CHINA MENGNIU DAIRY COMPANY LIMITED

(Incorporated in the Cayman Islands with limited liability)
(Stock Code: 2319)

ANNUAL RESULTS ANNOUNCEMENT FOR THE YEAR ENDED 31 DECEMBER 2005

FINANCIAL HIGHLIGHTS

	2005	**2004**	**Changes**
	RMB'000	*RMB'000*	
Revenue	10,824,950	7,213,827	+50.1%
Net profit attributable to equity holders of the Company	456,847	319,393	+43.0%
Net cash from operating activities	1,328,297	572,317	+132.1%
Earnings per share (RMB)			
– Basic	0.365	0.357	+2.2%
– Diluted	0.334	0.285	+17.2%
Proposed final dividend per share (RMB)	0.0686	0.0585	+17.3%

- Revenue surged 50.1% to RMB10,825.0 million as a result of successful brand building and market penetration strategies. According to ACNielsen survey, by sales volume, the Group's market share in the China liquid milk market, excluding milk beverages and yogurt, increased by 6.6 percentage points from 22.0% in December 2004 to 28.6% in December 2005.
- Net profit attributable to equity holders of the Company was up by 43.0% to RMB456.8 million.
- Net cash from operating activities grew by 132.1% to RMB1,328.3 million.

The directors (the "Directors") of China Mengniu Dairy Company Limited (the "Company") are pleased to announce the audited results of the Company and its subsidiaries (the "Group") for the year ended 31 December 2005.

CONSOLIDATED INCOME STATEMENT
For the year ended 31 December 2005

	Notes	2005 RMB'000	2004 RMB'000
REVENUE	3	10,824,950	7,213,827
Cost of sales		(8,411,745)	(5,607,363)
GROSS PROFIT		2,413,205	1,606,464
Other income		24,967	13,138
Selling and distribution costs		(1,494,970)	(1,039,282)
Administrative expenses		(267,817)	(136,662)
Other operating expenses		(23,897)	(4,040)
PROFIT FROM OPERATING ACTIVITIES	4	651,488	439,618
Interest income		12,898	10,346
Finance costs	5	(43,956)	(39,432)
Share of (losses)/profits of associates		(3,295)	21
PROFIT BEFORE TAX		617,135	410,553
Income tax expense	6	(61,612)	(18,454)
NET PROFIT FOR THE YEAR		555,523	392,099
Attributable to:			
Equity holders of the Company		456,847	319,393
Minority interests		98,676	72,706
		555,523	392,099
DIVIDENDS			
Dividends paid	7	80,053	61,860
Proposed final dividends	7	93,873	80,053
EARNINGS PER SHARE ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY			
Basic	8	RMB0.365	RMB0.357
Diluted	8	RMB0.334	RMB0.285

CONSOLIDATED BALANCE SHEET
As at 31 December 2005

	Notes	2005 RMB'000	2004 RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment		3,140,433	2,227,528
Construction in progress		235,373	292,013
Land use rights		65,923	33,015
Interests in associates		18,700	20,578
Available-for-sale investments		8,029	3,409
Goodwill		115,549	115,549
		3,584,007	2,692,092
CURRENT ASSETS			
Inventories		781,001	714,799
Bills receivable	*9*	81,528	80,406
Trade receivables	*10*	174,657	179,163
Prepayments, deposits and other receivables		164,475	130,233
Pledged deposits		53,673	20,763
Cash and cash equivalents		1,247,764	1,018,928
		2,503,098	2,144,292
CURRENT LIABILITIES			
Trade and bills payables	*11*	1,117,005	694,597
Deferred income		4,145	4,145
Accruals and other payables		976,574	758,160
Interest-bearing bank loans		365,590	544,812
Other loans		23,600	22,600
Income tax payable		8,472	1,436
		2,495,386	2,025,750
NET CURRENT ASSETS		7,712	118,542
TOTAL ASSETS LESS CURRENT LIABILITIES		3,591,719	2,810,634
NON-CURRENT LIABILITIES			
Interest-bearing bank loans		445,702	239,500
Other loans		11,481	18,000
Long term payables		311,521	189,925
Deferred income		55,936	60,081
		824,640	507,506
NET ASSETS		2,767,079	2,303,128
EQUITY			
Equity attributable to equity holders of the Company			
Issued capital		145,573	118,138
Retained earnings		559,307	318,650
Other reserves		1,625,741	1,313,050
Convertible instrument		–	204,636
		2,330,621	1,954,474
Minority interests		436,458	348,654
TOTAL EQUITY		2,767,079	2,303,128

NOTES

1. **CORPORATE INFORMATION**

The Company was incorporated in the Cayman Islands on 16 February 2004 as an exempted company with limited liability. The Company is an investment holding company and its subsidiaries are engaged in the manufacture and distribution of dairy products in the People's Republic of China (the "PRC").

