

MANAGEMENT DISCUSSION AND ANALYSIS

Financial review

For the six months ended 30 June 2002, the Group's turnover amounted to HK\$557.5 million, increased by 72.5% over the same period last year. The growth in turnover was a result from the increase in both sales volume and average selling price. During the period, sales volume was up 62.4% from 273,164 tonnes (2.7 million hl) in 2001 to 443,713 tonnes (4.4 million hl) in 2002, while the average price per tonne (average price per hl) rose 6.2% from HK\$1,183 per tonne (HK\$119.7 per hl) in 2001 to HK\$1,256 per tonne (HK\$127.1 per hl) in 2002.

For the six months ended 30 June 2002, the three breweries acquired by the Group in June 2001 ("2001 Acquired Breweries") recorded a net profit of HK\$7.7 million. This is a significant turnaround from an unaudited loss of approximately HK\$6.9 million for the same period last year. This demonstrated the Group's continued success in enhancing the operating efficiencies of the 2001 Acquired Breweries. For the six months ended 30 June 2002, the Group achieved a strong gross profit amounting to HK\$237.3 million with a growth of 48.5% by comparing with the same period in 2001. The Group's overall gross margin for the first six months ended 2002 and the same period last year were 43% and 49% respectively. Gross margin for the HB Company (5 existing breweries prior to the acquisition of 2001 Acquired Breweries), which were at 47% for the six months ended 30 June 2002 by comparing with 50% in the same period last year, slightly decreased due to a change of product mix during the periods.

Despite this, the Group's strong capability in turning around loss operations to profitable ones with higher gross margins was once again well demonstrated, enabling the Group to maintain its high level of gross profit margin. The Group's 2001 Acquired Breweries recorded gross margin at 20% prior to the acquisition in June 2001, and the margin were tremendously improved to 33% for the six months ended 30 June 2002 after the Group's management taking office in the Acquired Breweries in 2001.

For the six months ended 30 June 2002, profit from operating activities amounted to HK\$107.4 million, increased by 68.4% over the same period last year. This growth was mainly attributable to the increase in sales volume and effective control of operating costs. Net profit attributable to shareholders for the six months ended 30 June 2002 was HK\$54.3 million, representing an increase of 39.9% from that of last year.

The improved financial performance has set the ground for a solid financial standing of the Group. The Group's cash position was also greatly improved with net proceeds of HK\$288.7 million raised from its share offer after listing on the Stock Exchange on 27 June 2002. Subsequent to the interim period, on 15 July 2002, the Group raised net proceeds of HK\$49.4 million by exercising the Over-allotment Option referred to in the Prospectus. This further enhances the Group's cash position.

The debt to equity ratio of the Group was 106% as at 30 June 2002, greatly improved from 226% as at 31 December 2001. The net debt to equity ratio of the Group was 60% as at 30 June 2002. The management expects that the Group's debt to equity ratio will be further improved in the second half of 2002 after repaying part of its debts from its operating income and from the proceeds raised from its share offer.

Business review

In order to better facilitate the integration of and co-ordination with various breweries and different functional units, the Group has developed a centrally co-ordinated, process-based management model to enhance the operation processes and resources deployment. As the model has been synergistically implemented in the existing breweries, and successfully improved the efficiencies and operating results of the newly acquired or established breweries within a relatively short period of time, the Group will apply this to the other breweries that the Group may acquire as it expands into other regions in the PRC to facilitate its scaleable business model.

(i) ***Turnover analysis by product category***

The Group's products are divided into three categories: Original, Classic and Premium, targeting at the mass, middle-income and premium markets respectively. The products are packaged in glass bottles, aluminum cans and kegs in the form of processed beer and draught beer.

The sale of Original products remained to be the Group's major income source, representing 75% of the total turnover for the six months ended 30 June 2002. Turnover of Original products increased by 64% from approximately HK\$249.7 million in the corresponding period of 2001 to HK\$411.5 million.

For the six months ended 30 June 2002, the sale of Classic products continued its growing trend, amounting to 16% of the total turnover. Its contribution to the total turnover in the corresponding period last year was 13%. Turnover from Classic products increased from approximately HK\$41 million to approximately HK\$89.3 million, representing a growth of 117.8%.

