance percentage**
Independent Non-Executive Directors		
Mr. Qian Laizhong (Chairman)	1/1	100%
Mr. Woo Che-wor, Alex	1/1	100%
Executive Directors		
Mr. Li Shengdi	1/1	100%

NOMINATION OF DIRECTORS *(Continued)*

The majority of the members of the Nomination Committee are independent non-executive directors.

The Nomination Committee is responsible for the formulating the nomination policy of the directors and recommending the Board on nomination and appointment of directors. The Nomination Committee is provided with sufficient resources for discharging its duties.

TERM OF APPOINTMENT AND RE-ELECTION

Each of the executive directors has entered into a service contract with the Company for initial fixed term of three years, and will continue thereafter for successive terms of three year until terminated by not less than three months' notice in writing served by either party on the other. The independent non-executive directors of the Company are appointed with specific terms inside the letter of appointment for initial fixed terms of two years.

In accordance with Article 87 of the articles of association of the Company, at each annual general meeting, one-third of directors for the time being shall retire from office by rotation and, will be eligible for re-election. Chairman of the Board will not be subject to retirement by rotation. Ms. Chi Chuan and Ms. Man Au Vivian will retire by rotation and, being eligible, will offer themselves for re-election at the forthcoming annual general meeting.

AUDIT COMMITTEE

Audit Committee was established in June 2003 with written terms of reference compliance with Rule 5.28 of the GEM Listing Rules and five meetings were held during the financial year under review. The members of the committee and the attendance record are as follow:

Attendants	**Number of meetings attended/Total**	**Attendance percentage**
Independent Non-Executive Directors		
Mr. Hu Xiaoping (Chairman)	5/5	100%
Mr. Qian Laizhong	5/5	100%
Mr. Woo Che-wor, Alex	5/5	100%

The members of the Audit Committee are independent non-executive directors. No former partner of the Company's existing auditing firm acted as a member of the Audit Committee within one year on the date of his ceasing to be a partner or had any financial interests in the auditing firm.

The Board and the Audit Committee had reviewed the remuneration, independence and scope of work of the external auditors. There was no disagreement between the Board and the Audit Committee on the selection, appointment, resignation or dismissal of the external auditors.

AUDIT COMMITTEE *(Continued)*

The Audit Committee is responsible for reviewing the accounting principles and practices adopted by the Group, recommending the Board on the Group's internal control and risk management system, and ensuring the Group's financial statements present a true and fair view of the Group's financial position. The Audit Committee had reviewed with management the accounting principles and practices and discussed internal controls and financial reporting matters including a review of the audited financial statements of the Company and Group for the year ended 31st December 2006.

The Audit Committee is provided with sufficient resources for discharging its duties.

INTERNAL CONTROL

The internal audit department of the Company is responsible for the financial control and operational control of the Group. The Board from time to time reviewed the effectiveness of the Group's internal control system and an external accounting firm had been appointed for reviewing and giving recommendations on the Group's internal control system during the year under review.

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TO THE SHAREHOLDERS OF KO YO ECOLOGICAL AGROTECH (GROUP) LIMITED

(Incorporated in Cayman Islands with limited liability)

We have audited the consolidated financial statements of Ko Yo Ecological Agrotech (Group) Limited (the "Company") and its subsidiaries (together, the "Group") set out on pages 33 to 84, which comprise the consolidated and company balance sheets as at 31 December 2006, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

DIRECTORS' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The directors of the Company are responsible for the preparation and the true and fair presentation of these consolidated financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with the Companies Law, Cap 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2006 and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 28 March 2007

Consolidated Balance Sheet

	Note	As at 31 December 2006 RMB'000	2005 RMB'000
ASSETS			
Non-current assets			
Land use rights	5	**44,346**	45,124
Property, plant and equipment	6	**304,351**	189,528
Deferred income tax assets	18	**771**	—
Available-for-sale investment	7	**—**	1,000
		349,468	235,652
Current assets			
Inventories	9	**76,804**	74,340
Trade and other receivables	10	**64,378**	53,329
Pledged bank deposits	11, 12, 13	**20,801**	77,800
Cash and cash equivalents	13	**12,839**	47,758
		174,822	253,227
Total assets		**524,290**	488,879
EQUITY			
Capital and reserves attributable to the Company's equity holders			
Share capital	15	**53,449**	44,713
Reserves			
— Proposed final dividends	16, 26	**3,541**	6,580
— Others	16	**235,872**	151,634
		292,862	202,927
Minority interest		**—**	—
Total equity		**292,862**	202,927

Consolidated Balance Sheet

	Note	2006	2005
		As at 31 December	
		RMB'000	RMB'000
LIABILITIES			
Non-current liabilities			
Long-term loans, secured	14	**—**	8,800
Provision for staff compensation	17	**4,573**	7,330
Deferred income tax liabilities	18	**—**	162
		4,573	16,292
Current liabilities			
Trade and other payables	11	**90,919**	121,693
Current income tax liabilities		**1,660**	3,097
Current portion of long-term loans, secured	14	**8,800**	9,000
Short-term bank loans, secured	12	**125,476**	135,870
		226,855	269,660
Total liabilities		**231,428**	285,952
Total equity and liabilities		**524,290**	488,879
Net current liabilities		**(52,033)**	(16,433)
Total assets less current liabilities		**297,435**	219,219

Li Weiruo
Director

Yuan Bai
Director

The notes on pages 39 to 84 are an integral part of these consolidated financial statements.

Balance Sheet

		As at 31 December	
	Note	**2006**	2005
		RMB'000	RMB'000
ASSETS			
Non-current assets			
Investments in subsidiaries	8	**132,310**	74,803
Current assets			
Other receivables	10	**39,509**	39,367
Cash		**20**	52
		39,529	39,419
Total assets		**171,839**	114,222
EQUITY			
Capital and reserves attributable to the Company's equity holders			
Share capital	15	**53,449**	44,713
Reserves			
— Proposed final dividends	16, 26	**3,541**	6,580
— Others	16	**111,434**	59,454
Total equity		**168,424**	110,747
LIABILITIES			
Current liabilities			
Accruals and other payables	11	**3,415**	3,475
Total liabilities		**3,415**	3,475
Total equity and liabilities		**171,839**	114,222
Net current assets		**36,114**	35,944
Total assets less current liabilities		**168,424**	110,747

Li Weiruo
Director

Yuan Bai
Director

The notes on pages 39 to 84 are an integral part of these consolidated financial statements.

Consolidated Income Statement

	Note	Year ended 31 December 2006 RMB'000	2005 RMB'000
Turnover	19	**610,587**	627,616
Cost of sales	21	**(513,212)**	(497,767)
Gross profit		**97,375**	129,849
Other income	20	**6,322**	3,780
Distribution costs	21	**(22,182)**	(34,640)
Administrative expenses	21	**(41,282)**	(38,646)
Operating profit		**40,233**	60,343
Finance costs — net	22	**(6,909)**	(7,143)
Profit before income tax		**33,324**	53,200
Income tax expense	23	**(4,728)**	(6,421)
Profit for the year		**28,596**	46,779
Attributable to:			
Equity holders of the Company	24	**28,596**	46,802
Minority interest		**—**	(23)
		28,596	46,779
Earnings per share for profit attributable to the equity holders of the Company during the year			
(expressed in RMB per share)	25		
— Basic		**0.060**	0.111
— Diluted		**0.060**	0.111
Dividends	26	**6,172**	8,773

The notes on pages 39 to 84 are an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity

	Note	Attributable to equity holders of the Company Share capital RMB'000	Reserves RMB'000	Minority interest RMB'000	Total RMB'000
Balance at 1 January 2005		44,713	118,747	567	164,027
Profit for the year		—	46,802	(23)	46,779
Acquisition of minority interest		—	—	(544)	(544)
Dividends	26	—	(7,335)	—	(7,335)
Balance at 31 December 2005		44,713	158,214	—	202,927
Balance at 1 January 2006		44,713	158,214	—	202,927
Employee share option scheme:					
— value of employee services		—	4,188	—	4,188
Issue of ordinary shares		8,736	57,626	—	66,362
Profit for the year		—	28,596	—	28,596
Dividends	26	—	(9,211)	—	(9,211)
Balance at 31 December 2006		53,449	239,413	—	292,862

The notes on page 39 to 84 are an integral part of these consolidated financial statements.

Consolidated Cash Flow Statement

	Note	Year ended 31 December 2006 RMB'000	2005 RMB'000
Cash generated from operating activities	29(a)	**1,513**	99,559
Income tax paid		**(7,098)**	(6,891)
Interest paid		**(7,905)**	(8,060)
Net cash (outflow)/inflow from operating activities		**(13,490)**	84,608
Cash flows from investing activities			
Acquisition of minority interest		**—**	(600)
Payments for land use rights		**(183)**	(3,140)
Purchases of property, plant and equipment and payments for construction-in-progress		**(119,235)**	(38,887)
Proceeds from disposal of property, plant and equipment		**77**	525
Dividend received from available-for -sale investment		**—**	130
Proceeds from disposal of available-for-sale investment		**1,733**	—
Interest income received		**1,423**	1,351
Net cash used in investing activities		**(116,185)**	(40,621)
Net cash (outflow)/inflow before financing activities		**(129,675)**	43,987
Cash flows from financing activities	29(b)		
Decrease/ (increase) in pledged bank deposits		**56,999**	(23,860)
Issue of ordinary shares		**66,362**	—
New loans payable		**125,476**	135,870
Repayment of bank loans		**(144,870)**	(114,830)
Dividends paid	26	**(9,211)**	(7,335)
Net cash inflow/(used) in financing activities		**94,756**	(10,155)
Net (decrease)/ increase in cash and cash equivalents		**(34,919)**	33,832
Cash and cash equivalents at 1 January		**47,758**	13,926
Cash and cash equivalents at end of the year		**12,839**	47,758

The notes on pages 39 to 84 are an integral part of these consolidated financial statements.

