INDEBTEDNESS

Borrowings and banking facilities

As at 30th June, 2007, the Group had outstanding bank loans of approximately RMB110,000,000, which will be due within a year at fixed interest rates ranging from 6.12% to 6.39% per annum. The banking facilities available to the Group has been fully utilised as at 30th June, 2007. There is no default in repayment of bank loan during the Track Record Period.

For the outstanding bank loans of RMB110,000,000 as at 30th June, 2007, Xinjiang Tianye Company Limited (新疆天業股份有限公司) had granted guarantees to a bank for securing loans in the principal sum of RMB80,000,000 at an interest rate of 6.12% per annum. The above guarantees will be released before the Introduction. Property, plant and equipment of approximately RMB81,675,000 has been pledged to a bank for securing loan in the principal sum of RMB30,000,000 at an interest rate of 6.39% per annum.

Commitments

As at 30th June, 2007, the Group had contracted but not provided for capital commitment of RMB24,349,000. The Group has committed to acquire facilities and machineries to increase at least 30% in production lines for all products at the Company and at Kuitun.

Contingent liabilities

As at 30th June, 2007, the Group had no contingent liabilities.

Disclaimer

The Directors have confirmed that save as aforesaid and apart from intra-group liabilities, as at the close of business on 30th June, 2007, the Group did not have outstanding loan capital, bank borrowings and liabilities under acceptances or other similar indebtedness, debentures, mortgages, charges or loans or acceptance credits or hire purchase commitments, guarantees or other material contingent liabilities.

The Directors have confirmed that there has not been any material adverse change in the indebtedness and contingent liabilities of the Group since 30th June, 2007.

DISCLOSURE UNDER RULES 13.13 TO 13.19 OF THE LISTING RULES

The Directors have confirmed that, as at the Latest Practicable Date, there is no circumstance which would give rise to a disclosure requirement under Rules 13.13 to 13.19 of the Listing Rules.

LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE

Liquidity ratios

The current ratio and quick ratio of the Group as at 31st December, 2006 were approximately 4.29 and 2.43, respectively, representing an increase of 1.74 and 1.15, respectively when compared to 31st December, 2005. This is primarily due to approximately 41.19% increase in inventories, approximately 50.99% increase in trade and other payables as at 31st December, 2006 and approximately 185.42% increase in bank balances and cash and approximately 71.73% increase in bills receivable during the year under review.

The current ratio and quick ratio of the Group as at 30th June, 2007 were approximately 2.87 and 1.74, respectively, representing a decrease of 1.42 and 0.69, respectively when compared to 31st December, 2006. This was primarily due to approximately 98.20% increase in short-term bank borrowings during the period under review.

Net current assets

As at the close of business on 30th June, 2007, the Group had net current assets of approximately RMB482,924,000. Components of current assets and current liabilities comprise:

	RMB'000
Current assets	
Inventories	291,734
Trade and other receivables	246,844
Bills receivable	39,540
Tax refundable	8,399
Bank balances and cash	155,022
	741,539
Current liabilities	
Trade and other payables	148,615
Short-term bank borrowings	110,000
	258,615
Net current assets	482,924

The current assets were funded by internal resources and banking facilities provided by its bankers.

Financial resources

The Group currently finances its operations mainly by internal generated funds, net proceeds from initial public offering and cash on hand. The Directors are of the view that, in the long run, the Group will generate its liquidity from business operations and will consider making use of further equity finances or bank loans, when necessary.

Capital expenditure

For each of the three years ended 31st December, 2006 and the six months ended 30th June, 2007, capital expenditure of the Group in respect of acquisition of property, plant and equipment and prepaid leasing premium amounted to approximately RMB44,659,000, RMB5,565,000, RMB26,526,000 and RMB15,120,000 respectively, which were in line with the expansion plans of the Group.

Capital structure

For each of the three years ended 31st December, 2006 and the six months ended 30th June, 2007, the Group had gearing ratio (which is defined as total borrowings over total equity) of approximately 16.06%, 20.46%, 8.74% and 16.97% respectively. The Directors confirm that the Group financed its operations principally from cash generated from its business operations and banking facilities and had not experienced any liquidity problem during the Track Record Period.

Funding and treasury policies

The Directors confirm that the Group's funding and treasury policies are mainly based on its cash flow forecast and budgetary system to monitor and control the sources and applications of funds.

The objectives of the Group's funding and treasury policies are to prevent the unreasonable utilisation of funding, enhance the effectiveness on the utilisation of working capital, ensure the punctual repayment of the Group's liabilities upon the relevant maturity date and ensure liquidity of the working capital, so as to optimise the Group's net cash flow position.

Cash flow from operating activities

Net cash used in operating activities for the six months ended 30th June, 2007 amounted to approximately RMB20.3 million, while the net cash from operating activities for the corresponding period in 2006 amounted to approximately RMB53.6 million. The different between net cash used in operating activities and profits before taxation of approximately RMB52.7 million was mainly attributable to the adjustment for depreciation of property, plant and equipment of approximately RMB11.7 million, the increase in inventories of approximately RMB24.0 million, the increase in trade and other receivables of approximately RMB85.3 million, the increase in bills receivable of approximately RMB12.1 million and the increase in trade and other payables of approximately RMB60.5 million.

Net cash used in operating activities for the year ended 31st December, 2006 amounted to approximately RMB30.5 million, while the net cash from operating activities for the year ended 31st December, 2005 amounted to approximately RMB35.1 million. The result in 2006 is mainly attributable to the decrease in profit before taxation by approximately 5.4% to approximately RMB59.2 million. The different between net cash from operating activities and profits before taxation of approximately RMB89.7 million was mainly attributable to the adjustment for depreciation of property, plant, and equipment of approximately RMB22.9 million, the increase in inventories of approximately RMB78.1 million, the increase in trade and other receivables of approximately RMB41.4 million, the increase in bills receivable of approximately RMB11.5 million and the increase in trade and other payables of approximately RMB28.8 million.

Net cash from operating activities for the year ended 31st December, 2005 amounted to approximately RMB35.1 million, while the net cash from operating activities for the year ended 31st December, 2004 amounted to approximately RMB7.8 million. The improvement was mainly attributable to the increase in profit before taxation by approximately 20.3% to approximately RMB62.6 million. The different between net cash from operating activities and profits before taxation of approximately RMB27.5 million was mainly attributable to the adjustment for depreciation of property, plant, and equipment of approximately RMB22.4 million, the increase in inventories of approximately RMB12.6 million, the decrease in trade and other receivables of approximately RMB39.5 million, the increase in bills receivable of approximately RMB15.9 million and the decrease in trade and other payables of approximately RMB56.0 million.

Cash flow from investing activities

Net cash used in investing activities for the six months ended 30th June, 2007 amounted to approximately RMB14.0 million, while the net cash used in investing activities for the corresponding period in 2006 amounted to approximately RMB6.4 million. The result for the six months ended 30th June, 2007 was mainly due to the purchase of property, plant and equipment of approximately RMB15.1 million, purchase of equity investments of approximately RMB9.8 million and proceeds from sale of equity investments of approximately RMB10.5 million mainly for the purpose of effective management of idle cash the Group, resulted in gain on disposal of approximately RMB0.7 million during the six months ended 30th June, 2007.

Net cash used in investing activities for the year ended 31st December, 2006 amounted to approximately RMB21.8 million, while net cash from investing activities for the year ended 31st December, 2005 amounted to approximately RMB0.4 million. The result for the year ended 31st December, 2006 was mainly due to the purchase of property, plant and equipment of approximately RMB18.9 million, purchase of equity investments of approximately RMB35 million and proceeds from sale of equity investments of approximately of approximately RMB37.5 million mainly for the purpose of effective management of idle cash of the Group, resulted in gain on disposal of approximately RMB2.5 million during the year ended 31st December, 2006.

Net cash from investing activities amounted to approximately RMB0.4 million for the year ended 31st December, 2005, while net cash used in investing activities amounted to approximately RMB46.4 million for the year ended 31st December, 2004. The improved result was mainly due to the reduced purchase of property, plant and equipment of approximately RMB4.8 million as compared to RMB44.6 million for the previous year and the repayment of the advance to Tianye Holdings Group of approximately RMB5.7 million for the year ended 31st December, 2005.