Turnover derived from the sale of Premium products accounted for 9% of the total turnover for the six months ended 30 June 2002, as compared to 10% of the total turnover in the corresponding period in 2001. Turnover increased 45.8% from approximately HK\$32.5 million in the same period of 2001 to approximately HK\$47.4 million. The Group will continue to maintain its presence in the premium market segment.

(ii) ***Turnover analysis by geographical location***

The Group's products were mainly sold to the Northeast Region, accounting for 94% of the total turnover for the six months ended 30 June 2002. Turnover from the Northeast Region amounted to HK\$516.6 million, an increase of 63% from HK\$316.7 million in the same period last year. Heilongjiang Province remained to be the single largest market of the Group, contributing 69% of the Group's turnover. The Group's market penetration in the rest of Northeast Region continued to increase with a growth rate of 157% compared with the same period last year, contributing 25.3% of the total turnover this year as compared with 17% during the same period in 2001.

5.7% of the Group's turnover for the six months ended 30 June 2002 was generated from sales in non-Northeast Region and overseas. Its contribution to the Group's turnover increased by 381% compared with the same period last year.

(iii) ***Production operations***

The Group has adopted a growth strategy through acquiring and developing brewing operations since 1996 to expand its production capacity and strengthen its market share in the Northeast Region.

The production volume of the Group for the six months ended 30 June 2001 reached 273,163 tonnes (approximately 2.7 million hl), and the volume jumped over 62.4% to achieve 443,713 tonnes (approximately 4.4 million hl) for the first six months in 2002, leveraging the increase in aggregate production capacity of the 2001 Acquired Breweries. The utilisation rate of all breweries under the reviewing period was at 94.4%.

(iv) ***Marketing strategy***

In the belief of a “Single-megabrand Strategy”, the Group is promoting “Harbin” as the brand of “the oldest brewery in China” providing high quality products. The Group’s marketing objective is to build up its brand as a nation-wide brand in the PRC beer market. An integrated marketing strategy has been put in place, which covers brand building strategy, product mix management, pricing policy and distribution network establishment.

Prospects

To sustain future business growth, the Group will continue to seek acquisition opportunities to synergistically enlarge its production scale, establish a stronger distribution network both in the Northeast Region and other regions in China and to adjust its product mix for higher profits. The Group's proven success in turning around loss operations and improving profitability of the acquired breweries demonstrated that the Group is able to effectively integrate acquired businesses into its existing operations.

In addition, the implementation of an Enterprise Resources Planning ("ERP") system and continued application of the centrally co-ordinated, process-based management model will be instrumental to reengineer brewery operations for optimal resources deployment, higher revenue and profit, and more efficient communications.

The Group will also formulate its long-term strategic plan to strengthen communications and to explore possible co-operation opportunities with world renowned brewery groups.

Looking forward, the Group's objective is to increase market share and profitability in order to become a leading brewery group in the PRC. China's beer industry is currently undergoing consolidation where small and inefficient breweries are gradually being driven out of the market. The Group is well positioned to capture the rising opportunities from the current market consolidation in the PRC. Furthermore, the Group targets at fully utilising its production capacity in order to meet the increasing demand of the new and existing markets.

In view of the momentum on market demand and the progress on corporate reengineering and cost control measures, the Group is optimistic on the operating results for the full year of 2002, and is confident in bringing satisfactory returns to shareholders.

Use of net proceeds from the New Issue

The net proceeds from the share offer of the Company's listing on the Stock Exchange on 27 June 2002 amounted to approximately HK\$288.7 million. At the date of this announcement, the Group has utilised a total of approximately HK\$191 million of the proceeds. Approximately HK\$70 million, HK\$64.6 million, HK\$48.5 million and HK\$7.9 million have been applied towards the acquisition, the repayment of bank loan, the repayment of shareholders' loan and as general working capital, respectively. The remaining proceeds are placed on short-term deposits with licensed banks in Hong Kong.

On 15 July 2002, the Company raised net proceeds of approximately HK\$49.4 million by exercising the Over-allotment Option referred to in the Prospectus. At the date of this announcement, the proceeds have not been utilised and are placed on short-term deposits with licensed banks in Hong Kong.

Number and remuneration of employees

The Group employs a total of approximately 4,979 full time employees in Hong Kong and PRC. The Group recognises the importance of its human resources to its success. Remuneration is maintained at competitive levels with discretionary bonuses payable on a merit basis and in line with industry practice. Other staff benefits provided by the Group include mandatory provident fund, insurance schemes and performance related commissions.