1 GENERAL INFORMATION

Ko Yo Ecological Agrotech (Group) Limited (the "Company") was incorporated in the Cayman Islands on 11 February 2002 as an exempted company with limited liability under the Companies Law Cap. 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands. Its shares have been listed on the Growth Enterprise Market (the "GEM") of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") since 10 July 2003.

The Company is an investment holding company. The Company and its subsidiaries (the "Group") are principally engaged in the manufacture and sale of chemical products and chemical fertilisers in Mainland China.

The address of the registered office and principal place of business of the Company are disclosed in the "Corporate Information" section of the annual report.

These consolidated financial statements are presented in thousands of units of Renminbi Yuan (RMB'000), unless otherwise stated. These consolidated financial statements have been approved for issue by the Board of Directors on 28 March 2007.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

2.1 Basis of preparation

The Group had net current liabilities of RMB52,033,000 as at 31 December 2006 (2005: net current liabilities of RMB16,433,000). The directors of the Company have given due consideration to the liquidity of the Group and have adopted the going concern basis in preparing the consolidated financial statements for the year ended 31 December 2006 on the basis that the Group has profitable operations and that it will succeed in negotiating with its bankers to roll over the outstanding bank loans. As described in Note 33, subsequent to the balance sheet date, bank loans of RMB40 million have been rolled over for a further year and new additional bank loans of RMB26 million have been granted with maturity after one year. One this basis the directors are of the opinion that the Group will have sufficient working capital to finance its operation. Accordingly, the directors are satisfied that it is appropriate to prepare the consolidated financial statements on a going concern basis.

The consolidated financial statements of the Company have been prepared in accordance with Hong Kong Financial Reporting Standards (HKFRS). The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale financial assets, financial assets and financial liabilities (including derivative instruments) at fair value through profit or loss, which are carried at fair value.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.1 Basis of preparation *(Continued)*

The preparation of financial statements in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in Note 4.

(a) Standards/Interpretations to existing standards that are not yet effective and have not been early adopted by the Group

The following standards/interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2007 or later periods that the Group has not early adopted:

- HK(IFRIC)-Int 8, Scope of HKFRS 2 (effective for annual periods beginning on or after 1 May 2006). HK(IFRIC)-Int 8 requires consideration of transactions involving the issuance of equity instruments – where the identifiable consideration received is less than the fair value of the equity instruments issued – to establish whether or not they fall within the scope of HKFRS 2. The Group will apply HK(IFRIC)-Int 8 from 1 January 2007, but it is not expected to have any impact on the Group's consolidated financial statements;

- HK(IFRIC)-Int 10, Interim Financial Reporting and Impairment (effective for annual periods beginning on or after 1 November 2006). HK(IFRIC)-Int 10 prohibits the impairment losses recognised in an interim period on goodwill, investments in equity instruments and investments in financial assets carried at cost to be reversed at a subsequent balance sheet date. The Group will apply HK(IFRIC)-Int 10 from 1 January 2007, but it is not expected to have any impact on the Group's consolidated financial statements;

- HKFRS 7, Financial instruments: Disclosures, and the complementary Amendment to HKAS 1, Presentation of Financial Statements – Capital Disclosures, will be effective for the Group's accounting period beginning on or after 1 January 2007. HKFRS 7 introduces new disclosures to improve the information about financial instruments. The Group will apply HKFRS 7 from 1 January 2007, but it is not expected to have any impact on the classification and valuation of the Company's financial statements; and

- HK(IFRIC)-Int 11, HKFRS2-Group and Treasury Share Transactions (effective for annual period beginning on or after 1 March 2007). HK(IFRIC)-Int 11 addresses equity-settled awards and group scheme. The Group will apply HK(IFRIC)-Int 11 from 1 January 2008, but is is not expected to have any impact on the Group's consolidated financial statements.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.1 Basis of preparation *(Continued)*

(b) Interpretation to existing standards that is not yet effective and not relevant for the Group's operations

The following interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2007 or later periods but are not relevant for the Group's operations:

- HK(IRFIC)-Int 7, Applying the Restatement Approach under HKAS 29, Financial Reporting in Hyperinflationary Economies (effective from 1 March 2006). HK(IFRIC)-Int 7 provides guidance on how to apply requirements of HKAS 29 in a reporting period in which an entity identifies the existence of hyperinflation in the economy of its functional Currency, when the economy was not hyperinflationary in the prior period. As none of the group entities have a Currency of a hyperinflationary economy as its functional Currency, HK(IFRIC)-Int 7 is not relevant to the Group's operations;

- HK(IFRIC)-Int 9, Reassessment of embedded derivatives (effective for annual periods beginning on or after 1 June 2006). HK(IFRIC)-Int 9 requires an entity to assess whether an embedded derivative is required to be separated from the host contract and accounted for as a derivative when the entity first becomes a party to the contract. Subsequent reassessment is prohibited unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract, in which case reassessment if required. As none of the group entities have involved in such contracts, HK(IFRIC)-Int 9 is not relevant to the Group's operations; and

- HK(IFRIC)-Int 12, Service Concession Arrangements (effective for annual period beginning on or after 1 January 2008). HK(IFRIC)-Int 12, applies to companies that participate in service concession arrangement. It provides guidance on the accounting by operators in public-to-private service concession arrangements. As none of the group companies have participated in such service concession arrangements, HK(IFRIC)-Int 12 is not relevant to the Group's operations.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.1 Basis of preparation *(Continued)*

(c) Standards, amendments and interpretations effective in 2006 but not relevant for the Group's operations

The following standards, amendments and interpretations are mandatory for accounting periods beginning on or after 1 January 2006 but are not relevant to the Group's operations:

- HKAS 19 (Amendment) - Employee Benefits;
- HKAS 21 Amendment - New Investment in a Foreign Operation;
- HKAS 39 Amendment - Cash Flow Hedge Accounting of Forecast Intragroup Transactions;
- HKAS 39 Amendment - The Fair Value Option;
- HKAS 39 Amendment - Financial Guarantee Contracts;
- HKFRS 6, Exploration for and Evaluation of Mineral Resources;
- HKFRS 1 Amendment - First-time Adoption of International Financial Reporting Standards;
- HK(IFRIC)-Int 4, Determining whether an Arrangement contains a Lease;
- HK(IFRIC)-Int 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds; and
- HK(IFRIC)-Int 6, Liabilities arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.2 Consolidation

The consolidated financial statements include the financial statements of the Company and all its subsidiaries made up to 31 December.

(a) Subsidiaries

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Company's balance sheet the investments in subsidiaries are stated at cost less provision for impairment losses (Note 2.6). The results of subsidiaries are accounted for by the Company on the basis of dividend received and receivable.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.2 Consolidation *(Continued)*

(b) Transactions with minority interest

The Group applies a policy of treating transactions with minority interest as transactions with parties external to the Group. Disposals to minority interest result in gains and losses for the Group that are recorded in the income statement. Purchases from minority interest result in goodwill, being the difference between any considerations paid and the relevant share acquired of the carrying value of net assets of the subsidiary.

2.3 Segment reporting

The Group regards chemical products and chemical fertilisers as a single business segment. The Group also operates within one geographical segment as its revenues are primarily generated in Mainland China and its assets are located there. Accordingly, no segmental information is presented.

2.4 Foreign currency translation

(a) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in Renminbi ("RMB"), which is the Company's functional and presentation currency.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as qualifying cash flow hedges or qualifying net investment hedges.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.4 Foreign currency translation *(Continued)*

(c) Group companies

The results and financial position of all the group entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

— assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;

— income and expenses for each profit and loss account are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and

— all resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity. When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain or loss on sale.

2.5 Property, plant and equipment

Construction-in-progress represents plant and properties under construction and is stated at cost, which includes development and construction expenditure incurred and other direct costs attributable to the construction, less accumulated impairment losses. Construction-in-progress is not depreciated until such time as the assets are completed and put into operational use.

Other assets, comprising buildings, plant and machinery, motor vehicles, office equipment and others, are stated at cost less accumulated depreciation and accumulated impairment losses.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are expensed in the income statement during the financial period in which they are incurred.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.5 Property, plant and equipment *(Continued)*

Depreciation of other assets is calculated using the straight-line method to allocate their costs or revalue amounts to their residual values over their estimated useful lives, as follows:

—	Buildings	35 years
—	Plant and machinery	12 - 14 years
—	Motor vehicles	10 years
—	Office equipment and others	7 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2.6).

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within other income, in the income statement.

2.6 Impairment of investments in subsidiaries, associates and non-financial assets

Assets that have an indefinite useful life or have not yet available for use are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.7 Financial assets

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, and available-for-sale investments. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition and re-evaluates this designation at every reporting date.

During the year, other than loans and receivables and available-for-sale investment, the Group did not hold any financial assets in other categories.

(a) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. Loans and receivables are classified as 'trade and other receivables' in the balance sheet.

Loans and receivables are carried at amortised cost using the effective interest method.

(b) Available-for-sale investments

Available-for-sale investments are non-derivatives equity securities that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date.