Cash flow from financing activities

Net cash from financing activities for the six months ended 30th June, 2007 amounted to approximately RMB35.5 million, while the net cash from financing activities for the corresponding period in 2006 amounted to approximately RMB177.9 million. The decrease compared to the corresponding period in 2006 was mainly due to the issue of shares of approximately RMB247.2 million and the settlement of the Company's GEM listing expenses of approximately RMB34.5 million in 2006.

Net cash from financing activities amounted to approximately RMB152.3 million for the year ended 31st December, 2006, while net cash used in financing activities amounted to approximately RMB16.0 million for the year ended 31st December, 2005. The increase in net cash from financing activities was mainly due to the issue of shares of approximately RMB247.2 million, the bank loan raised of approximately RMB55.5 million, the repayment of bank loans of approximately RMB80.0 million, the dividends paid to equity holders of the Company of approximately RMB40.4 million and the listing expenses paid of approximately RMB36.3 million for the year ended 31st December, 2006.

Net cash used in financing activities amounted to approximately RMB16.0 million for the year ended 31st December, 2005, while net cash used in financing activities amounted to approximately RMB36.8 million for the year ended 31st December, 2004. The improved result was mainly due to the bank loan raised of approximately RMB80.0 million, the repayment of bank loans of approximately RMB60.0 million and the dividends paid to equity holders of the Company of approximately RMB29.4 million for the year ended 31st December, 2005.

Directors' opinion on sufficiency of working capital

The Directors are of the opinion that, taking into account the internally generated resources of the Group and the banking facilities available to the Group, the Group has sufficient working capital for its present requirements, that is for at least the next 12 months from the date of this document.

Foreign currency exposure

As confirmed by the Directors, the Group's present operations are carried out in the PRC, and all of the Group's receipts and payments in relation to the operations are denominated in RMB. In this respect, the Directors consider there is no significant currency mismatch in its operational cashflows and the Group is not exposed to any significant foreign currency exchange risk in its operation.

TRADING RECORD

The table below sets out a summary of the audited consolidated results of the Group for each of the three years ended 31st December, 2006 and the six months ended 30th June, 2007. The summary has been prepared on the basis that the current structure of the Group had been in existence throughout the period under review or from the respective dates of acquisition/establishment of the companies now comprising the Group, where this is a shorter period. The summary should be read in conjunction with the accountants' report of the Group set out in Appendix I to this document.

		Year ended 31st December,			For the six months ended 30th June,	
		2004	**2005**	**2006**	**2006**	**2007**
	Notes	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
					(Unaudited)	
Turnover	1	389,183	376,251	461,809	257,716	297,205
Cost of sales		(308,947)	(280,373)	(366,601)	(208,264)	(243,637)
Gross profit		80,236	95,878	95,208	49,452	53,568
Other operating income		1,769	336	6,983	606	2,240
Distribution costs		(14,170)	(18,512)	(22,965)	(11,349)	(10,546)
Administrative expenses		(12,173)	(11,197)	(15,525)	(5,447)	(9,665)
Other operating expenses		(93)	(305)	(631)	(29)	(573)
Profit from operations		55,569	66,200	63,070	33,233	35,024
Finance costs		(3,523)	(3,566)	(3,840)	(2,051)	(2,688)
Profit before taxation		52,046	62,634	59,230	31,182	32,336
Taxation		(7,951)	(7,595)	824	(4,789)	(183)
Profit for the year/period		44,095	55,039	60,054	26,393	32,153
Profit (loss) attributable to:						
Equity holders of the Company		42,432	52,658	62,497	26,128	31,504
Minority interests		1,663	2,381	(2,443)	265	649
		44,095	55,039	60,054	26,393	32,153
Dividends		8,879	34,883	34,860	34,860	18,703
Earnings per Share — basic	2	RMB0.13	RMB0.17	RMB0.13	RMB0.06	RMB0.06

Notes:

1. Turnover is measured at the fair value of the consideration received and receivable for goods sold, net of returns, allowances and value-added tax and revenue arising on long-term contracts during the Track Record Period.

2. The calculation of the basic earnings per Share for the year ended 31st December, 2004 and 31st December, 2005 is based on the profit for that year attributable to equity holders of the Company and 317,121,560 Shares in issue during that year.

The calculation of the basic earnings per Share for the year ended 31st December, 2006, six months ended 30th June, 2006 and six months ended 30th June, 2007 is based on the profit for the year/period attributable to equity holders of the Company and on the weighted average number of 485,623,477 Shares, 451,163,549 Shares and 519,521,560 Shares respectively in issue during the year/period.

No diluted earnings per share has been presented for the Track Record Period as there was no dilutive shares outstanding during the Track Record Period.

CRITICAL ACCOUNTING POLICIES

In preparation of the financial information of the Group which is included in the accountants' report of the Company set out in Appendix I to this document, the Company adopts the significant accounting policies as set out in note 4 of the accountants' report. In applying such policies, the Company has made critical estimates and assumptions based on historical experience which it believes to be reasonable under the respective circumstances. The Directors believe the following critical accounting policies involve the most significant judgments and estimates used in the preparation of the financial information.

Business Combinations

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured as the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities meeting the conditions for recognition under Hong Kong Financial Reporting Standard 3 "Business Combinations" are recognised at their fair values at the acquisition date.

The interest of minority shareholders in the acquiree is initially measured at the minority's proportion of the net fair value of the assets, liabilities and contingent liabilities recognised.

Goodwill

Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Capitalised goodwill on an acquisition of a subsidiary is presented separately in the consolidated balance sheets.

Goodwill arising on the acquisition of a subsidiary represents the excess of the cost of the business combination over the Group's interest in the net fair values of the identifiable assets, liabilities and contingent liabilities of the subsidiary recognised at the date of acquisition.

For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually and whenever there is an indication that the unit may be impaired. For goodwill arising on an acquisition in a financial year. The cash generating units to which goodwill has been allocated is tested for impairment before the end of that year. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. Any impairment loss for goodwill is recognised directly in the consolidated income statements. An impairment loss recognised for goodwill is not reversed in a subsequent consolidated period.

On subsequent disposal of a subsidiary, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Revenue recognition

Revenue is recognised at the fair value of the consideration received or receivables and represents amounts receivable from goods sold in the normal course of business, net of discounts and sales related tares.

Sales of goods are recognised when goods are delivered and title has passed.

When the outcome of a long-term contract can be estimated reliably, revenue from fixed price contracts is recognised on the percentage of completion method, measured by reference to the proportion that costs incurred to date bear to estimated total costs for each contract. Variations in contract work, claims and incentive payments are included to the extent that they have been agreed with the customer.

When the outcome of a long-term contract cannot be estimated reliably, revenue is recognised only to the extent of contract costs incurred that it is probable will be recoverable.

Interest income from a financial asset is accrued on a time basis, by reference to the principal outstanding and at the interest rate applicable, which is the rate that exactly discounts the estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Sales of equity investments are recognised on a trade date basis when the rules and rewards of ownership are transferred and title has passed.

MANAGEMENT DISCUSSION AND ANALYSIS

Overview

As a pioneer in providing one-stop solutions for water saving irrigation system in the PRC, the Group is principally engaged in the design, manufacturing and sales of drip films, PVC/PE pipelines and drip assemblies used in water saving irrigation system. The Group is also engaged in the provision of installation services of water saving irrigation system for its customers. Drip irrigation system plays a significant role in water conservation. It is a slow water delivery system in which every drop of water can be applied to the soil surface near the root of plant. The burden of deciding the timing of irrigation and the required amount of water can be relieved from the properly designed automatic drip irrigation system. The potential and importance of water saving irrigation system have been recognised by both the PRC Government and producers of agricultural products in the PRC.

The drip films sold by the Group can be categorised into three types, including (i) single-sided labyrinth-style drip films; (ii) embedded-style drip films; and (iii) heavy flow compensatory-style drip films.

Along with the opportunities and challenges, the Group may face certain risks involved in its business. The high oil price, as well as the continuous upward trend in the price of down-stream plastic raw materials would lead to an increase in the costs of the Group's products, thus lowering their competitiveness. In the short term, the Group relies on its key management and personnel. The Group also relies on the stable business relationships with certain major customers. In view of these, the Group will continue to maintain good relationships with its staff and will continue to provide training to its staff. Moreover, the Group will place great emphasis on its after-sales services to its customers and will widen its customer base by expanding its sales and distribution network.