2.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs"). They are prepared on a historical cost basis, except for available-for-sale investments that have been measured at fair value. They are presented in Renminbi ("RMB") and all values are rounded to the nearest thousand (RMB'000) except when otherwise indicated.

Basis of consolidation

The consolidated financial statements comprise the financial statements of the Company and its subsidiaries (the "Group") for the year ended 31 December 2005. The financial statements of the subsidiaries are prepared for the same reporting year as the Company, using consistent accounting policies. All intra-group balances, transactions, income and expenses and profits and losses resulting from intra-group transactions that are recognised in assets, are eliminated in full. Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the day that such control ceases.

Minority interests represent the portion of profit and loss and net assets of the Company's subsidiaries not held by the Group and are presented separately in the consolidated income statement and within equity in the consolidated balance sheet, separately from the Company's shareholders' equity.

2.2 EFFECT OF ADOPTING NEW AND REVISED IFRSs

In 2005, the Group adopted the following new and revised IFRSs which are relevant to its operations and comparative amounts have been amended as required.

IAS 1	Presentation of Financial Statements
IAS 2	Inventories
IAS 8	Accounting Policies, Changes in Accounting Estimates and Errors
IAS 10	Events after the Balance Sheet Date
IAS 16	Property, Plant and Equipment
IAS 17	Leases
IAS 21	The Effects of Changes in Foreign Exchange Rates
IAS 24	Related Party Disclosures
IAS 27	Consolidated and Separate Financial Statements
IAS 28	Investments in Associates
IAS 32	Financial Instruments: Disclosure and Presentation
IAS 33	Earnings per Share
IAS 39	Financial Instruments: Recognition and Measurement
IFRS 2	Share-based Payment
IFRS 5	Non-current Assets Held for Sale and Discontinued Operations

The adoption of the above new and revised IFRSs did not result in substantial changes to the Group's accounting policies nor any significant financial impact on the Group. In summary:

– IAS 1 has affected the presentation of minority interests on the face of the consolidated balance sheet, consolidated income statement, consolidated statement of changes in equity and other disclosures. In addition, in prior periods, the Group's share of tax attributable to associates was presented as a component of the Group's total tax charge in the consolidated income statement. Upon the adoption of IAS 1, the Group's share of the results of associates is presented net of the Group's share of tax attributable to associates.

– The adoption of IASs 2, 8, 10, 16, 17, 24, 27, 28, 32, 33 and 39 has had no material effect on the Group's accounting policies.

– IAS 21 requires goodwill to be allocated to foreign operations and carried at that foreign operation's functional currency. Goodwill and fair value adjustments are translated at the closing rate. Such change has had no material effect on the Group but the wording of the accounting policy on foreign currency translation has been amended to align with the new wording adopted in the revised IAS 21.

– IFRS 2 requires the cost of share options and other share-based incentives to be expensed in the income statement when the Group receives goods or services as consideration. Although the Group's share option scheme was approved on 28 June 2005, no share options or other share-based incentives have been granted during the year. Therefore, the adoption of IFRS 2 has had no material effect on the Group.

– IFRS 5 requires those non-current assets held for sale to be presented separately in the balance sheet. Such assets are measured at the lower of carrying amount and fair value less costs to sell and are not depreciated. The adoption of IFRS 5 has had no material effect on the Group.

3. REVENUE AND SEGMENT INFORMATION

Revenue, being the turnover of the Group, represents the net invoiced value of goods sold, after allowances for goods returns and trade discounts, and after eliminations of all significant intra-group transactions.

Business segment

The Group's operating businesses are organised and managed separately according to the nature of the products. The following tables present revenue, results and certain asset and liability information for the Group's business segments for the year ended 31 December 2005.