Regular purchases and sales of investments are recognised on trade-date - the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognised at fair value and transaction costs are expensed in the income statement. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership.

Available for-sale investment are subsequently carried at fair value. Dividends on available-for-sale equity instruments are recognised in the income statement as part of other income when the Group's right to receive payments is established.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.7 Financial assets *(Continued)*

(b) Available-for-sale investments *(Continued)*

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, and option pricing models refined to reflect the issuer's specific circumstances.

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity securities classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss - measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss - is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement. Impairment testing of trade receivables is described in Note 2.9.

2.8 Inventories

Inventories comprise stocks and work in progress and are stated at the lower of cost and net realisable value. Cost, calculated on the weighted average basis, comprises materials, direct labour and an appropriate proportion of all production overhead expenditure. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

2.9 Trade and other receivables

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the assets is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement within distribution costs. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts previously written off are credited against distribution costs in the income statement.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.10 Share capital

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

2.11 Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the balance sheet.

2.12 Trade payables

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

2.13 Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

2.14 Employee benefits

(a) Employee leave entitlements

Employee entitlements to annual leave and long service leave are recognised when they accrue to employees. A provision is made for the estimated liability for annual leave and long-service leave as a result of services rendered by employees up to the balance sheet date.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.14 Employee benefits *(Continued)*

(b) Pension obligations

Pursuant to laws and regulations in the People's Republic of China ("Mainland China"), contributions to the basic old age insurance for the Group's Mainland China employees are made monthly to a government agency based on 25% of the standard salary set by the provincial government, of which 20% is borne by the Group and the remainder is borne by the employees. Except for the monthly contribution of 20% on standard salary to the government agency, the Group has no further obligation in connection with Mainland China employees' retirement benefits. The government agency is responsible for the pension liabilities relating to such employees on their retirement. The Group accounts for these contributions on an accrual basis.

The subsidiary in Hong Kong operates a defined contribution scheme which is available to qualified employees. The assets of the scheme are held separately from those of the subsidiary in independently administered funds. Monthly contributions made by the subsidiary are calculated based on certain percentages of the applicable payroll costs or HKD1,000, whichever is lower.

Contributions to the above retirement schemes are charged to the income statement as incurred.

(c) Share-based compensation

The Group operates a number of equity-settled, share-based compensation plans. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example, profitability and sales growth targets). Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. At each balance sheet date, the entity revises its estimates of the number of options that are expected to vest. It recognises the impact of the revision of original estimates, if any, in the income statement, with a corresponding adjustment to equity.

The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised.

2.15 Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.15 Deferred income tax *(Continued)*

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

2.16 Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

All borrowing costs are charged to the income statement in the year in which they are incurred.

2.17 Contingent liabilities

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised but is disclosed in the notes to the consolidated financial statements. When a change in the probability of an outflow occurs so that the outflow becomes probable, it will then be recognised as a provision.

2.18 Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services in the ordinary course of the Group's activities. Revenue is shown net of value-added tax, returns, rebates and discounts and after eliminating sales within the Group.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.18 Revenue recognition *(Continued)*

The Group recognises revenue when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity and specific criteria have been met for each of the Group's activities as described below. The amount of revenue is not considered to be reliably measurable until all contingencies relating to the sale have been resolved. The Group bases its estimates on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement.

Revenue from the sale of goods is recognised on the transfer of risks and rewards of ownership, which generally coincides with the time when the goods are delivered to customers and title has passed.

Interest income is recognised on a time-proportion basis, using the effective interest method.

Dividend income is recognised when the right to receive payment is established.

2.19 Government grants and tax refund

Grants and tax refund from the government are recognised at their fair value where there is a reasonable assurance that the grants and tax refund will be received and the Group will comply with all attached conditions.

Government grants relating to costs are deferred and recognised in the income statement over the period necessary to match them with the costs that they are intended to compensate.

Government grants relating to the purchase of fixed assets are included in non-current liabilities as deferred government grants and are recognised in the income statement on a straight-line basis over the expected lives of the related assets.

Government grants and tax refund are recognised in the income statement as part of other income.

2.20 Operating leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

2.21 Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the financial statements in the period in which dividends are approved by the Company's shareholders.

3 FINANCIAL RISK MANAGEMENT

3.1 Financial risk factors

The Group's principal financial instruments comprise pledged short-term time deposits, trade and other receivables, trade and other payables and bank loans.

The Group's activities expose it to a variety of financial risks: market risks including currency risk, fair value interest rate risk and cash flow interest rate risk), credit risk, and liquidity risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

(a) Foreign exchange risk

The Group exposes to foreign exchange risks as certain portion of sales are denominated in foreign currencies, primarily with respect to the US dollar. The Group currently does not have a foreign currency hedging policy as the directors are of the opinion that the Group's exposure to foreign exchange risk is insignificant because sales denominated in foreign currencies are less than 10% of its total sales and the collection periods of the related trade receivables are within 30 days. However, the management monitors foreign exchange exposure and will consider hedging significant foreign currency exposure should the need arises.

The conversion of RMB into foreign currencies and the remittance of bank balances and cash out of Mainland China are subject to the rules and regulations of foreign exchange control promulgated by the Mainland China government.

(b) Fair value and cash flow interest rate risk

The Group's exposure to fair value and cash flow interest rate risk is minimal as the Group does not have any long term financial assets and liabilities as at 31 December 2006 (2005: RMB8,800,000).

(c) Credit risk

The Group has no significant concentrations of credit risk. It has policies in place of determination of credit limits and credit approval. The Group performs ongoing credit evaluations for its customers' financial condition and generally does not require collateral on trade receivables. The Group maintains a provision for doubtful debts and actual losses have been within management's expectation.

(d) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and the availability of funding through an adequate amount of committed credit facilities. Due to the dynamic nature of the underlying businesses, the Group aims to maintain flexibility in funding by keeping committed credit lines available.

3 FINANCIAL RISK MANAGEMENT *(Continued)*

3.2 Fair value estimation

The carrying value less impairment provision of trade receivables and payables are a reasonable approximation of their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Estimates and judgement are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

4.1 Estimates

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

(a) Depreciation of fixed assets

The Group's net book value of fixed assets as at 31 December 2006 was RMB304,351,000 approximately. The Group depreciates the fixed assets on a straight line basis over the estimated useful life of seven to thirty-five years, and after taking into account of their estimated residual value, using the straight-line method, at the rate 2.6% to 12.9% per annum, commencing from the date the equipment is placed into productive use. The estimated useful life and dates that the Group places the fixed assets into productive use reflect the directors' estimate of the periods that the Group intend to derive future economic benefits from the use of the Group's fixed assets.

(b) Provision for doubtful receivables

The policy for provision for doubtful receivables of the Group is based on the evaluation of collectability and aging analysis of accounts and on management's judgment. A considerable amount of judgment is required in assessing the ultimate realisation of these receivables, including the current creditworthiness and the past collection history of each customer. If the financial conditions of customers of the Group were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS *(Continued)*

4.2 Judgements

In the process of applying the Group's accounting policies, management has made the judgements on impairment of assets and recognition of share-based compensation expenses, apart from those involving estimations as discussed above, which have the most significant effect on the amounts recognised in the financial statements.

(a) Impairment of assets

In determining whether an asset is impaired or the event previously causing the impairment no longer exists, management has to exercise judgement in the area of asset impairment, particularly in assessing: (1) whether an event has occurred that may affect the asset value or such event affecting the asset value has not been in existence; (2) whether the carrying value of an asset can be supported by the net present value of future cash flows which are estimated based upon the continued use of the asset or derecognition; and (3) the appropriate key assumptions to be applied in preparing cash flow projections including whether these cash flow projections are discounted using an appropriate rate. Changing the assumptions selected by management to determine the level of impairment, including the discount rates or the growth rate assumptions in the cash flow projections, could materially affect the net present value used in the impairment test.

(b) Recognition of share-based compensation expenses

As mentioned in Note 15(b), the Company has granted share options to employees of its subsidiaries. Management has used the Black-Scholes valuation model to determine the total fair value of the options granted, which is to be expensed over the vesting period. Significant judgement, such as risk free rate, dividend yield, expected volatility and option life, is required to be made by management as the parameters for applying the Black-Scholes valuation model.

5 LAND USE RIGHTS — GROUP

The Group's land use rights represent prepaid operating lease payments and their net book values are analysed as follows:

	2006	2005
	RMB'000	RMB'000
Opening net book value	**45,124**	42,957
Additions	**183**	3,140
Amortisation of prepaid operating lease payment	**(961)**	(973)
	44,346	45,124

All the Group's land use rights are located in Mainland China. The remaining lease periods of the land use rights are between 10 to 50 years.

As at 31 December 2006, certain land use rights with a total net book value of approximately RMB42,872,000 (2005: RMB43,817,000) were pledged as collateral for the Group's short-term bank loans and long-term bank loans (Notes 12 and 14).