Results of Operations

Six months ended 30th June, 2007 compared to six months ended 30th June, 2006

Turnover

For the six months ended 30th June, 2007, the turnover of the Group was approximately RMB297,205,000, an increase of approximately 15.32% from approximately RMB257,716,000 for the six months ended 30th June, 2006.

The following table summaries the breakdown of the total turnover of the Group for each of the six months ended 30th June, 2006 and 2007 by products or services:

Category	For the six months ended 30th June, 2007 Turnover	% of total turnover	For the six months ended 30th June, 2006 Turnover	% of total turnover	Period-on-period Percentage change
	RMB'000	%	*RMB'000*	%	%
Drip films	177,378	59.7	149,934	58.2	18.3
PVC/PE pipelines	92,800	31.2	76,929	29.8	20.6
Drip assemblies	25,063	8.4	30,814	12.0	-18.7
Provision of installation service	1,964	0.7	39	—	4935.9
Total	297,205	100.0	257,716	100.0	

For the six months ended 30th June, 2007, sales of drip films increased by approximately 18.3% to approximately RMB177,378,000, while sales of PVC/PE pipelines increased by approximately 20.6% to approximately RMB92,800,000. At the same time, the sales volume of drip films increased from approximately 10,949 tonnes for the six months ended 30th June, 2006 to approximately 12,442 tonnes for the six months ended 30th June, 2007, while the sales volume of PVC/PE pipelines increased from approximately 11,315 tonnes for the six months ended 30th June, 2006 to approximately 12,841 tonnes for the six months ended 30th June, 2007. The increase in the sales volume of the Group's product was mainly attributable to the growth in the demand for water saving irrigation system in the PRC. The sales of drip assemblies decreased by approximately 18.7% to approximately RMB25,063,000 which was mainly due to certain customers purchased the drip assemblies from other suppliers. The increase in the provision of installation services from approximately RMB39,000 to approximately RMB1,964,000 was mainly due to the increase in request for installation services during the period.

Cost of sales

For the six months ended 30th June, 2007, cost of sales of the Group was approximately RMB243,637,000, with an increase of approximately 16.98% from approximately RMB208,264,000 for the six months ended 30th June, 2006. Costs of sales for the six months ended 30th June, 2007 comprised direct materials of approximately RMB211,504,000, direct labors of approximately RMB6,122,000 and production overhead of approximately RMB26,011,000, which accounted for approximately 86.81%, 2.51%, 10.68%, respectively, of total costs of sales for the period under review. Costs of sales for the six months ended 30th June, 2006 comprised direct materials of approximately RMB175,358,000, direct labors of approximately RMB4,644,000 and production overhead of approximately RMB28,262,000, which accounted for approximately 84.20%, 2.23%, 13.57%, respectively, of total costs of sales for the period under review.

Gross profit

The Group realised a gross profit of approximately RMB53,568,000 for the six months ended 30th June, 2007, representing an increase of approximately 8.32% compared to the previous period. The Group's gross profit margin decreased from 19.19% for the six months ended 30th June, 2006 to 18.02% for the six months ended 30th June, 2007. The decrease was mainly due to the increase in costs of raw materials. The selling price of PE resins for the period under review increased by 7.42% when compared to the previous period and the selling price of PVC resins also increased by 14.10% when compared to the same period in 2006.

Other operating income

Other operating income consists primarily of bank interest income, gain arising from sales of equity investments and exchange gain. Such income was increased from approximately RMB606,000 for the six months ended 30th June, 2006 to approximately RMB2,240,000 for the six months ended 30th June, 2007. The increase was mainly attributable to the increase of gain arising from sales of equity investments and exchange gain for the period under review which amounted to approximately RMB714,000 and RMB1,094,000 respectively.

Distribution costs

Distribution costs were decreased by approximately 7.08% to approximately RMB10,546,000 for the six months ended 30th June, 2007. The amount accounted for approximately 3.55% of the total turnover for the six months ended 30th June, 2007, decreased from that of approximately 4.40% of total turnover for the six months ended 30th June, 2006. Distribution costs mainly comprised of transportation costs, sales service expenses, salaries, commission for sales staff, depreciation charges, traveling expenses and business entertainment fees, etc. The decrease was mainly due to the decrease in traveling expenses of approximately 41.24% to approximately RMB330,000 and entertainment fees of approximately 48.5% to approximately RMB490,000.

Administrative expenses

Administrative expenses were increased by approximately 77.44% to approximately RMB9,665,000 for the six months ended 30th June, 2007. The amount accounted for approximately 3.25% of total turnover for the six months ended 30th June, 2007, increased from that of approximately 2.11% of total turnover for the six months ended 30th June, 2006. The increase was mainly contributed by the increase in salaries of approximately 47.15% to approximately RMB2,995,000 and allowance for bad debt to approximately RMB1,806,000.

Operating profit

As a result of the factors discussed above, the Group's operating profit for the six months ended 30th June, 2007 was approximately RMB35,024,000, representing an increase of approximately 5.39% from approximately RMB33,233,000 for the six months ended 30th June, 2006. The Group's operating margin (profit from operations expressed as a percentage of Group's turnover) was approximately 11.78% for the six months ended 30th June, 2007 and 12.90% for the six months ended 30th June, 2006.

Finance costs

Finance costs for the six months ended 30th June, 2007 amounted to approximately RMB2,688,000, representing an increase of approximately 31.06% as compared to the corresponding period in the previous year. It was mainly due to the increase of the Company's borrowings of RMB59,000,000 when compared with corresponding period in previous year.

Profit attributable to equity holders of the Company

As a result of the factors discussed above, the profit attributable to equity holders of the Company increased by approximately 20.58%, from approximately RMB26,128,000 for the six months ended 30th June, 2006 to approximately RMB31,504,000 for the six months ended 30th June, 2007. For the six months ended 30th June, 2006 and 2007, the Group's net profit margin was approximately 10.14% and 10.60%, respectively.

Year ended 31st December, 2006 compared to year ended 31st December, 2005

Turnover

For the year ended 31st December, 2006, the turnover of the Group was approximately RMB461,809,000, an increase of approximately 22.74% from approximately RMB376,251,000 for the year ended 31st December, 2005.

The following table summaries the breakdown of the total turnover of the Group for each of the two years ended 31st December, 2006 by products or services:

	For the year ended 31st December, 2006		For the year ended 31st December, 2005		Year-on-year
	Turnover	% to total turnover	Turnover	% to total turnover	Percentage change
Category	*RMB'000*	*%*	*RMB'000*	*%*	*%*
Drip films	245,802	53.2	194,960	51.8	26.1
PVC/PE pipelines	157,602	34.1	123,785	32.9	27.3
Drip assemblies	55,346	12.0	53,047	14.1	4.3
Provision of installation services	3,059	0.7	4,459	1.2	–31.4
Total	461,809	100.0	376,251	100.0	

The change in turnover for the year ended 31st December, 2006 was mainly attributable to the effect of an expansion of farmland fitted with the water saving irrigation products of the Group. For the year ended 31st December, 2006, sales of drip films increased by approximately 26.1% to approximately RMB245,802,000, while sales of PVC/PE pipelines increased by approximately 27.3% to approximately RMB157,602,000. At the same time, the sales volume of drip films increased from approximately 14,926 tonnes for the year ended 31st December, 2005 to approximately 20,027 tonnes for the year ended 31st December, 2006, while the sales volume of PVC/PE pipelines increased from approximately 16,322 tonnes for the year ended 31st December, 2005 to approximately 24,389 tonnes for the year ended 31st December, 2006. The increase in the sales volume of the Group's products was mainly attributable to the growth in demand for water saving irrigation system in the PRC. Although the sales volume of the Group's drip films, drip assemblies and PC/PE pipelines increased, the amounts of sales for drip films and PVC/PE piplines have only increased by lesser extent than the sales volume, this is attributable to the decrease of selling prices of drip films by approximately 6.06% from RMB13,062 per tonne in 2005 to RMB12,270 per tonne in 2006 and the decrease of selling prices of PVC/PE pipelines by 14.79% from RMB7,584 per tonne in 2005 to RMB6,462 per tonne in 2006. On the contrary, the decrease in the provision of installation services from approximately RMB4,459,000 for the year ended 31st December, 2005 to approximately RMB3,059,000 for the year ended 31st December, 2006 was mainly due to the fact that some of the Company's customers installed water saving irrigation system by themselves; hence, the Group's income generated by the provision of installation services had decreased. As a result, the turnover in provision of installation services decreased by approximately 31.40% for the period under review.