	2005	**2004**
	RMB'000	*RMB'000*
Segment revenue		
Liquid milk	9,314,688	6,097,187
Ice cream	1,295,861	805,208
Other dairy products	214,401	311,432
	10,824,950	7,213,827
Segment results		
Liquid milk	637,292	414,265
Ice cream	80,492	53,821
Other dairy products	(623)	24,142
	717,161	492,228
Unallocated corporate expenses	(65,673)	(52,610)
Profit from operating activities	651,488	439,618
Interest income	12,898	10,346
Finance costs	(43,956)	(39,432)
Share of (losses)/profits of associates	(3,295)	21
Profit before tax	617,135	410,553
Income tax expense	(61,612)	(18,454)
Net profit for the year	555,523	392,099

	2005	2004
	RMB'000	*RMB'000*
Segment assets		
Liquid milk	4,274,241	3,566,647
Ice cream	886,902	585,881
Other dairy products	169,559	285,661
Unallocated corporate assets	1,226,247	808,970
Eliminations	(469,844)	(410,775)
Total assets	6,087,105	4,836,384
Segment liabilities		
Liquid milk	2,547,286	2,303,830
Ice cream	386,960	170,511
Other dairy products	67,239	161,876
Unallocated corporate liabilities	788,385	307,814
Eliminations	(469,844)	(410,775)
Total liabilities	3,320,026	2,533,256
Capital expenditure		
Liquid milk	739,821	764,715
Ice cream	246,915	252,653
Other dairy products	20,823	81,732
Others	38,294	65,341
	1,045,853	1,164,441
Depreciation		
Liquid milk	208,987	125,092
Ice cream	51,972	35,692
Other dairy products	5,713	1,628
Others	10,292	7,064
	276,964	169,476
Other non-cash expenses/(income)		
Liquid milk	(764)	3,040
Ice cream	219	910
Other dairy products	2,795	6,058
Others	(95)	377
	2,155	10,385

Geographical segment

Since the Group's revenue, expenses, results, assets and liabilities and capital expenditure were principally generated in the PRC, geographical segment analysis is not presented.

4. PROFIT FROM OPERATING ACTIVITIES

The Group's profit from operating activities is arrived at after charging/(crediting):

	2005	2004
	RMB'000	*RMB'000*
Cost of inventories sold	8,411,745	5,607,363
Employee benefits expenses (excluding directors' remuneration)		
– Wages, salaries and bonuses	380,277	248,809
– Retirement benefit contributions	10,050	3,459
	390,327	252,268
Depreciation on property, plant and equipment	276,964	169,476
Amortisation of land use rights	1,309	906
Research and development costs	6,291	7,428
(Write-back of)/provision for doubtful debts	(194)	4,113
Write-down of inventories to net realisable value	2,349	6,212
Minimum lease payments under operating leases on land and buildings	8,788	3,073
Display space leasing fees	60,886	38,597
Losses on disposal of items of property, plant and equipment	3,243	60
Auditors' remuneration	2,270	1,500
Foreign exchange differences, net	(5,733)	1,969

5. **FINANCE COSTS**

	2005	2004
	RMB'000	*RMB'000*
Interest on bank loans wholly repayable within five years	46,241	46,294
Less: Amounts capitalised	(2,285)	(6,862)
	43,956	39,432

The amounts capitalised are borrowing costs related to funds borrowed specifically for the purpose of obtaining qualifying assets. The interest rates on such capitalised borrowings during the year varied from 2.88% to 5.76% (2004: 2.88% to 5.76%) per annum.

6. **INCOME TAX EXPENSE**

Hong Kong profits tax has not been provided as the Group had no assessable profits arising in Hong Kong during the year. The tax charge represents the provision for PRC corporate income tax ("CIT") for the year.

Under PRC income tax law, except for certain preferential treatment available to fourteen (2004: six) of the Group's subsidiaries, the entities within the Group are subject to CIT at a rate of 33% on the taxable income as reported in their statutory accounts which are prepared in accordance with PRC accounting standards and financial regulations.