6 PROPERTY, PLANT AND EQUIPMENT — GROUP

	Buildings	Plant and machinery	Motor vehicles	Office equipment and others	Construction-in-progress	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
At 1 January 2005						
Cost	58,605	99,156	4,609	7,450	26,917	196,737
Accumulated depreciation	(6,788)	(21,557)	(743)	(3,771)	—	(32,859)
Net book amount	51,817	77,599	3,866	3,679	26,917	163,878
Year ended 31 December 2005						
Opening net book amount	51,817	77,599	3,866	3,679	26,917	163,878
Transfers	3,453	24,241	—	4,741	(32,435)	—
Additions	2,391	391	887	678	34,540	38,887
Disposals (Note 29)	—	(1,362)	(229)	(8)	—	(1,599)
Depreciation (Note 21)	(1,497)	(8,571)	(417)	(1,153)	—	(11,638)
Closing net book amount	56,164	92,298	4,107	7,937	29,022	189,528
At 31 December 2005						
Cost	64,449	121,535	5,137	12,858	29,022	233,001
Accumulated depreciation	(8,285)	(29,237)	(1,030)	(4,921)	—	(43,473)
Net book amount	56,164	92,298	4,107	7,937	29,022	189,528
Year ended 31 December 2006						
Opening net book amount	56,164	92,298	4,107	7,937	29,022	189,528
Transfers	8,969	9,609	—	530	(19,108)	—
Additions	—	765	947	402	126,389	128,503
Disposals (Note 29)	—	(220)	(33)	(21)	—	(274)
Depreciation (Note 21)	(1,443)	(9,724)	(484)	(1,755)	—	(13,406)
Closing net book amount	63,690	92,728	4,537	7,093	136,303	304,351
At 31 December 2006						
Cost	73,418	131,588	6,047	13,731	136,303	361,087
Accumulated depreciation	(9,728)	(38,860)	(1,510)	(6,638)	—	(56,736)
Net book amount	63,690	92,728	4,537	7,093	136,303	304,351

6 PROPERTY, PLANT AND EQUIPMENT — GROUP *(Continued)*

Depreciation expense of RMB12,209,000 (2005: RMB10,631,000) had been charged in cost of goods sold and RMB1,197,000 (2005: RMB1,007,000) in administrative expenses.

All the Group's buildings are located in Mainland China. As at 31 December 2006, certain buildings with a total net book value of approximately RMB40,518,000 (2005: RMB41,720,000) and plant and machinery with a total net book value of approximately RMB24,296,000 (2005: RMB25,092,000) were pledged as collateral for the Group's short-term bank loans and long-term bank loans (Notes 12 and 14).

7 AVAILABLE-FOR-SALE INVESTMENT — GROUP

	2006	2005
	RMB'000	RMB'000
Unlisted equity investment, at cost		
Beginning of the year	**1,000**	1,000
Additions	**—**	—
Disposals	**(1,000)**	—
	—	1,000

The unlisted equity investment is denominated in RMB and represents the Group's 1.2% equity interest in Sichuan Jiuda Industrial Salt Co. Ltd. ("Sichuan Jiuda"). The largest investor of Sichuan Jiuda, which has approximately 86% interest in Sichuan Jiuda, is one of the Group's largest suppliers, selling industrial salt to the Group.

During the year, the Group sold this investment to the largest investor of Sichuan Jiuda with consideration of RMB1,733,300. The difference between consideration and net book value had been recognised to other income in the income statement (Note 20).

8 INVESTMENTS IN SUBSIDIARIES — COMPANY

	2006 RMB'000	2005 RMB'000
Unlisted investments, at cost	**70,361**	70,361
Investment arising from share-based compensation *(Note a)*	**4,188**	—
Amounts due from subsidiaries *(Note b)*	**63,544**	10,225
Amounts due to subsidiaries *(Note b)*	**(5,783)**	(5,783)
	132,310	74,803

(a) The amount represents share-based compensation expenses arising from grant of share options of the Company to employees of subsidiaries in exchange for their services offered to the subsidiaries.

(b) The amounts due from/to subsidiaries are unsecured, non-interest bearing and have no fixed repayment term.

The following is a list of the subsidiaries as at 31 December 2006:

Name	Place of incorporation/ establishment and kind of legal entity	Principal activities and place of operation	Particulars of issued, registered and fully paid up capital	Interest held
Ko Yo Ecological Agrotech (BVI) Limited ("Ko Yo BVI") *	British Virgin Islands ("BVI"), limited liability company	Investment holding in BVI	100 ordinary shares of USD1 each	100%
Ko Yo Development Company Limited ("Ko Yo Hong Kong")	Hong Kong, limited liability company	Investment holding in Hong Kong	3,000,000 non-voting deferred shares and 100 ordinary shares of HKD1 each	100%
Chengdu Ko Yo Chemical Industry Co., Ltd. ("Chengdu Ko Yo Chemical")	Mainland China, wholly foreign owned enterprise	Manufacture and sale of chemical products including sodium carbonate, ammonia, and chemical fertilisers including urea and ammonium chloride in Mainland China	RMB27,000,000 **	100%

8 INVESTMENTS IN SUBSIDIARIES — COMPANY *(Continued)*

Name	Place of incorporation/ establishment and kind of legal entity	Principal activities and place of operation	Particulars of issued, registered and fully paid up capital	Interest held
Chengdu Ko Yo Compound Fertilisers Co., Ltd. ("Chengdu Ko Yo Compound")	Mainland China, wholly foreign owned enterprise	Manufacture, research, development and sale of bulk blended fertilisers in Mainland China	RMB15,000,000	100%
Dezhou Ko Yo Compound Fertilisers Co., Ltd.("Dezhou Ko Yo Compound")	Mainland China, wholly foreign owned enterprise	Manufacture, research, development and sale of bulk blended fertilisers in Mainland China	RMB3,000,000	100%
Dazhu city Dazhu Ko Yo Chemical Industry Co., Ltd. ("Dazhu Ko Yo Chemical")	Mainland China, wholly foreign owned enterprise	Manufacture and sale of chemical products including ammonia, ammonia carbonate and urea in Mainland China	RMB112,323,000 **	100%
Qingdao Ko Yo Chemical Industry Co., Ltd. ("Qingdao Ko Yo Chemical")	Mainland China, wholly foreign owned enterprise	Manufacture, research, development and sale of bulk blended fertilisers in Mainland China	USD2,100,000 (equivalent to RMB17,032,000)	100%

* Shares held directly by the Company.

** During the year, RMB14,000,000 and RMB64,323,000 were injected in Chengdu Ko Yo Chemical and Dazhu Ko Yo Chemical, respectively, as paid-in capital, by Ko Yo Hong Kong. The additional capital injections had been verified by local certified public accountants.

9 INVENTORIES — GROUP

	2006	2005
	RMB'000	RMB'000
Raw materials	**48,095**	47,615
Work in progress	**10,001**	4,840
Finished goods	**18,708**	21,885
	76,804	74,340

9 INVENTORIES — GROUP *(Continued)*

The cost of inventories recognised as expense and included in cost of goods sold amounted to RMB333,057,000 (2005: RMB334,010,000).

At 31 December 2006, there were no inventories stated at net realisable value (2005: Nil).

10 TRADE AND OTHER RECEIVABLES

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Trade receivables *(Note a)*	**13,961**	22,335	**—**	—
Prepayments, purchase deposits and other deposits	**40,811**	23,714	**332**	190
Notes receivable *(Note b)*	**808**	2,212	**—**	—
Other receivables	**8,798**	5,068	**—**	—
Dividends receivable from a subsidiary	**—**	—	**39,177**	39,177
	64,378	53,329	**39,509**	39,367

(a) Trade receivables

The credit terms of trade receivables granted by the Group are normally within 3 months. The ageing analysis of trade receivables is as follows:

	Group	
	2006	2005
	RMB'000	RMB'000
Aged:		
Less than 3 months	**8,648**	18,384
More than 3 months but not exceeding 1 year	**7,896**	5,250
More than 1 year but not exceeding 2 years	**534**	1,627
More than 2 years but not exceeding 3 years	**1,607**	656
More than 3 years	**656**	—
	19,341	25,917
Less: provision for doubtful receivables	**(5,380)**	(3,582)
	13,961	22,335

10 TRADE AND OTHER RECEIVABLES *(Continued)*

(b) Notes receivable

The balance represents bank acceptance notes with maturity dates within six months.

11 TRADE AND OTHER PAYABLES

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Due to related companies *(Note 31)*	**—**	50	**—**	—
Trade payables *(Note a)*	**30,450**	15,514	**—**	—
Notes payable *(Note b)*	**12,000**	25,100	**—**	—
Deposits from customers	**29,582**	51,919	**—**	—
Accruals and other payables	**18,887**	29,110	**3,415**	3,475
	90,919	121,693	**3,415**	3,475

(a) Trade payables

The ageing analysis of trade payables of the Group is as follows:

	2006	2005
	RMB'000	RMB'000
Aged:		
Less than 1 year	**29,898**	15,193
More than 1 year but not exceeding 2 years	**552**	305
More than 2 years but not exceeding 3 years	**—**	—
More than 3 years	**—**	16
	30,450	15,514

(b) Notes payable

Notes payable represented bank acceptance notes issued by the Group and were interest-free and with maturity dates of less than one year. As at 31 December 2006, notes payable of approximately RMB12,000,000 (2005: RMB25,100,000) were pledged by bank deposits of RMB5,601,000 (2005: RMB18,800,000).

12 SHORT-TERM BANK LOANS, SECURED

The bank loans are denominated in RMB and bear interest with rates ranging from 4.80% to 7.50% (2005: 4.80% to 6.98%) per annum and are secured by a bank deposit of RMB15,200,000 (2005: RMB59,000,000) and certain land use rights and properties, plants and equipments of the Group (Notes 5 and 6).

13 PLEDGED BANK DEPOSITS/CASH AND CASH EQUIVALENTS — GRUOP

The effective interest rates on pledged bank deposits are ranging from 0.72% to 0.73% (2005: 0.72% to 1.71%).