Cost of sales

For the year ended 31st December, 2006, cost of sales of the Group was approximately RMB366,601,000, with an increase of approximately 30.75% from approximately RMB280,373,000 for the year ended 31st December, 2005. Costs of sales for the year ended 31st December, 2006 comprised direct materials of approximately RMB309,274,000, direct labors of approximately RMB10,187,000 and production overhead of approximately RMB47,140,000, which accounted for approximately 84.36%, 2.78% and 12.86%, respectively, of total costs of sales for the year under review. Costs of sales for the year ended 31st December, 2005 comprised direct materials of approximately RMB222,025,000, direct labors of approximately RMB9,949,000 and production overhead of approximately RMB48,399,000, which accounted for approximately 79.19%, 3.55% and 17.26%, respectively, of total costs of sales for 2005.

Gross profit

The Group realised a gross profit of approximately RMB95,208,000 for the year ended 31st December, 2006, which stood at the same level as in the year ended 31st December, 2005. The Group's gross profit margin decreased from approximately 25.48% for the year ended 31st December, 2005 to approximately 20.62% for the year ended 31st December, 2006. The decrease in gross profit margin was mainly due to the increase in costs of raw materials and recycle materials for drip films and hence the costs to mix formulas were increased during the year. The cost of PE resins increased by approximately 12.3% from RMB9,400 per tonne in 2005 to RMB10,560 per tone in 2006 and the cost of recycle materials increased by approximately 21.8% from RMB7,010 per tonne in 2005 to RMB8,540 per tonne in 2006. In addition, as a result of the fierce competition among the PVC pipeline manufacturers and the decrease in cost of PVC resins by approximately 16.2% from approximately RMB6,000 per tonne in 2005 to RMB5,030 per tone in 2006, the price of the PVC pipelines decreased during 2006. In view of the above situation and in order to maintain its competitiveness, the Group reduced the selling price of PVC pipelines from RMB7,455 per tonne in

2005 to RMB6,650 per tonne in 2006 which represented a decrease of approximately 10.8%. In short, the principle reason for the decrease in our gross profit was the increase in our raw material costs as a result of the rise in our costs of raw materials and recycled raw materials for the production of drip films. A decrease of approximately 10.8% in the unit selling price of our PVC pipelines also contributed to the decrease in our overall gross profit in 2006.

Other operating income

Other operating income consists primarily of bank interest income and gain arising from sales of equity investments. Such income had increased from approximately RMB336,000 for the year ended 31st December, 2005 to approximately RMB6,983,000 for the year ended 31st December, 2006. The increase was mainly attributable to the increase of gain arising from sales of equity investments and bank interest income for the year which amounted to approximately RMB2,500,000 and RMB2,209,000 respectively.

Distribution costs

Distribution costs was approximately RMB22,965,000 for the year ended 31st December, 2006, representing an increase of approximately 24.05%. The amount accounted for approximately 4.97% of the total turnover for the year ended 31st December, 2006, more than its share of total turnover of approximately 4.92% for the corresponding period in the previous year. Distribution costs mainly comprised transportation costs, sales service expenses, salaries, commissions for sales staff, depreciation charges, traveling expenses and business entertainment fees, etc. For the year ended 31st December, 2006, sales and transportation costs, salaries, traveling expenses and business entertainment fees increased by approximately 28.02%, 4.92%, 29.17% and 38.13% to approximately RMB7,462,000, RMB6,614,000, RMB961,000 and RMB739,000, respectively, while sales services expenses decreased by approximately 37.68% to approximately RMB387,000.

Administrative expenses

Administrative expenses increased by approximately 38.65% to approximately RMB15,525,000 for the year ended 31st December, 2006. The amount accounted for approximately 3.36% of total turnover for the year ended 31st December, 2006, more than its share of total turnover of approximately 2.98% for the corresponding period in the previous year. For the year ended 31st December, 2006, salary costs increased by 3.73% to approximately RMB3,478,000 and traveling expenses increased by approximately 443.88% to approximately RMB2,355,000, while business entertainment fees decreased by approximately 10.43% to approximately RMB352,000 and allowance for trade receivables decreased by approximately 96.13% to approximately RMB52,000.

Profit from operations

As a result of the factors discussed above, the Group's profit from operations for the year ended 31st December, 2006 was approximately RMB63,070,000, representing a decrease of approximately 4.73% from approximately RMB66,200,000 for the corresponding period in the previous year. The Group's gross operating margin (expressed as a percentage of profit from operations over the Group's turnover) were approximately 17.59% and 13.66% respectively for the years ended 31st December, 2005 and 2006.

Finance costs

Finance costs for the year ended 31st December, 2006 amounted to approximately RMB3,840,000, representing an increase of approximately 7.68% as compared to the corresponding period in the previous year. Higher finance costs were mainly resulted from the slight increase of lending rate.

Profit attributable to equity holders of the Company

As a result of the factors discussed above, the profit attributable to equity holders of the Company increased by approximately 18.68%, from approximately RMB52,658,000 for the year ended 31st December, 2005 to approximately RMB62,497,000 for the year ended 31st December, 2006. For the two years ended 31st December, 2005 and 2006, the Group's net profit margin was approximately 14.00% and 13.53%, respectively.

Year ended 31st December, 2005 compared to year ended 31st December, 2004

Turnover

For the year ended 31st December, 2005, the turnover of the Group was approximately RMB376,251,000, with a decrease of approximately 3.3% from approximately RMB389,183,000 for the year ended 31st December, 2004. The Directors consider that the Group's turnover of drip films increased of RMB29,104,000 by 17.5% comparing with the preceding year. Sales of drip films were exempted from value-added tax in 2004. Value-added tax of sales of drip films was paid at a rate of 13% in 2005, therefore deducting the accrued value-added tax from the Group's turnover. RMB25,905,000 was deducted from the Group's turnover as value-added tax was paid at the same rate during the year. The above factors reduced the turnover of drip films by 13.3% of RMB25,905,000. With an increase of sales of diversion pipelines, sales of PVC/PE pipelines of the year increased by approximately 12.3%, which is RMB13,569,000, from approximately RMB110,216,000 in the preceding year to approximately RMB123,785,000. Sales of Drip assemblies of the year decreased from approximately RMB81,105,000 of the preceding year to approximately RMB53,047,000, representing approximately 34.6% decrease of RMB28,058,000. In order to increase the number of customers using the Group's drip system and lower their usage cost per hectare, the Group has altered the design of drip system, reduced the number of pipelines connecting accessories, hence reducing the amount of drip fittings and corresponding revenue. The Group's turnover generated by the provision of installation services had decreased from approximately RMB32,006,000 during the preceding year to approximately RMB4,459,000 this year, representing a 86.1% decrease of approximately RMB27,547,000. This was mainly due to the fact that some of the Company's customers installed water saving irrigation system by themselves after grasping the installation technique, hence the Group's turnover generated by the provision of installation services had decreased.

In conclusion, turnover of the year decreases by 3.3% as compared to last year, which was mainly attributable to a 17.5% and 12.3% increase of sales of drip films and PVC/PE pipelines respectively, and a 34.6% and 86.1% decrease in turnover of drip assemblies and provision of installation.