A reconciliation of the income tax expense applicable to profit before tax at the statutory income tax rate to income tax expense at the Group's effective income tax rate for the year is as follows:

		2005	2004
	Note	*RMB'000*	*RMB'000*
Profit before tax		617,135	410,553
At PRC CIT rate of 33%		203,655	135,482
Non-deductible/(taxable) items and others, net		22,685	(188)
Effect on tax exemption	*(1)*	(164,728)	(116,840)
At effective income tax rate of 10.0% (2004: 4.5%)		61,612	18,454

(1) Fourteen (2004: six) subsidiaries were subject to tax exemption in 2005. The profit subject to tax exemption in respect of these subsidiaries amounted to approximately RMB499,176,000 (2004: RMB354,060,000) in aggregate. Out of the fourteen subsidiaries, seven (2004: five) subsidiaries were granted tax exemption by the state tax bureau in accordance with the "Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises" under which these subsidiaries would be exempted from CIT for the first two profitable years and subject to 50% of the applicable tax rate for the following three profitable years. The remaining seven (2004: one) subsidiaries were granted tax exemption by the local tax bureau in accordance with the policy of "The Notice of Income Tax Exemption for the Country's Key Enterprises in Agricultural Industries" of the tax authorities.

(2) The share of tax attributable to associates amounting to approximately RMB1,687,000 (2004: RMB11,000) is included in the share of (losses)/ profits of associates on the face of the consolidated income statement.

7. **DIVIDENDS**

		2005	2004
	Note	*RMB'000*	*RMB'000*
Declared and paid during the year			
Equity dividends on ordinary shares		80,053	61,860
Proposed for approval at AGM			
Equity dividends on ordinary shares			
Proposed final – RMB0.0686 (2004: RMB0.0585) per ordinary share	*(1)*	93,873	64,966
Interest on convertible instrument		–	15,087
		93,873	80,053

(1) The proposed final dividend for the year is subject to the approval of the Company's shareholders at the forthcoming Annual General Meeting ("AGM"). Such dividend is not recognised as a liability in the consolidated financial statements as at 31 December 2005 but will be reflected as an appropriation of retained earnings for the year ending 31 December 2006.

8. **EARNINGS PER SHARE**

The calculation of basic earnings per share for the year is based on the net profit for the year attributable to ordinary equity holders of the Company of RMB456,847,000 (2004: RMB319,393,000) and the weighted average number of 1,251,129,000 (2004: 893,965,000) ordinary shares in issue during the year.

The weighted average number of shares used to calculate the basic earnings per share for the year ended 31 December 2005 includes approximately 257,891,000 ordinary shares issued upon conversion of the convertible instrument on 16 June 2005. The weighted average number of shares used to calculate the basic earnings per share for the year ended 31 December 2004 included 250,000,000 ordinary shares issued upon the listing of the Company's shares on The Stock Exchange of Hong Kong Limited ("Hong Kong Stock Exchange") on 10 June 2004 and approximately 110,525,000 ordinary shares issued upon conversion of the convertible instrument on 20 December 2004.

The calculation of diluted earnings per share is based on the net profit for the year attributable to ordinary equity holders of the Company of RMB456,847,000 (2004: RMB319,393,000) and the weighted average number of approximately 1,368,416,000 (2004: 1,118,851,000) ordinary shares in issue during the year, being the weighted average number of ordinary shares outstanding during the year, adjusted for the effects of dilutive potential ordinary shares outstanding during the year.

A reconciliation of the weighted average number of shares used in calculating the basic and diluted earnings per share amounts is as follows:

	2005 Number of shares'000	**2004 Number of shares'000**
Weighted average number of ordinary shares for the purpose of the basic earnings per share calculation	1,251,129	893,965
Weighted average number of ordinary shares, assumed to be issued at the conversion of convertible instrument at the beginning of the year	117,287	224,886
Weighted average number of ordinary shares for the purpose of the diluted earnings per share calculation	1,368,416	1,118,851

9. BILLS RECEIVABLE

An aging analysis of the bills receivable of the Group is as follows:

	2005 *RMB'000*	**2004** *RMB'000*
Within 3 months	81,167	77,952
4 to 6 months	361	2,454
	81,528	80,406

As at 31 December 2005, bills receivable amounting to approximately RMB80,590,000 (2004: RMB74,270,000) were factored with recourse to financial institutions. The corresponding amounts were recorded as short term bank loans. Subsequent to the balance sheet date, the bills receivable have been fully settled.