The effective interest rate on cash and cash equivalents is 0.72% (2005: 0.72%).

14 LONG-TERM BANK LOANS, SECURED

	Group	
	2006	2005
	RMB'000	RMB'000
Amounts due:		
Less than 1 year	**8,800**	9,000
More than 1 year but not exceeding 2 years	**—**	8,800
	8,800	17,800
Amounts due within 1 year included in current liabilities	**(8,800)**	(9,000)
	—	8,800

The bank loans are denominated in RMB and bear interest with rates ranging from 6.14% to 6.21% (2005: 6.14% to 6.21%) per annum and are secured by certain land use rights and properties, plants and equipments of the Group (Notes 5 and 6).

15 SHARE CAPITAL

	Authorised	
	Number of shares	Share capital
		RMB'000
At 31 December 2006 and 2005	1,000,000,000	106,000

	Issued and fully paid	
	Number of shares	Share capital
		RMB'000
At 1 January 2005 and 31 December 2005	421,820,000	44,713
Issue of ordinary shares	84,000,000	8,736
At 31 December 2006	505,820,000	53,449

(a) Issue of ordinary shares

On 17 May 2006, the issued share capital of the Company was increased to approximately RMB53,449,000 by issuing 84,000,000 ordinary shares to third party investors at a price of HKD0.78 per share through a placing and subscription arrangement, these shares rank pari passu with the existing shares. The difference between the amount recognised in share capital and total net consideration was recognised to share premium reserve in the balance sheet (Note 16).

15 SHARE CAPITAL *(Continued)*

(b) Share options

Date of grant	23 September 2003	11 April 2006	16 May 2006	
Exercise price (HKD per option)	0.62	0.75	0.75	
Granted to	2 executive directors, 2 independent directors and 6 employees	18 employees	2 executive directors and 1 independent director	Total
Exercisable period	10 years *(Note i)*	10 years	10 years *(Note ii)*	
At 1 January 2005 and 31 December 2005	25,200,000	—	—	25,200,000
Granted	—	10,500,000	1,240,000	11,740,000
Lapsed due to resignation of employees	(800,000)	—	—	(800,000)
At 31 December 2006	24,400,000	10,500,000	1,240,000	36,140,000

The Company has a share option scheme adopted on 10 June 2003 (the "Share Option Scheme"). The purpose of the Share Option Scheme is to recognise the contribution of the eligible participants, and to provide a performance related incentive to them. The eligible participants include the employees (including executive and non-executive directors) and consultants of the Group.

The number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the Share Option Scheme and any other schemes must not exceed 30% of the shares in issue from time to time. The total number of shares which may be issued upon exercise of all options to be granted under the Share Option Scheme and any other schemes must not exceed 42,000,000 shares, 10% of the shares of the Company at the date of commencement of dealings of the Company's shares on GEM.

15 SHARE CAPITAL *(Continued)*

(b) Share options *(Continued)*

Each participant is entitled to a maximum of 4,200,000 share options, which are valid for a period of 10 years from the date of grant. Participants need to pay option price at HKD10 per option for each acceptance of option offer. The subscription price will be determined by the Company's board of directors, and will not be less than the highest of (a) the closing price of the shares quoted on the GEM of the Stock Exchange on the date of the offer; (b) the average closing price of the shares quoted on the GEM of the Stock Exchange for the five business days immediately preceding the date of the offer and (c) the nominal value of the shares.

(i) Share options that were granted on 23 September 2003 and remained outstanding at end of year were held by the following employees (including executive and non-executive directors),

Exercise period	Directors	Number of options 2006
23 September 2004 to 22 September 2013	Ms. Chi Chuan	4,200,000
23 September 2004 to 22 September 2013	Mr. Li Shengdi (appointed on 29 April 2004)	4,200,000
23 September 2004 to 22 September 2013	Ms. Man Au, Vivian	3,800,000
23 September 2004 to 22 September 2013	Mr. Hu Xiaoping	400,000
23 September 2004 to 22 September 2013	Mr. Woo Che-wor, Alex	400,000
		13,000,000
23 September 2004 to 22 September 2013	Other employees	11,400,000
		24,400,000

(ii) Share options that were granted on 16 May 2006 and remained outstanding at end of year were held by the following executive and non-executive directors,

Exercise period	Directors	Number of options 2006
16 May 2006 to 15 May 2016	Mr. Li Weiruo	420,000
16 May 2006 to 15 May 2016	Mr. Yuan Bai	400,000
16 May 2006 to 15 May 2016	Mr. Qian Laizhong	420,000
		1,240,000

15 SHARE CAPITAL *(Continued)*

(b) Share options *(Continued)*

Movements in the number of share options outstanding during the years are as follows:

	2006		2005	
	Average exercise price (HKD per share)	**Options (thousands)**	Average exercise price (HKD per share)	Options (thousands)
At 1 January	**0.62**	**25,200**	0.62	25,200
Granted	**0.75**	**11,740**		—
Lapsed	**0.62**	**(800)**		—
At 31 December	**0.66**	**36,140**	0.62	25,200

The weighted average fair value of options granted during the year determined using the Black-Scholes valuation model was HKD0.36 (RMB0.36) per option. The significant inputs into the model were share price of HKD0.75 (11 April 2006) and HKD1.08 (16 May 2006) respectively, at each grant date, the exercise price shown above, volatility of 68.7%, dividend yield of 4.75%, an expected option life of ten years and on annual risk-free interest rate of 4.8%. The volatility measured at the standard deviation of continuously compounded share returns is based on statistical analysis of daily share prices over the last one year before 11 April 2006. Given that the total number of share options granted in 2006 is 11,740,000, the total fair value was HKD4,188,000 (approximate to RMB4,188,000), which was recognised as administrative expense and a corresponding increase in reserve (Note 16).

16 RESERVES

Movements of the Group's reserves were as follows:

	Share premium RMB'000	Merger reserve RMB'000 *(Note c)*	Reserve fund RMB'000	Enterprise expansion fund RMB'000	Retained earnings RMB'000	Total RMB'000
At 1 January 2006	19,204	(22,041)	11,307	943	148,801	158,214
Fair value of share options *(Note 15 b)*	—	—	4,188	—	—	4,188
Issue of ordinary shares *(Note a)*	59,405	—	—	—	—	59,405
Cost of share issue *(Note a)*	(1,779)	—	—	—	—	(1,779)
Profit for the year	—	—	—	—	28,596	28,596
Appropriation *(Note b)*	—	—	3,307	—	(3,307)	—
Dividends *(Note 26)*	—	—	—	—	(9,211)	(9,211)
At 31 December 2006	76,830	(22,041)	18,802	943	164,879	239,413
Representing:						
2006 final dividend proposed					3,541	3,541
Others					161,338	235,872
					164,879	239,413

Movements of the Company's reserves were as follows:

	Share premium RMB'000	Other reserves RMB'000	Retained earnings RMB'000	Total RMB'000
At 1 January 2006	56,366	—	9,668	66,034
Fair value of share options *(Note 15 b)*	—	4,188	—	4,188
Issue of ordinary shares *(Note a)*	59,405	—	—	59,405
Cost of share issue *(Note a)*	(1,779)	—	—	(1,779)
Profit attributable to shareholders	—	—	(3,662)	(3,662)
Dividends *(Note 26)*	—	—	(9,211)	(9,211)
At 31 December 2006	113,992	4,188	(3,205)	114,975
Representing:				
2006 final dividend proposed			3,541	3,541
Others			(6,746)	111,434
			(3,205)	114,975

16 RESERVES *(Continued)*

(a) Share premium reserve

The net consideration of subscription received was HKD63,809,000 (RMB66,362,000). Accordingly, HKD8,400,000 (RMB8,736,000) and HKD55,409,000 (RMB57,626,000) were recorded as share capital and share premium reserve, respectively.

(b) Statutory reserves

The Company's subsidiaries established in Mainland China are governed by the laws and regulations of Mainland China and their articles of association. They are required to provide for certain statutory funds, namely, reserve fund, enterprise expansion fund and staff and workers' bonus and welfare fund which are appropriated from net profit after taxation but before dividend distribution based on the local statutory financial statements prepared in accordance with accounting principles and relevant financial regulations applicable to enterprises established in Mainland China. They are required to allocate at least 10% of their net profit to the reserve fund until the balance of such fund has reached 50% of its registered capital. Appropriations of enterprise expansion fund and staff and workers' bonus and welfare fund are determined at the discretion of its directors. Appropriation to staff and workers' bonus and welfare fund is charged to expenses. The reserve fund can only be used, upon approval by the relevant authorities, to offset accumulated losses or increase capital. The enterprise expansion fund can only be used to increase capital upon approval by the relevant authorities. The staff and workers' bonus and welfare fund can only be used for special bonus or collective welfare of their employees, and assets acquired through this fund shall not be treated as assets of the Group. Accordingly, the balance of staff and workers' bonus and welfare fund is recorded as a liability of the Group.

(c) Merger reserve

Merger reserve of the Group represents the difference between the nominal value of the share capital issued by the Company and share capital and share premium of a subsidiary acquired through an exchange of shares.