The following table highlights the breakdown of total turnover of the Group for each of the two years ended 31st December, 2005 by products or services:

	For the year ended 31st December, 2005		For the year ended 31st December, 2004		Year-on-year
	Turnover	% to total turnover	Turnover	% to total turnover	Percentage change
Category	*RMB'000*	%	*RMB'000*	%	%
Drip films	194,960	51.8	165,856	42.6	17.5
PVC/PE pipelines	123,785	32.9	110,216	28.3	12.3
Drip assemblies	53,047	14.1	81,105	20.9	–34.6
Provision of installation services	4,459	1.2	32,006	8.2	–86.1
Total	376,251	100.0	389,183	100.0	

The change in turnover for the year ended 31st December, 2005 was mainly attributable to the overall effect of an expansion of farmland fitted with the Company's water saving irrigation products and the decrease in provision of installation services. For the year ended 31st December, 2005, sales volume of drip films increased by approximately 17.5% of approximately RMB29,104,000, while sales volume of PVC/PE pipelines increased by approximately 12.3% of approximately RMB13,569,000. At the same time, selling price of both drip films and PVC pipelines increased from approximately RMB12,544 per tonne and RMB6,279 per tonne, respectively, for the year ended 31st December, 2004 to that of approximately RMB13,062 per tonne and RMB7,455 per tonne, respectively, for the year ended 31st December, 2005. The increase in both the sales volume and selling price of the Group's products were attributable to the growth in demand for water saving irrigation system in the PRC. On the contrary, the decrease in the provision of installation services from approximately RMB32,006,000 to approximately RMB4,459,000 was mainly due to the fact that some of the Group's customers installed water saving irrigation system by themselves, hence the Group's turnover generated by the provision of installation services had decreased. As a result, the turnover in provision of installation services decreased by approximately 86.1% for the year under review.

Cost of sales

For the year ended 31st December, 2005, cost of sales of the Group was approximately RMB280,373,000, with a decrease of approximately 9.2% from approximately RMB308,947,000 compared to the previous year. For the year ended 31st December, 2005, costs of sales comprised direct materials of approximately RMB222,025,000, direct labors of approximately RMB9,949,000 and production overhead of approximately RMB48,399,000, which accounted for approximately 79.2%, 3.5% and 17.3%, respectively, of total costs of sales for the year under review. For the year ended 31st December, 2004, costs of sales comprised direct materials of approximately RMB226,298,000, direct labors of approximately RMB12,247,000 and production overhead of approximately RMB70,402,000, which accounted for approximately 73.2%, 4.0% and 22.8% respectively, of total costs of sales for the year under review.

Gross profit

The Group realised a gross profit of approximately RMB95,878,000 for the year ended 31st December, 2005, representing an increase of approximately 19.5% compared to the previous year. The Group's gross profit margin increased from approximately 20.6% for the year ended 31st December, 2004 to approximately 25.5% for the year ended 31st December, 2005. The increase in gross profit margin was due to the overall effect of increase in recycle rate of drip films, decrease of prescription cost of raw materials.

Other operating income

Other operating income consists primarily of interest income. It decreased from approximately RMB1,769,000 for the year ended 31st December, 2004 to approximately RMB336,000 for the year ended 31st December, 2005.

Distribution costs

Distribution costs increased by approximately 30.6% to approximately RMB18,512,000 for the year ended 31st December, 2005. It accounted for approximately 4.9% of total turnover for the year ended 31st December, 2005, increased from that of approximately 3.6% of total turnover for the corresponding period in the previous year. Distribution costs mainly comprised of transportation costs, sales services expenses, salaries, commissions for sales staff, depreciation charges, traveling expenses and business entertainment fees, etc.

Administrative expenses

Administrative expenses decreased by approximately 8% to approximately RMB11,197,000 for the year ended 31st December, 2005. It accounted for approximately 3.0% of total turnover for the year ended 31st December, 2005, which was comparable to that of approximately 3.1% of total turnover for the corresponding period in the previous year. For the year ended 31st December, 2005, salary costs decreased by 19.6% to RMB3,353,000, labour insurance increased by 15.6% to RMB2,725,000, business entertainment fees increased by 32.8% to RMB393,000 and allowance for bad debts decreased by approximately 46.4% to approximately RMB1,343,000.

Operating profit

As a result of the factors discussed above, the Group's operating profit for the year ended 31st December, 2005 was approximately RMB66,200,000, representing an increase of approximately 19.1% from approximately RMB55,569,000 for the corresponding period in the previous year. The Group's operating margin (profit from operations expressed as a percentage of Group's turnover) was approximately 14.3% and 17.6%, respectively for the year ended 31st December, 2004 and 2005.

Finance costs

Finance costs for the year ended 31st December, 2005 amounted to approximately RMB3,566,000 representing an increase of 1.2% for the corresponding period in the previous year.

Profit attributable to equity holders of the Company

As a result of the factors discussed above, the Group's net profit increased by approximately 24.1%, from approximately RMB42,432,000 for the year ended 31st December, 2004 to approximately RMB52,658,000 for the year ended 31st December, 2005. The Group's net profit margin for the year ended 31st December, 2004 and 2005 was approximately 10.9% and 14.0%, respectively.

ANALYSIS ON SELECTED BALANCE SHEET ITEMS

Inventory

As of 31st December, 2004, 31st December, 2005, 31st December, 2006 and 30th June, 2007, the Group recorded balances of inventory of approximately RMB177.1 million, RMB189.6 million, RMB267.7 million and RMB291.7 million, respectively, whilst cost of sales for the respective periods amounted to approximately RMB308.9 million, RMB280.4 million, RMB366.6 million and RMB243.6 million, respectively. Inventory turnover periods, expressed as closing balances of inventory for the year end over total cost of sales for the relevant year times number of days in the relevant year, were approximately 209 days, 247 days, 267 days and 217 days during the Track Record Period. The lengthening of inventory turnover day for the year 2006 was mainly attributable to the expected continuous growth of the market in 2007 spring and the Group started to increase the raw material purchases and productions in order to satisfy the expected customer demand in 2007 leading to an increase of approximately 41% for the year end inventory of 2006 comparing to 2005.

The Directors confirm that as the main targeted customers of the Group's products are farmers, the features of agricultural production cycle are relevant to the Group. As a result, the production and sales of the Group's products are subject to seasonality. The Directors also confirm that in general, the production peak season is from November of a year to February of next year, while the sales peak season is from March to May of a year, and the low season for production and sales is from July to October of a year. Owing to the seasonality factor, the annual inventory turnover period is approximately seven to eight months, and the Directors believe that this is in line with the production pattern of the Company.

As at the Latest Practicable Date, subsequent sales of inventories as at 30th June, 2007 amounted to approximately RMB23,149,000.

Trade receivables

As of 31st December, 2004, 31st December, 2005, 31st December, 2006 and 30th June, 2007, the Group had trade receivables (less allowances) amounted to approximately RMB61.7 million, RMB80.1 million, RMB111.3 million and RMB157.0 million, respectively, whilst turnover for the respective periods amounted to approximately RMB389.2 million, RMB376.3 million, RMB461.8 million and RMB297.2 million, respectively. As of 31st December, 2004, 31st December, 2005, 31st December, 2006 and 30th June, 2007, approximately 20.7%, 6.0%, 5.0% and 2.2%, respectively, of trade receivables aged from one to two years. Debtors' turnover periods (expressed as closing balances of trade receivables for the year end over total turnover for the relevant year times number of days in the relevant year), were approximately 58 days, 78 days, 88 days and 96 days during the Track Record Period. Before 2005, the customers normally settled their outstanding amount of sales upon the time of delivery. Since 2005, in order to encourage farmers to fully utilise drip products and increase the Group's market share, the Group offered favourable payment terms to customers with good reputations, according to which they could first pay 30% of the goods' value for their purchase in autumn. The remaining balance will be paid at various time-intervals such as (i) upon delivery of the goods, (ii) upon completion of installation in the next spring and (iii) at the end of the warranty period. Therefore, the customers took the advantage of favourable payment terms and more customers selected to use the favourable payment terms. Consequently, the favourable payment terms to customers by the Group leads to the increase of the debtors' turnover period during the Track Record Period. Meanwhile, the cycle for agricultural market starts from autumn each year to autumn of next year, which is different from the Group's normal financial year, thus this results a slightly longer turnover days of trade receivables.

As at the Latest Practicable Date, subsequent settlement of the Group's trade receivables as at 30th June, 2007 amounted to approximately RMB43,240,000.

Other receivables and prepayments

Other receivables and prepayments mainly comprised advance for raw material purchase, initial public offering intermediary expenses, bid deposits, staff advances and other tax receivables. As of 31st December, 2004, 31st December, 2005, 31st December, 2006 and 30th June, 2007, the Group had other receivables and prepayments amounted to approximately RMB15.2 million, RMB24.0 million, RMB26.9 million and RMB22.2 million, respectively, whilst the staff advance as at the respective date amounted to approximately RMB3.5 million, RMB1.7 million, RMB7.0 million and RMB5.3 million, respectively and the IPO intermediary as at 31st December, 2004 and 31st December, 2005 amounted to approximately RMB5.5 million and RMB11.2, respectively.