10. TRADE RECEIVABLES

The Group normally allows a credit period of not more than 30 days to its customers. The Group closely monitors overdue balances. In view of the aforementioned and that the Group's trade receivables relate to a large number of diversified customers, there is no significant concentration of credit risk. Trade receivables are non-interest-bearing.

An aging analysis of the trade receivables of the Group is as follows:

	2005 *RMB'000*	**2004** *RMB'000*
Within 3 months	168,626	162,465
4 to 6 months	7,965	21,904
7 to 12 months	6,926	3,513
Over 1 year	–	64
	183,517	187,946
Less: Provision for doubtful debts	(8,860)	(8,783)
	174,657	179,163

11. TRADE AND BILLS PAYABLES

An aging analysis of the trade and bills payables of the Group, based on the invoice date, is as follows:

	2005 *RMB'000*	**2004** *RMB'000*
Within 3 months	896,018	585,208
4 to 6 months	198,911	81,172
7 to 12 months	15,438	26,100
Over 1 year	6,638	2,117
	1,117,005	694,597

MANAGEMENT DISCUSSION AND ANALYSIS

Financial Review

During the year, the Group achieved significant growth in revenue from RMB7,213.8 million in 2004 to RMB10,825.0 million in 2005, representing an increase of 50.1%. Net profit attributable to equity holders of the Company increased by 43.0% to reach RMB456.8 million. Basic earnings per share were RMB0.365 (2004: RMB0.357), and the diluted earnings per share were RMB0.334 (2004: RMB0.285), representing an increase of 2.2% and 17.2% respectively as compared with 2004.

Gross Profit

In 2005, the Group's gross profit reached RMB2,413.2 million, representing a surge of 50.2% over that of 2004. Gross profit margin was sustained at 22.3%. The introduction of new high value-added products and the change in product mix offset the effect of keen competition in the market and increase in production costs during the year.

Operating Expenses

The Group's operating expenses mainly consisted of selling and distribution costs, administrative expenses and other operating expenses. Its total operating expenses for the year was RMB1,786.7 million (2004: RMB1,180.0 million).

Benefiting from greater economies of scale and stringent cost control, the Group's total operating expenses as a percentage of revenue in 2005 was 16.5%, similar to that of 2004.

Profit from Operating Activities

In 2005, at its effective cost control measures including streamlining and automating operating procedures and centralizing procurement control, the Group's EBITDA improved by 51.9% to RMB926.5 million (2004: RMB610.0 million) and EBITDA margin was 8.6%.

Net Profit

The Group's net profit attributable to equity holders of the Company reached RMB456.8 million for the year ended 31 December 2005, representing a surge of 43.0% from RMB319.4 million in the previous year.

During the year, one of the Group's subsidiaries, a sino-foreign joint venture, ceased to be eligible for the two-year tax holiday granted by the PRC government and was taxed at preferential rate. Nevertheless, the Group still enjoyed a relatively low effective tax rate of 10.0%, 5.5 percentage points higher than last year's.

Capital Structure, Liquidity and Financial Resources

The Group's cash and cash equivalents amounted to RMB1,247.8 million as at 31 December 2005 (2004: RMB1,018.9 million). During the reviewing period, the Group effectively centralized cash flow which contributed to a surge of 132.1% in net cash from operating activities to RMB1,328.3 million.

As at 31 December 2005, the Group had outstanding bank loans amounted to RMB811.3 million, representing a slight increase of RMB26.98 million from RMB784.3 million as at 31 December 2004. Of the outstanding bank loans, RMB365.6 million was repayable within one year and RMB445.7 million was repayable beyond one year. The total debt to equity ratio (total bank loans divided by total equity) of the Group was 29.3% as at 31 December 2005, representing a drop of 4.8 percentage points over the same period in 2004.

Total equity of the Group increased from RMB2,303.1 million as at 31 December 2004 to RMB2,767.1 million in 2005.

Net finance cost slightly increased by 6.7% to RMB31.06 million in 2005 (2004: RMB29.10 million).

Market Review

Riding on the economic prosperity of the country, the dairy industry in China sustained strong growth in 2005. According to a survey conducted by ACNielsen in 2005, by sales volume, the liquid milk market in China, excluding milk beverages and yogurt, grew an average 29% in 2005.