17 PROVISION FOR STAFF COMPENSATION

	2006	2005
	RMB'000	RMB'000
At 1 January	**7,330**	7,388
Payments	**(2,757)**	(58)
At 31 December	**4,573**	7,330

17 PROVISION FOR STAFF COMPENSATION *(Continued)*

Upon the establishment of Chengdu Ko Yo Chemical, certain government loans made to Xin Du Fertilisers Company and certain payables related to staff benefits were conditionally assigned to the former employees of Xin Du Fertilisers Company as provision for staff compensation. Under the arrangement, Chengdu Ko Yo Chemical is required to pay an amount of compensation predetermined at the date of its establishment to these employees if they are laid off by Chengdu Ko Yo Chemical or if they resign before their retirement.

Upon retirement, these employees will be covered by the defined contribution retirement schemes organised by the relevant local government authorities in Mainland China (Note 2.14), and will not be entitled to the repayment of the provision for staff compensation assigned to them. The unpaid balances of the provision for staff compensation are included in non-current liabilities in the balance sheet and were recognised as income upon the retirement of the employees as Chengdu Ko Yo Chemical no longer had any obligations to make repayment to them.

18 DEFERRED INCOME TAX — GROUP

Deferred taxation is calculated in full on temporary differences under the liability method using the taxation rates applicable to the respective companies.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The offset amounts are as follows:

	2006	2005
	RMB'000	RMB'000
Deferred tax assets:		
— Deferred tax asset to be recovered after more than 12 months	**532**	239
— Deferred tax asset to be recovered within 12 months	**239**	223
	771	462
Deferred tax liabilities:		
— Deferred tax liabilities to be settled after more than 12 months	**—**	—
— Deferred tax liabilities to be settled within 12 months	**—**	(624)
	—	(624)
	771	(162)

18 DEFERRED INCOME TAX — GROUP *(Continued)*

The gross movement on the deferred income tax account is as follows:

	2006	2005
	RMB'000	RMB'000
At 1 January	**(162)**	(266)
Deferred taxation credited to income statement *(Note 23)*	**933**	104
At 31 December	**771**	(162)

The movement in deferred tax assets and liabilities during the year, without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

	Deferred tax liabilities		**Deferred tax assets**		**Total**	
	Difference in tax depreciation		**Impairment of assets**			
	2006	2005	**2006**	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000	**RMB'000**	RMB'000
At 1 January	**(624)**	(624)	**462**	358	**(162)**	(266)
Credited to income statement	**624**	—	**309**	104	**933**	104
At 31 December	**—**	(624)	**771**	462	**771**	(162)

19 TURNOVER AND REVENUE

Turnover represents invoiced value of sale of chemical products and chemical fertilisers to customers in Mainland China, net of goods returned and value-added tax ("VAT"), where applicable.

The Group's sales made in Mainland China are subject to VAT on sales ("output VAT"). Such output VAT is payable after offsetting VAT paid by the Group on purchases. The applicable rates of output VAT range from 0% to 17%.

20 OTHER INCOME

	2006 RMB'000	2005 RMB'000
Government grants *(Note a)*	**895**	380
VAT refund *(Note b)*	**—**	1,905
Tax refund for reinvestments *(Note c)*	**2,865**	—
Dividend income from unlisted investment	**—**	130
Gain from disposal of available-for-sale investment *(Note 7)*	**733**	—
Sales of waste materials	**1,021**	1,365
Others	**808**	—
	6,322	3,780

(a) Government grants

Pursuant to the document (1999) No.33 issued by the local government authority, Chengdu Ko Yo Chemical is entitled to receive a government grants equal to certain percentage of its net VAT paid to the local tax bureau. The applicable rates for the two years ended 30 June 2001 and the four years ended 30 June 2005 are 80% and 50%, respectively. Such policy was terminated on 1 July 2005.

Pursuant to the document (2006) No. 62 and No. 178 issued by local authority of finance, Chengdu Ko Yo Chemical is entitled to receive government grants as subsidy for certain construction works relating to energy saving and environment protection.

(b) VAT refund

Until 1 July 2005, pursuant to the document Cai Shui (2004) No.33 issued by the Ministry of Finance and the National Tax Bureau of Mainland China in 2004, companies established in Mainland China are entitled to a refund of VAT paid on sale of certain qualified agricultural chemical fertilisers. Chengdu Ko Yo Chemical and Dazhu Ko Yo Chemical are entitled to receive a refund for its net VAT paid on its sales of urea and the tax refund rate was 50%.

And pursuant to the document Cai Shui (2005) No.87 issued by the Ministry of Finance and the National Tax Bureau of Mainland China in 2005, since 1 July 2005, companies established in Mainland China are entitled to an entire exemption of VAT for sale of urea. Accordingly, Chengdu Ko Yo Chemical and Dazhu Ko Yo Chemical are entitled to this exemption treatment since 1 July 2005.

Pursuant to the document Guo Shui (1999) No.171 issued by the National Tax Bureau of Mainland China in 1999 and as approved by the local taxation bureau, Dazhu Ko Yo Chemical is entitled to receive a refund for its VAT paid on its purchase of machinery from mainland China enterprises, which are local machinery suppliers and unrelated to the Group and the tax refund rate was 100%.

20 OTHER INCOME *(Continued)*

(c) Tax refund for reinvestments

Amount represented income tax refund for reinvestments in subsidiaries by way of capitalisation of dividend.

21 EXPENSES BY NATURE

	2006 RMB'000	2005 RMB'000
Changes in inventories of finished goods and work in progress	**6,403**	(9,719)
Raw materials and consumables used	**326,654**	343,729
Power and natural gas consumed	**128,600**	115,698
Maintenance expenses	**9,596**	9,653
Customs duty	**1,237**	5,817
Staff costs *(Note 27)*	**47,024**	38,710
Depreciation, amortisation and impairment charges *(Note 5 and 6)*	**14,367**	12,611
Provisions for doubtful receivables *(Note 10)*	**1,798**	1,356
Loss on disposal of property, plant and equipment *(Note 29 (a))*	**197**	1,074
Transportation expenses	**15,822**	18,057
Advertisement expenses	**3,602**	6,128
Operating lease payments	**1,130**	1,195
Auditors' remuneration	**1,561**	1,200
Other expenses	**18,685**	25,544
Total cost of sales, distribution costs and administrative expenses	**576,676**	571,053

22 FINANCE COSTS-NET

	2006 RMB'000	2005 RMB'000
Interest expenses of bank borrowings	**7,928**	7,170
Interest income	**(1,425)**	(917)
Others	**406**	890
	6,909	7,143

23 INCOME TAX EXPENSE

No provision for profits tax in the Cayman Islands, British Virgin Islands or Hong Kong has been made, as the Group had no assessable profit arising in or derived from those jurisdictions during the years ended 31 December 2006 and 2005.

Chengdu Ko Yo Chemical, Chengdu Ko Yo Compound, Dezhou Ko Yo Compound, Dazhu Ko Yo Chemical and Qingdao Ko Yo Chemical were established as foreign investment enterprises in Mainland China. They are all subject to Enterprise Income Tax ("EIT") at the rate of 15% except for Dezhou Ko Yo Compound which the EIT rate is 33%, and entitled to full exemption from EIT in the first two profitable years and a 50% reduction for the next three years thereafter.

Pursuant to Chuan Guo Shui Han (2006) No. 40 issued by the local tax bureau of Sichuan province, foreign-invested enterprises established in Sichuan province are subject to Local Enterprise Income Tax ("LEIT") at the rate of 3%, since 1 January 2006.

Since the preferential treatment had expired for Chengdu Ko Yo Chemical in the year ended 31 December 2006, the overall rate (both EIT and LEIT) applicable to Chengdu Ko Yo Chemical in 2006 is 18% (2005: 15%). Accordingly, current income tax provision made for Chengdu Ko Yo Chemical for the year ended 31 December 2006 was RMB4,733,000 (2005: RMB5,900,000).

The preferential EIT rate applicable to Chengdu KoYo Compound for the year ended 31 December 2006 is 7.5% (2005: 7.5%), plus the rate of 3% of LEIT, the overall rate applicable is 10.5% (2005: 7.5%). Accordingly, current income tax provision made for Chengdu Ko Yo Compound for the year ended 31 December 2006 was RMB713,000 (2005: RMB625,000).

The preferential EIT rate applicable to Dazhu KoYo Chemical for the year ended 31 December 2006 is 0% (2005: 0%), plus the rate of 3% of LEIT, the overall rate applicable is 3% (2005: 0%). Accordingly, current EIT provision made for Dazhu KoYo Chemical for the year ended 31 December 2006 was RMB215,000 (2005: nil).

Dezhou Ko Yo Compound and Qingdao Ko Yo Chemical did not have taxable profit for the year ended 31 December 2006 (2005: Nil).

23 INCOME TAX EXPENSE *(Continued)*

The amount of taxation charged to the consolidated income statement represents:

	2006 RMB'000	2005 RMB'000
Current tax for Mainland China	**5,661**	6,525
Deferred income tax *(Note 18)*	**(933)**	(104)
	4,728	6,421

The taxation on the Group's profit before taxation differs from the theoretical amount that would arise using the statutory taxation rate applicable to profits of the consolidated companies as follows:

	2006 RMB'000	2005 RMB'000
Profit before taxation	**28,596**	53,200
Calculated at statutory taxation rate of 18% (2005: 15%)	**5,147**	7,980
Expenses not deductible for tax purposes	**—**	314
Effect of deduction of 40% of cost of machinery acquired from Mainland China enterprises	**—**	(2,389)
Tax losses for which no deferred income tax was recognised	—	1,002
Effects on tax holiday available to different companies of the Group	**(419)**	(486)
Taxation	**4,728**	6,421

24 LOSS ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

The loss attributable to equity holders of the Company is dealt with in the financial statements of the Company to the extent of RMB3,661,000 (2005: profit of RMB11,784,000).