The increase in other receivables and prepayments of approximately 12.1% as at 31st December, 2006 in comparison with that of 31st December, 2005 was mainly due to the increase in staff advances while the increase in other receivables and prepayments as at 31st December, 2005 as compared with that of 31st December, 2004 was mainly caused by the increase in expenses for the preparation of the Company's listing on GEM.

The decrease in other receivables and prepayments of approximately 17.5% as at 30th June, 2007 as compared with that of 31st December, 2006 was mainly caused by the increase in advance for raw material purchase and expenses for the preparation of the Company's listing on Main Board which was offset by a decrease in bid deposits, staff advance and other tax receivable, resulted in an overall decrease in other receivables and prepayments by approximately RMB4,755,000 as compared with that of 31st December, 2006.

Trade payables

As of 31st December, 2004, 31st December, 2005, 31st December, 2006 and 30th June, 2007, the Group had trade payables amounted to approximately RMB38.2 million, RMB27.9 million, RMB46.6 million and 83.9 million, respectively, whilst cost of sales for the respective periods amounted to approximately RMB308.9 million, RMB280.4 million, RMB366.6 million and RMB243.6 million, respectively. The significant increase in trade payables of approximately 80.0% as at 30th June, 2007 in comparison with that as at 31st December, 2006 was mainly due to the increase in demand for their raw materials during 2007. In response to the expected increase in demand, the Group has to maintain sufficient inventories which in turn increases the purchase of raw materials resulting in a corresponding increase in trade payable. The Group believes that maintaining a reasonable inventory level is necessary in order to meet the growth in turnover as the sales of the Company is highly seasonal and keeping adequate level of inventories is more costs effective for any sudden increase of sales demand within a short period. As of 31st December, 2004, 31st December, 2005, 31st December, 2006 and 30th June, 2007, approximately 97.1%, 89.5%, 92.0% and 86.1%, respectively, of trade payables aged within one year. Creditors' turnover periods (expressed as closing balances of trade payables for the year end over total cost of sales for the relevant year times number of days in the relevant year) were approximately 45 days, 36 days, 46 days and 62 days during the Track Record Period. The Directors confirmed that the credit periods granted to the Group normally ranged from 30 to 90 days.

During the year ended 31st December, 2006, the Group's customers requested one-year warranty period for drip assembles and assembles for drip system (such as power generator and water pump etc.) with payment upon expiry of the warranty period. The Group, accordingly, requested the suppliers of the abovementioned parts to extend the warranties for their products to one year. Consequently, the payment terms of such parts was extended to one year, that was, payment upon expiry of the warranty period. Therefore, the balance of trade payables and other payables increased accordingly.

Other payables and accruals

Other payables and accruals mainly comprised accrued staff cost, accrued utilities expenses, other tax payable, accrued transportation charges and others. As of 31st December, 2004, 31st December, 2005, 31st December, 2006 and 30th June, 2007, the Group had other payables and accruals amounted to approximately RMB13.4 million, RMB13.2 million, RMB11.4 million and RMB11.8 million, respectively, whilst accrued staff cost as at the respective date amounted to approximately RMB3.3 million, RMB2.6 million, RMB2.4 million and RMB3.8 million, respectively and the other tax payable as at 31st December, 2004 and 31st December, 2005 amounted to approximately RMB1.9 million and RMB3.4, respectively.

The decrease in other payables and accruals of approximately 13.6% as at 31st December, 2006 in comparison with that as at 31st December, 2005 was mainly due to the decrease in other tax payable while the decrease in other payables and accruals as at 31st December, 2005 as compared with that of 31st December, 2004 was mainly caused by decrease in accrued staff cost and an increase in other tax payable.

The increase in other payables and accruals of approximately 3.5% as at 30th June, 2007 as compared with that of 31st December, 2006 was mainly due to the increase in accrued staff cost and accrued transportation charges and a decrease in accrued utility expenses.

Government grants

The government grants provided to the Group were designated for the development of two specific projects. During the Track Period, these projects were in progress and the related expenses incurred in relation to these projects were capitalised as property, plant and equipment. During the year ended 31st December, 2003, the Group received government grants of RMB900,000 for the Company's development of certain water saving irrigation system and equipment. Save as disclosed, no other government grants were received by the Group during the Track Record Period. The two projects are "development and application of new system of underground drip film" and "semi-trial of connectors for pipes". The projects had been completed in March 2006 and May 2006. The amounts of the equipment expenses were amounting to approximately RMB320,000 and RMB680,000, respectively.

Upon completion of these projects, verification reports will be submitted to the government for approval and the grants will become unconditional when the government approval is obtained. No other contingencies are attached to such grants.

Amounts due from or due to Tianye Holdings Group

As at 31st December, 2004, 31st December, 2005, 31st December, 2006 and 30th June, 2007, amount due from Tianye Holdings Group amounted to approximately RMB6.1 million, RMB4.8 million, nil and nil, respectively, while amount due to Tianye Holdings Group amounted to approximately RMB13.9 million, RMB1.3 million, RMB0.5 million and RMB10.3 million respectively.

The terms of the above non-trade receivables as at 31st December, 2004 are unsecured and have no fixed terms of repayment. The non-trade balance due to Tianye Holdings Group carried interest at 120% of the standard annual rate offered by The People's Bank of China. The amount was fully repaid during the year 2005.

To enhance the capital management within the Group, Tianye Holdings Group has established the Tianye Holdings Group Settlement Centre (the "**Settlement Centre**") to regulate the working capital of the Group and provide capital support to the subsidiaries of Tianye Holdings. The Settlement Centre does not function as a profit-making centre. Interest bearing amount due from Tianye Holding Group carries interest at the standard annual rate effected by the PBOC. Interest bearing amount due to Tianye Holdings Group carries interest at 120% of the standard annual rate offered by the PBOC. The Group paid higher interests to Tianye Holdings Group during the Track Record Period because the loans offered by Tianye Holding Group bear different interest rates for short, medium and long-term loans. The medium and long-term loans bear higher interest rates. The interests charged to the Group was based on 1-year short-term loan and therefore, a premium over the standard annual rate offered by the PBOC was charged for Tianye Holdings Group to maintain its cost.

The Group's deposits with the Settlement Centre were short-term deposits. The interests paid by the Settlement Centre were based on standard rate per annum similar to that for demand deposits with commercial banks. Hence, the Group considered it is reasonable to deposit its working capital at the Settlement Centre. As at the Latest Practicable Date, non-trade receivables and payables due from/to Tianye Holdings Group have been fully settled.

The PRC legal advisers of the Company is concerned that the funding activities between the Group and Tianye Company violated the Rule 61 of the General Principles Regarding Providing Facility and POBC can implement administrative punishment on the companies in accordance with Rule 73 of the General Principles Regarding Providing Facility. Pursuant to the Administrative Punishment Law of the PRC (《中華人民共和國行政處罰法》) ("**Administrative Punishment Law**") that came into effect on 1st October, 1996, administrative punishment implemented by administrative bodies should follow the relevant requirements of the Administrative Punishment Law. According to Rule 27 of the Administrative Punishment Law, administrative punishment is not necessary if the violation is minor and is rectified immediately without causing harmful consequences. Since the funds used between the Group and Tianye Company have been repaid in full, there were no actual or potential legal disputes. As such, the PRC legal advisers of the Company opined that the violations of departmental regulations were minor and were immediately rectified without causing any harmful consequences and that such acts did not constitute a material reason for administrative punishment, so POBC would not implement administrative punishment on the companies.

The Group has enhanced its corporate governance by appointing independent non-executive Directors and hired a financial controller to implement and monitor the internal control procedures of the Group for ensuring the compliance of the relevant laws and regulations with regard to the borrowings.

Since the Company's listing on the GEM up to the Latest Practicable Date, the Directors have confirmed that save and except the borrowings which are in compliance with the relevant laws and regulations in the PRC and other jurisdictions, where applicable, the Group has not and will not borrow from corporations other than the financial institutions in the PRC. Also, the Group has not and will not engage in lending activities that are not permitted under the relevant laws and regulations in the PRC.