Competition for traditional products continued to be keen in the review period, leading inevitably to market consolidation. In the highly consolidated industry, it is the major dairy players of massive operating scale, who enjoy strong brand recognition supported by well-developed distribution networks who stand favorable, while small players with only weak brand and distribution back up are likely to be gradually ousted.

The average consumption of liquid milk in China is 18kg per capita per annum for the year, which is relatively low when compared with other Asian countries and developed areas. This points to promising business opportunities for the Chinese dairy industry and Mengniu as a major player in the industry.

Business Review

Branding and Marketing

According to a ACNielsen survey, the Group had 28.6% share of the liquid milk market by volume in December 2005, and 22.0% in the previous year. The increase was the result of strong brand equity, growing customer loyalty, aggressive marketing campaign and effective product differentiation strategy, all of which are our advantages as a key incumbent player in the industry. The top three players in China together had 61.3% share of the market in December 2005, as compared with 55.5% in December 2004. It showed that the China dairy industry had continued to consolidate.

The Group's effective nationwide sales and distribution network is made up of over 2,500 predominantly exclusive third party distributors located across the country. The Group employs sales personnel in key markets to ensure close communication with distributors and gain fine understanding of market situations and dynamics to help it map out effective operational plans for the different markets. Flexible logistics arrangement and using the latest enterprise resources planning (ERP) system have enabled the Group to effect timely meeting of market demands.

The Group's advertising and promotion expenses in 2005 amounted to RMB655.0 million, comparable to 6.1% of the revenue against 6.3% in 2004. This showed that the Group has been successful in realizing better economies of scale from its branding and marketing efforts.

The Group's positive image and superior quality products won for it the certificates of "Exclusive Dairy Products for Chinese Cosmonauts" and "Exclusive Dairy Products for National Athletes of the Training Bureau of the State Administration of Sports". The continuous active involvement of the Group in these sponsorship programs has greatly strengthened its brand image.

2005 was an important year to the Group in terms of business development as it rolled out effective promotion and advertising campaigns, which enhanced consumers' awareness of its brand and products. Apart from buying prime time slots on national television channels, the Group also mounted several innovative and unique marketing campaigns, such as title sponsorship – the "Mengniu Suan Suan Ru Super Girl Singing Contest" (蒙牛酸酸乳超級女聲), a nationwide singing competition organized by Hunan TV (湖南衛視) . The campaign was a huge success, boosting significantly the popularity of the Group as well as the Suan Suan Ru series among consumers.

Products

The Group boasted a comprehensive product portfolio comprising over 210 varieties of liquid milk, ice cream and other dairy products.

Liquid milk

The liquid milk segment continued to be the major revenue contributor and accounted for 86.0% of the Group's revenue. Revenue of this segment was RMB9,314.7 million in 2005, or an increase of 52.8% as compared with 2004. The growth was mainly due to our successful market differentiation strategy, which enabled us to introduce products with appeals to different consumer segments.

UHT milk accounted for 70.4% of the liquid milk segment's revenue. Its revenue increased by 35.8% to RMB6,555.3 million, thanks to the Group's strong brand building efforts. To meet different nutritional requirements of different consumer segments, the Group offered a variety of functional UHT milk products such as milk with high calcium and low fat, milk enriched with iron and zinc, nutritious milk for students and milk with low lactose content.

During the year, the Group launched a series of new functional milk products namely Breakfast milk (早餐奶) and Good Night milk (晚上好奶), with added nutrients such as malt essence, whey protein and vitamins, to cater for the daily needs of busy city dwellers. In addition, the Group launched the premium nutrition milk series, Milk Supreme (奶爵六特乳) and Milk Deluxe (特倫蘇), demonstrating its capability to satisfy market demand for high-end milk products.

For the milk beverages segment, the Group promoted Suan Suan Ru (酸酸乳), riding on the hit Super Girl Program. As a result, Suan Suan Ru was very well received and stood out among similar products in popularity. Revenue of the segment surged 134.7% to RMB2,118.2 million, and accounted for 22.7% of the liquid milk segment's revenue.

During the year under review, revenue from yogurt was RMB641.2 million, representing an increase of 74.7% over that of 2004. In early 2005, the Group launched new products using the proprietary probiotics it has jointly developed with Chr Hansen, a world-renowned probiotics manufacturer, and the market returned encouraging responses.