25 EARNINGS PER SHARE

(a) Basic

Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year.

	2006 RMB'000	2005 RMB'000
Profit attributable to equity holders of the Company	**28,596**	46,802
Weighted average number of ordinary shares in issue (thousands)	**474,271**	421,820
Basic earnings per share (RMB per share)	**0.060**	0.111

(b) Diluted

Diluted earnings per share is calculated adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The Company has just one category of dilutive potential ordinary shares: share options. For the share options, a calculation is made in order to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Company's shares) based on the monetary value of the subscription rights attached to outstanding share options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the share options.

	2006 RMB'000	2005 RMB'000
Profit attributable to equity holders of the Company	**28,596**	46,802
Weighted average number of ordinary shares in issue (thousands)	**474,271**	421,820
Adjustment - share options (thousands)	**640**	—
Weighted average number of ordinary shares for diluted earnings per share (thousands)	**474,911**	421,820
Diluted earnings per share (RMB per share)	**0.060**	0.111

26 DIVIDENDS

	2006 RMB'000	2005 RMB'000
Interim, paid, of HKD0.005 (2005: HKD0.005) per ordinary share	**2,631**	2,193
Final, proposed, of HKD0.007 (2005: HKD0.015) per ordinary share	**3,541**	6,580
	6,172	8,773

At a meeting held on 10 August 2006, the directors declared an interim dividend of HKD0.005 (equivalent to RMB0.0052) per ordinary share, totalling approximately RMB2,631,000, which was paid during the year ended 31 December 2006.

At a meeting held on 16 March 2007, the directors proposed a final dividend of HKD0.007 (equivalent to RMB0.007) per ordinary share, totalling approximately RMB3,541,000 This proposed dividend is not reflected as a dividend payable in these financial statements, but will be reflected as an appropriation of retained earnings for the year ending 31 December 2007.

27 STAFF COSTS

	2006 RMB'000	2005 RMB'000
Wages and salaries	**36,207**	33,669
Pension costs — defined contribution plans	**3,977**	3,093
Social security costs	**2,652**	1,948
Share options granted to directors and employees *(Note 15 b)*	**4,188**	—
	47,024	38,710

28 DIRECTORS' AND SENIOR MANAGEMENT's EMOLUMENTS

(a) Directors' emoluments

The remuneration of every director for the year ended 31 December 2006 is set out below:

Name of director	Fees	Salaries, allowances, and benefits in kind	Bonuses	Contributions to pension schemes	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Executive Directors					
Mr. Li Weiruo	618	250	200	22	1,090
Mr. Yuan Bai	124	220	150	10	504
Ms. Chi Chuan	124	220	150	10	504
Mr. Li Shengdi	124	250	150	11	535
Ms. Man Au, Vivian	124	371	150	12	657
Independent non-executive directors					
Mr. Hu Xiaoping	62	—	10	—	72
Mr. Woo Che-wor, Alex	62	—	10	—	72
Mr. Qian Laizhong	62	—	10	—	72
	1,300	1,311	830	65	3,506

28 DIRECTORS' AND SENIOR MANAGEMENT's EMOLUMENTS *(Continued)*

(a) Directors' emoluments *(Continued)*

The remuneration of every director for the year ended 31 December 2005 is set out below:

Name of director	Fees	Salaries, allowances, and benefits in kind	Bonuses	Contributions to pension schemes	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Executive Directors					
Mr. Li Weiruo	624	180	206	24	1,034
Mr. Yuan Bai	125	173	156	7	461
Ms. Chi Chuan	125	173	156	7	461
Mr. Li Shengdi	125	173	156	7	461
Ms. Man Au, Vivian	125	377	156	11	669
Independent non-executive directors					
Mr. Hu Xiaoping	62	—	11	—	73
Mr. Woo Che-wor, Alex	62	—	11	—	73
Mr. Qian Laizhong	62	—	11	—	73
	1,310	1,076	863	56	3,305

(b) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for both years include four directors (2005: four) whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining individual (2005: also only one individual) during the year are as follows:

	2006	2005
	RMB'000	RMB'000
Basic salaries, housing allowances, other allowances and benefits in kind	**460**	638
Bonuses	**—**	—
Contributions to pension schemes	**12**	13
	472	651

28 DIRECTORS' AND SENIOR MANAGEMENT's EMOLUMENTS *(Continued)*

(b) Five highest paid individuals *(Continued)*

The emoluments fell within the following bands:

	Number of individuals	
	2006	2005
	RMB'000	RMB'000
Emolument bands		
Nil to RMB1,000,000 (equivalent to HKD1,000,000)	**1**	1

During the year, the Group did not pay any amount to the five highest paid individuals (including directors and the employee) nor any other directors of the Company as an inducement to join or upon joining the Group or as compensation for loss of office and no directors waived any emoluments during the year.

29 CONSOLIDATED CASH FLOW STATEMENT

(a) Reconciliation of profit before taxation to cash generated from operating activities

	2006	2005
	RMB'000	RMB'000
Profit before taxation	**33,325**	53,200
Depreciation	**13,406**	11,638
Amortisation of land use rights	**961**	973
Loss on disposal of property, plant and equipment	**197**	1,074
Impairment of goodwill arising from acquisition of minority interest	**—**	56
Interest income	**(1,425)**	(917)
Interest expenses	**7,928**	8,060
Dividend income	**—**	(130)
Gain from disposal of available-for-sale investment	**(733)**	—
Share options granted to directors and employees	**4,188**	—
Operating profit before working capital changes	**57,847**	73,954
Increase in inventories	**(648)**	(23,303)
Decrease in trade and other receivables	**(12,862)**	(4,566)
(Decrease)/ increase in trade and other payables	**(40,017)**	53,606
Decrease in other long-term payables	**(2,757)**	(58)
Decrease in amount due to related companies	**(50)**	(74)
Cash generated from operating activities	**1,513**	99,559

29 CONSOLIDATED CASH FLOW STATEMENT *(Continued)*

(a) Reconciliation of profit before taxation to net cash inflow/(outflow) from operating activities *(Continued)*

In the cash flow statement, proceeds from disposal of property, plant and equipment comprise:

	2006	2005
	RMB'000	RMB'000
Net book amount *(Note 6)*	**274**	1,599
Loss on disposal of property, plant and equipment	**(197)**	(1,074)
Proceeds from disposal of property, plant and equipment	**77**	525

(b) Analysis of changes in financing during the year

	Pledged bank deposit		Share capital including premium		Minority interest		Loans	
	2006	2005	**2006**	2005	**2006**	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000	**RMB'000**	RMB'000	**RMB'000**	RMB'000
At 1 January	**(77,800)**	(53,940)	**63,917**	63,917	**—**	567	**153,670**	132,630
Decrease/(increase)in pledged bank deposit	**56,999**	(23,860)	**—**	—	**—**	—	**—**	—
Issue of share capital	**—**	—	**66,362**	—	**—**	—	**—**	—
New loans payable	**—**	—	**—**	—	**—**	—	**125,476**	135,870
Repayment of amounts borrowed	**—**	—	**—**	—	**—**	—	**(144,870)**	(114,830)
Minority interest' share of profits	**—**	—	**—**	—	**—**	(23)	**—**	—
Acquisition of monitory interests	**—**	—	**—**	—	**—**	(544)	**—**	—
At 31 December	**(20,801)**	(77,800)	**130,279**	63,917	**—**	—	**134,276**	153,670

30 COMMITMENTS

(a) Capital commitments for property, plant and equipment

	2006	2005
	RMB'000	RMB'000
Contracted but not provided for		
— Acquisition of production facilities *(Note 32)*	**214,014**	—
— Constructions-in-progress	**50,464**	14,140
	264,478	14,140

(b) Commitments under operating leases

At 31 December 2006, the Group had future aggregate minimum lease payments under non-cancellable operating leases for land and buildings as follows:

	2006	2005
	RMB'000	RMB'000
Not later than one year	**756**	848
Later than one year and not later than five years	**88**	269
	844	1,117

31 RELATED-PARTY TRANSACTIONS

The following transactions were carried out with related parties:

(a) Key management compensation (excluding directors' emoluments)

	2006	2005
	RMB'000	RMB'000
Salaries and other short-term employee benefits	**949**	987

The directors' emoluments are disclosed in Note 28.

(b) The amounts due to related companies as of 31 December 2005 as disclosed in Note 11 are due to parties controlled by relatives of Mr. Li Weiruo, a shareholder and director, arose from advances fro related companies and are unsecured and interest-free. The directors of the Company are of the opinion that the above balances arose in the ordinary course of the Group's business and were settled in 2006.

32 ACQUISITION OF PRODUCTION FACILITIES

In order to enhance the Group's production capacity and competitiveness in the fertilizer markets and facilitate the growth of the Group, on 5 October 2006, the Company announced that Dazhu Ko Yo Chemical, as the ultimate purchaser, entered into a sale and purchase contract (the "Contract") with a vendor (the "Vendor"), located in United States of America, to acquire certain production facilities for a total consideration of USD 35.9 million (equivalent to approximately RMB290.8 million). The consideration will be settled in cash and 35% of the enlarged registered capital in capital of Dazhu Ko Yo Chemical. The 35% of the enlarged registered capital of Dazhu Ko Yo Chemical will equal to RMB105 million and the corresponding amount of which in the USD will be calculated in accordance with the exchange rate on the effective date of the increase in the registered capital. The balance will be settled in cash according to payment terms and conditions that stipulated in the Contract.