Trade receivables from Tianye Holdings Group as at 31st December, 2004, 31st December, 2005, 31st December, 2006 and 30th June, 2007 amounted to approximately RMB479,000, RMB4,846,000, nil and nil, respectively. All of these balances aged within one year from the respective balance sheet dates and were unsecured, interest free and has no fixed repayment terms and the year-to-year fluctuations is resulted from the volume of transaction and the amount of repayment occurred during the period.

Trade payables to Tianye Holdings Group as at 31st December, 2004, 31st December, 2005, 31st December, 2006 and 30th June, 2007 amounted to approximately RMB9,933,000, RMB1,302,000, RMB517,000 and RMB10,313,000, respectively. All of these balances aged within one year from the respective balance sheet dates and were unsecured, interest free and has no fixed repayment terms and the year-to-year fluctuations is resulted from the volume of transaction and the amount of repayment occurred during the period.

According to the PRC legal adviser to the Company, the trade receivables and trade payables with Tianye Holdings Group during the Track Record Period were arisen in the ordinary and usual course of business of the Group and does not breach of any prevailing PRC laws and regulations.

PROPERTY INTERESTS

The text of the letter prepared by Castores Magi (Hong Kong) Limited, an independent property valuer, the summary of values and the valuation certificate of the property interests owned and leased by the Group are as set out in Appendix II to this document. The property interests attributable to the Group were valued as at 31st July, 2007 at HK$31,929,040 by Castores Magi (Hong Kong) Limited. Please refer to Appendix II to this document for further details.

DIVIDEND POLICY

The holders of the H Shares will share proportionately, on a per Share basis, all dividends and other distributions declared by the Board. For holders of the H Shares, cash dividend payments, if any, shall be declared by the Board in RMB and paid in HK dollars. If the Company does not have sufficient foreign exchange reserves to pay dividends in HK dollars, it intends to exchange the required HK dollars from authorised banks in the PRC or through other legal means.

A final dividend for the year ended 31st December, 2004 of RMB0.110 per share, amounting to RMB34,883,372 in aggregate, was declared on 15th April, 2005, RMB29,357,000 of which was paid to the shareholders of the Company during the year ended 31st December, 2005 and the remaining amount of RMB5,526,372 was paid to the shareholders of the Company during the year ended to 31st December, 2006.

A final dividend for the year ended 31st December, 2005 of RMB0.0671 per share, amounting to RMB34,859,897 in aggregate, has been declared and paid to the shareholders of the Company during the year ended 31st December, 2006.

A final dividend for the year ended 31st December, 2006 of RMB0.036 per share, amounting to RMB18,702,776 in aggregate, has been declared and paid to the Shareholders before 29th June, 2007.

The payment of any dividend by the Company must be recommended by the Board and approved by the Shareholders in the Shareholders' meeting. The decision to make a recommendation for the payment of any dividend and the amount of the dividend will depend on:

- the Company's results of operations and cash flows;
- the Company's financial position;
- the Company's shareholders' interests;
- general business conditions;
- the Company's future prospectus;
- statutory and regulatory restrictions on the payment of dividends by the Company; and
- other factors that the Board deems relevant.

In accordance with applicable requirements of the Company Law, the PRC legal advisers of the Company have confirmed that the Group may only distribute dividends after it has made allowance for:

- compensation of losses, if any;
- allocation to the statutory reserve fund; and
- allocation to a discretionary reserve fund if approved by the shareholders and after allocation is made to the statutory reserve fund.

The minimum aggregate allocation to the statutory reserve fund is 10% of the Group's net profit determined in accordance with PRC GAAP. Under the applicable PRC laws, the Group's distributable earnings will be equal to its profit, as determined in accordance with PRC GAAP or HKFRS, whichever is lower, less allocations to the statutory reserves. If the Group records no net profit for a particular financial year, it may not normally distribute dividends for such financial year.

TAXATION

During the Track Record Period, pursuant to the relevant laws and regulations in the PRC, the Company and its subsidiaries were subject to PRC Enterprise Income Tax ("EIT") of 33%. Pursuant to "Notice of Problem on Certain Incentives Policy on the Development of Western China" Cai Shui Zi [2001] No. 202 ("Notice No. 202") (財稅字[2001] 202號《關於西部大開發稅收優惠政策問題的通知》), for an entity operated in the western part of the PRC which is mainly engaged in the business prescribed in "Industries currently encouraged to be developed by the State, Technical Catalog of Products (2000 Revision)" (《當前國家重點鼓勵發展的產業、產品和技術目錄(2000年修訂)》) and that such business contributes to over 70% of its operating income (the "Prescribed Business"), such entity is entitled to specific tax relief.

New corporate income tax law

During the 5th Session of the 10th National People's Congress, which was concluded on 16th March, 2007, the PRC Corporate Income Tax Law ("New Corporate Income Tax Law") was approved and will become effective on 1 January 2008.

Pursuant to the New Corporate Income Tax Law, the enterprise income tax rate of an enterprise, whether domestic or foreign invested, will be 25%. An enterprise currently enjoying periodic tax holiday may go on enjoying the tax holiday until it expires. The enterprise will have an income tax rate of 25% after expiry of such tax holiday. Upon the expiry of existing preferential tax treatments of the Company, Gansu Tianye and Hami Tianye, according to the New Corporate Income Tax Law, the respective income tax rate for each of the abovementioned entities will be 25%. At the same time, the income tax rate of each of Tianye Recycling, Tianye Installation, Alaer Tiannong, Zhaoqing Tianye, Kuitun Tiantun and Hami Huimin, as the current income tax rate for each of them is 33%, will be 25% after the implementation of the New Corporate Income Tax Law. The New Corporate Income Tax Law meanwhile indicates the State Council may issue related enforcement regulations.

Other than Tianye Installation which business is not regarded as Prescribed Business, the entities comprising the Group satisfied these requirements and, on the assumptions that they will continue to meet these requirements in the relevant periods, these entities were entitled to certain tax relief as follows:

Name of entity	*Notes*	**2004**	**2005**	**2006**	**June 2007**
The Company	(i)	15%	15%	15%	Exempted
Tianye Recycling	(ii)	Exempted	Exempted	33%	33%
Gansu Tianye	(iii)	15%	15%	15%	Exempted
Tianye Installation		33%	33%	33%	33%
Alaer Tiannong	(iv)	Exempted	Exempted	33%	33%
Hami Tianye	(v)	15%	15%	15%	15%
Zhaoqing Tianye	(vi)	N/A	N/A	33%	33%
Kuitun Tiantun	(vii)	N/A	N/A	33%	33%
Hami Huimin		N/A	N/A	N/A	33%

Notes:

(i) Pursuant to "Notice of EIT on Certain Incentives Policy", Cai Shui Zi [1994] No. 1 (財稅字[1994]1號《關於企業所得稅若干優惠政策的通知》), issued by the Ministry of Finance (財政部) and the State Administration of Taxation (國家稅務總局), "EIT Exemption Management Method of State Administration of Taxation of Xinjiang Uygur Autonomous Region", Xin Guo Shui Fa [1999] No. 120 (新國稅發[1999]120號《新疆維吾爾自治區》國家稅務局企業所得稅減免稅管理辦法), "Approval of Exemption from EIT regarding Xinjiang Shihezi Tianye Water Saving Equipment Development Company Limited", Xin Guo Shui Ban [2001] No. 177 (新國稅辦[2001]77號《關於新疆石河子天業節水器具開發有限公司免徵企業所得稅的批覆》), issued by the State Administration of Taxation of Xinjiang Uygur Autonomous Region (新疆維吾爾自治區國家稅務局), Notice No. 202, "Notice of Adjustment of Level of Authorities in Approval of EIT Exemption and Related Issues", Xin Guo Shui Han [2003] No. 134 (新國稅函[2003]134號《關於調整企業所得稅減免稅審批權限及有關問題的通知》), issued by the State Administration of Taxation of Xinjiang Uygur Autonomous Region (新疆維吾爾自治區國家稅務局) and "Approval Document of Exemption from EIT regarding Xinjiang Tianye Water Saving Irrigation System Company Limited", Shi Guo