During the year, the Group paid USD 9.5 million (equivalent to approximately RMB76.8 million) to the Vendor. As of 31 December 2006, the capital commitment in relation to the Contract as disclosed in Note 30 was approximately RMB214.0 million.

For the purpose of financing the above-mentioned commitment, the Group is in application with several banks for a long-term bank loan of not less than RMB400 million. In this connection, the Group has received a letter of intent from one of the banks which indicated that it is in consideration to lend a long-term bank loan of RMB450 million to the Group but the approval is yet to be finalised. Furthermore, pursuant to a supplementary agreement signed by the Vendor and the Company dated 22 March 2007, the Vendor will not demand for further payment until the Group succeeds in obtaining the above-mentioned long-term bank loan and the Vendor's fulfilment of the payment conditions as stipulated in the Contract. The directors are of the view that it is reasonable to expect that the Group will obtain the borrowings from the banks and has no foreseeable funding gap in the near term.

33 EVENT AFTER THE BALANCE SHEET DATE

Subsequent to the balance sheet date, bank loans of RMB40 million have been rolled over for a further year and new additional bank loans of RMB26 million have been granted with maturity after one year, out of which approximately RMB15 million was drawn down by the Group. Furthermore, the Group has received letters of intent from certain banks indicating that they are willing to extend short-term loans of approximately RMB52 million, with maturity dates ranging from April 2007 to March 2008, for a further year upon maturity, subject to certain circumstances and conditions.

34 COMPARATIVE FIGURES

Certain comparative figures have been reclassified so as to conform with current year's presentation and details are as follows:

— Current income tax liabilities, which were included in with trade and other payables in 2005, have been separately disclosed; and

— Interest income, which was included in other income in 2005, has been included in finance costs.

FIVE YEAR FINANCIAL SUMMARY

The following table summarizes the audited results, assets and liabilities of the Group for the five years ended 31st December 2006.

	2006	2005	2004	2003	2002
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Turnover	**610,587**	627,616	422,728	281,810	277,572
Profit before taxation	**33,324**	53,200	33,894	24,104	31,199
Taxation	**(4,728)**	(6,421)	(1,215)	(31)	427
Profit after taxation	**28,596**	46,779	32,679	24,073	31,626
Minority interest	**—**	23	33	—	(286)
Profit attributable to shareholders	**28,596**	46,802	32,712	24,073	31,340
Total assets	**524,290**	488,879	361,174	266,221	239,276
Total liabilities	**(231,428)**	(285,952)	(209,513)	(143,290)	(174,709)
Minority interests	**—**	—	(567)	(600)	—
Shareholders' funds	**292,862**	202,927	151,094	122,331	64,567

NOTICE IS HEREBY GIVEN that the annual general meeting of the members of Ko Yo Ecological Agrotech (Group) Limited (the "Company") will be held at Suite No. 02, 31st Floor, Sino Plaza, 255-257 Gloucester Road, Causeway Bay, Hong Kong on 26th April 2007 at 11:00 a.m. for the following purposes:

1. To receive and consider the audited consolidated financial statements of the Company and its subsidiaries, the report of the directors and the auditors, and the corporate governance report for the year ended 31st December 2006;

2. To consider the re-election of the retiring directors of the Company;

3. To consider and authorize the board of directors (the "Board") of the Company to fix the directors' remunerations;

4. To consider and approve the final dividend of the Company for the year ended 31st December 2006;

5. To consider the re-appointment of PricewaterhouseCoopers as auditors of the Company and to authorize the Board to fix their remuneration; and

   As special business, to consider and if thought fit, pass the following resolutions as ordinary resolutions:

6. "THAT:

   (a) subject to sub-paragraph (c) below, the exercise by the directors of the Company ("Directors") during the Relevant Period (as defined below) of all the powers of the Company to allot, issue and deal with the ordinary shares of par value HKD0.10 each (the "Shares") in the capital of the Company and to make an offer or agreement or grant an option which would or might require such Shares to be allotted and issued be generally and unconditionally approved;

   (b) the Directors be authorized to make an offer or agreement or grant an option during the Relevant Period which would or might require Shares in the capital of the Company to be allotted and issued either during or after the end of the Relevant Period pursuant to sub-paragraph (a) above;

   (c) the aggregate nominal value of the Shares in the capital of the Company allotted or agreed conditionally or unconditionally to be allotted (whether pursuant to an option or otherwise) by the Directors pursuant to the approvals in sub-paragraphs (a) and (b) above, otherwise than pursuant to a rights issue (as defined below) or pursuant to the exercise of options which may be granted under the Share Option Scheme adopted by the Company on 10th June 2003 or an issue of Shares of the Company in lieu of the whole or part of a dividend on Shares of the Company in accordance with the articles of association of the Company, shall not exceed the aggregate of:

      (i) 20% of the aggregate nominal value of the share capital of the Company in issue; and

      (ii) conditional on the passing of Resolution No. 8 below, the aggregate nominal amount of the share capital of the Company purchased under the authority referred to in Resolution No. 7;

(d) for the purpose of this resolution:

"Relevant Period" means the period from the passing of this resolution until whichever is the earlier of:

(i) the conclusion of the next annual general meeting of the Company following the passing of this resolution; or

(ii) the expiration of the period within which the next annual general meeting of the Company is required by the laws of the Cayman Islands or the articles of association of the Company to be held; or

(iii) the passing of an ordinary resolution by the shareholders of the Company in general meeting revoking or varying the authority given to the Directors by this resolution; and

"rights issue" means the allotment or issue of Shares in the Company or other securities which would or might require Shares to be allotted and issued pursuant to an offer made to all the shareholders of the Company (excluding for such purpose any shareholder who is resident in a place where such offer is not permitted under the laws of that place) and, where appropriate, the holders of other equity securities of the Company entitled to such offer, pro rata (apart from fractional entitlements) to their existing holdings of Shares or such other equity securities."

7. "THAT:

(a) the Directors be granted a general mandate to exercise all the powers of the Company to purchase its own securities on the Stock Exchange of Hong Kong Limited (the "Stock Exchange") or on any other stock exchange on which shares in the capital of the Company may be listed and which is recognized by the Securities and Futures Commission and the Stock Exchange for this purpose, such number of securities as will represent up to 10% of the aggregate nominal value of the share capital of the Company in issue, during the Relevant Period (defined below) in accordance with all applicable laws and the requirements of the Rules Governing the Listing of Securities on the Growth Enterprise Market of the Stock Exchange ("GEM Listing Rules") (as amended from time to time) (or of such other stock exchange);

(b) for the purpose of this resolution:

"Relevant Period" means the period from the passing of this resolution until whichever is the earlier of:

(i) the conclusion of the next annual general meeting of the Company following the passing of this resolution; or

(ii) the expiration of the period within which the next annual general meeting of the Company is required by the laws of the Cayman Islands or the articles of association of the Company to be held; or

(iii) the passing of an ordinary resolution by shareholders of the Company in general meeting revoking or varying the authority given to the Directors by this resolution."

8. "THAT the unconditional general mandate referred to in Resolution No. 6 above be extended by the addition to the aggregate nominal amount of the share capital of the Company which may be allotted or agreed to be allotted by the Directors pursuant to such unconditional general mandate of an amount representing the aggregate nominal amount of the securities of the Company purchased by the Company pursuant to the mandate to purchase securities referred to in Resolution No. 7 above, provided that such extended amount shall not exceed 10% of the aggregate nominal value of the share capital of the Company in issue."

On behalf of the board

Chung Tin Ming
Company Secretary

Hong Kong, 28th March 2007

Notes:

(1) A member entitled to attend and vote at the meeting is entitled to appoint a proxy to attend and, in the event of, a poll, vote instead of him. A proxy need not be a member of the Company.

(2) In order to be valid, the form of proxy must be deposited with the Company's share registrar in Hong Kong, Union Registrars Limited, at Room 1803, Fook Lee Commerical Centre, Town Place, 33 Lockhart Road, Wanchai, Hong Kong, together with any power of attorney or other authority, under which it is signed, or a notarially certified copy of that power or authority, not less than 48 hours before the time for holding the meeting or any adjournment thereof.

(3) Where there are joint holders of any shares in the Company, any one of such joint holders may vote, either in person or by proxy, in respect of such shares as if he were solely entitled thereto, but if more than one of such joint holders are present at the meeting, the senior who tenders a vote, whether in person or by proxy, shall be accepted to the exclusion of the votes of the other joint holders, and for this purpose seniority shall be determined by the order in which the names stand in the register in respect of the joint holding.

(4) The register of members of the Company will be closed for the purpose of determining the entitlements of the proposed final dividend from 23rd April 2007 to 26th April 2007, both days inclusive, during which period no transfer of shares will be effected. In order to qualify for the proposed final dividend, all transfers, accompanied by the relevant share certificates, must be lodged for registration with the Company's registrar, Union Registrars Limited, at the above address no later than 4:00 p.m. on 20th April 2007.

(5) Concerning Resolutions No. 6 and No. 7, the Board wishes to state that there is no immediate plan to issue any new shares or to repurchase any shares of the Company. The general mandates are being sought from shareholders in compliance with the Companies Law (Law 3 of 1961, as revised and consolidated) of the Cayman Islands and the GEM Listing Rules.

(6) For the sake of good corporate governance practice, the Chairman intends to demand poll voting for all the resolutions set out in the notice of the annual general meeting.