Shui Ban [2004] No. 118 (石國税辦[2004]118號《關於新疆天業節水灌溉股份有限公司減徵企業所得税的批覆》), issued by the State Administration of Taxation of Shihezi (石河子國家税務局[2004] 118號), the Company was granted a reduced EIT tax rate of 15% for the seven years ending 31st December, 2010;

Pursuant to "The Provisional Measures on the Relief of Enterprise Income Tax Owing to the Investment in Domestic Equipment Used for Technological Reform" (《技術改造國產設備投資抵免企業所得税暫行辦法》) issued by the Ministry of Finance (財政部) and the State Administration of Taxation (國家税務總局) in 1999, "The Audit Management Measures on the Relief of Enterprise Income Tax Owing to the Investment in Domestic Equipment Used for Technological Reform", (Guo Shui Fa [2000] No. 13) (《技術改造國產設備投資抵免企業所得税審核管理辦法》(國税發[2000]13號)) issued by the State Administration of Taxation (國家税務總局), and approved by the State Tax Bureau of Shihezi in July 2006, the Company can enjoy a reduction of income tax amounting to approximately RMB16,668,000 after the installation of the machineries locally purchased in 2004. The Company has utilised such deduction to offset against the income tax provision for the year ended 31st December, 2006 amounting to approximately RMB9,539,000.

Pursuant to "Approval Notice of Exemption from EIT regarding Xinjiang Tianye Water Saving Irrigation System Company Limited", Kai Guo Shui Ban [2006] No. 72 (開國税辦[2006]72號《關於新疆天業節水灌溉股份有限公司減免企業所得税的通知》), issued by the State Administration of Taxation of Shihezi Economic and Technological Development Zone, Shihezi (石河子經濟技術開發區國家税務局), the Company is exempted from EIT for the two years ending 31st December, 2008 and was granted a 50% reduction in EIT for the period from 1st January, 2009 to 31st December, 2011;

(ii) Pursuant to "Approval of EIT Exemption for the Administration of Taxation of the Eight Enterprises of Shihezi Suburb from the State Administration of Taxation of Shihezi", Shi Guo Shui Ban [2004] No. 59 (石國税辦[2004]59號《石河子國家税務局關於對石河子城區國家税務局八戶企業減免企業所得税的批覆》), Tianye Recycling is exempted from EIT for the two years ended 31st December, 2005. Accordingly, Tianye Recycling is subjected to a EIT tax rate of 33% commencing from 1st January, 2006;

(iii) Pursuant to Notice No. 202 and Approval Application Document [2002] No. 44 issued by the State Administration of Taxation of Gansu Province (甘肅國家税務局[2002]44號批文), Gansu Tianye was granted a reduced EIT tax rate of 15% for the period from 1st January, 2002 to 31st December, 2010.

Pursuant to the "Provisional Regulations for Investments in PRC by Enterprises with Foreign Investment" (《關於外商投資企業境內投資的暫行規定》), "Approval Notice for the Transaction of Taxation Issue related to Enterprise Income Tax from State Tax Bureau of Ganzhou District" (Gan Qu Kuo Shui Fi Zi [2007] No. 001 (《甘州區國税局企業所得税務處理事項批復通知書》), (甘區國税批字[2007]001號) Gansu Tianye is exempted from EIT during the period from April 2007 to December 2007.

(iv) According to "Approval of EIT Exemption to Xinjiang Alaer Tiannong Water Saving Irrigation Company Limited", A Ke Su Shi Guo Shui [2003] No. 400 ([2003]400號《關於對新疆阿拉爾天農節水灌溉有限責任公司免徵企業所得税的批覆》阿克蘇市國税[2003] 400號), issued by State Administration of Taxation of Akesu (阿克蘇市國家税務局), Alaer Tiannong was exempted from EIT for the three years ended 31st December, 2005. Accordingly, Alaer Tiannong is subjected to a EIT tax rate of 33% commencing from 1st January, 2006;

(v) Pursuant to "Approval of EIT Exemption of State Administration of Taxation of Hami Region to Hami Tianye Hongxing Water Saving Irrigation Company Limited", Ha Guo Shui Ban [2005] No. 32 (哈國税辦[2005]32號《哈密地區國家税務局關於對哈密《哈密天業紅星節水灌溉有限責任公司減徵企業所得税的批覆》) issued by State Administration of Taxation of Hami Region (哈密地區國家税務局) on 28th January, 2005, Hami Tianye was granted a reduced EIT tax rate of 15% for the period from 1st January, 2004 to 31st December, 2007;

(vi) Zhaoqing Tianye is not entitled to any exemption from EIT as it is not complying with the requirements setting out in "Notice of Problem on Certain Incentives Policy on the Development of Western China" Cai Shui Zi [2001] No. 202 ("Notice No. 202") (財税字[2001] 202號《關於西部大開發税收》優惠政策問題的通知》);

(vii) According to "Notice of Problem on Certain Incentives Policy on the Development of Western China" Cai Shui Zi [2001] No. 202 ("Notice No. 202") (財稅字[2001] 202號《關於西部大開發稅收》優惠政策問題的通知》), Kuntun Tiantun was applying for a reduction of EIT tax rate for the period from 2007 to 2009. As at the Latest Practicable Date, the Group is in the process of applying for the exemption; and

(viii) According to the legal adviser to the Company, the Company and its subsidiaries have complied with the requirements of relevant PRC laws and regulations at the times when they lodge the tax returns to relevant authorities of the PRC and are not breach of any prevailing PRC laws and regulations and are not subject to any penalty.

The EIT for the year ended 31st December, 2006 is calculated at the EIT rate applicable to each of the entities comprising the Group as shown above.

The Group is not subject to Hong Kong profits tax as the Group's income neither arises in, nor is derived from, Hong Kong.

During each of the three years ended 31st December, 2006 and the six months ended 30th June, 2007, the total tax (credit)/charge by the Group amounted to approximately RMB7,951,000, RMB7,595,000, RMB(824,000) and RMB183,000, respectively, with an effective tax rate of approximately 15.28%, 12.13%, (1.39)% and 0.57%, respectively, in the relevant periods.

The lowered effective tax rate for the financial year ended 31st December, 2006 was mainly attributable to (i) the reduction of income tax in respect of the tax benefit on locally purchased machinery; (ii) effect of the tax exemption and reduction granted to the Group; and (iii) the over-provision of tax in year 2005 as a result of accreditation and implementation of performance linked payroll system by the Company in year 2005.

The lowered effective tax rate for six months ended 30th June, 2007 of 0.57% was mainly attributable to the grant of income tax exemption to the Company and Gansu Tianye in April 2007.

DISTRIBUTABLE RESERVE

The Company's reserve available for distribution to the Shareholders as at 30th June, 2007 prepared in accordance with PRC regulations amounted to RMB76,686,000 and pursuant to PRC laws and regulations, it represented the accumulated profits of the Company after appropriation to reserves. Details of the Company's accumulated profits of RMB70,590,000 as at 30th June, 2007 prepared under HKFRS are set out in note 28 under the paragraph headed "Notes to the Financial Information" in the accountants' report of the Group set out in Appendix I to this document.

Pursuant to relevant rules and regulations in the PRC, the Company's reserves available for distribution shall be the lower of the accumulated profits after appropriation to reserves as stated in the PRC statutory financial statements and the financial statements prepared under HKFRS.

NET TANGIBLE ASSETS

The following statement shows the Group's net tangible assets as at 30th June, 2007 shown in the accountants' report of the Group set out in Appendix I to this document.

	RMB'000
Audited net tangible assets of the Group attributable to equity holders of the Company as at 30th June, 2007 *(Note 1)*	632,044
Audited net tangible asset value per Share *(Note 2)*	RMB1.22

Notes:

1. The audited net tangible assets of the Group attributable to equity holders of the Company as at 30th June, 2007 is based on the accountants' report set out in Appendix I to this document, net of goodwill of approximately RMB98,000.

2. The net tangible asset value per Share has been arrived at based on the 519,521,560 Shares in issue as at the date of this document as if such Shares were outstanding throughout the financial period ended 30th June, 2007.

NO MATERIAL ADVERSE CHANGE

The Directors confirm that there has been no material adverse change in the financial or trading position of the Group since 30th June, 2007 (being the date to which the latest audited financial statements of the Group were made up).