Ice cream
Revenue from ice cream increased by 60.9% to RMB1,295.9 million in 2005, contributing 12.0% of the Group's revenue. The increase was attributable to the tasty favors, trendy packaging, fresh image, quality raw materials and broad mix of Group's products. To sustain its market leadership and capture different seasonal and regional demands across the nation, the Group continued to invest in research and development ("R&D") and apply stringent quality control.

To stay close to the markets and speed up market penetration, in mid 2005, the Group strategically set up a new production plant in Shenyang to produce ice cream products for consumers in northeastern China who like to have ice cream even in wintertime.

In 2005, the Group streamlined its layered distribution system, with the aim of speeding up response to market and bringing the Group closer to the end markets.

Other dairy products
Revenue from other dairy products contributed 2.0% of the Group's revenue. The operating environment of the milk tablets market changed during the year, leading to a 31.2% decrease in revenue for other dairy products to RMB214.4 million in 2005. The decrease was mainly due to the retreat in sales during the year relative to the initial tremendous response bolstering sales when the milk tablets were first launched in 2004. During the year, seeing strong potential in the high value-added baby milk powder products, the Group invested continuous efforts to develop the market.

Raw milk supply
The Group's key focus has been to strengthen milk source management. The first Mengniu-Australia International Model Ranch ("Model Ranch") started operation in 2005. Equipped with high-end imported equipment and adopting advanced western management practices, the Model Ranch is currently the biggest model farm in China. It is the first model farm in the country to introduce advanced milking robot and also an excellent demonstration ground for milk farmers to learn the latest knowledge in raising, feeding and milking cows to enhance the quality and quantity of raw milk supply. The superior quality of Milk Supreme and Milk Deluxe are proof of the success of the Model Ranch.

The Group has exclusive supply contracts with over 3,000 milk collection centers and raw milk suppliers. To maintain a stable supply of quality and safe raw milk that meets consumers' requirements, the Group has in place a comprehensive quality control mechanism that keeps track of quality throughout the collection, transporting and production processes.

Production
In 2005, the Group operated 14 production bases that are equipped with world-class production and packaging technologies and had a combined annual production capacity of 2.78 million tons. To have production bases in different parts of the nation is a strategic direction of the Group in its bid to shorten transportation distance thus save production cost, and also to make logistic arrangements more flexible.

Prospects
According to the China Dairy Industry Association, the dairy industry of China is expected to grow at an annual rate of more than 20% between 2006 and 2008, driven by the continuous growth in per capita income and rising consumer demands for quality dairy products. Building on its strong brand name, well-developed distribution network, and, most importantly, its supreme quality products, the Group is confident of outperforming the industry in growth.

By improving product quality and production capacity, introducing new products, penetrating new markets, optimizing managerial capability and fostering closer business partnership with both distributors and raw milk suppliers, the Group will seize market opportunities to enlarge its market share.

Product quality and production capacity improvement
The Group will further strengthen its management systems, particularly in optimizing the quality control process by improving the existing quality control system. Taking reference from international models, we will ensure all production procedures meet high standards. The Group will build new plants in strategic regions or expand production capacity through merger and acquisition, which will allow it to seize growth opportunities from rising demand for dairy products. To effectively expand its production capacity, the Group will pay close attention to the latest development in equipment and technology and continually improve its production techniques and product quality.

New product introduction
To consolidate its leading position in the dairy market, the Group will enrich its product portfolio by introducing more high-value added functional milk products and products that match consumers' needs. The Group's persistent R&D efforts, innovation and introduction of new products will ensure the continual supply of nutritious and delicious products that can meet consumers' increasing sophisticated tastes and needs. These moves will enable the Group to capture opportunities for growth.

To further sharpen the competitiveness of fast moving products, such as Breakfast milk and Suan Suan Ru, efforts will be put on developing second or third generation of new products with enhanced taste and functions. Furthermore, the Group will introduce more highly nutritious products, such as the Future Star, tailored for fostering children's health and growth.

To establish a strong hold throughout the country, the Group built a scalable ice cream production base in Maanshan in 2005 to satisfy the needs of markets in southeastern China. The plant has had new facilities installed and will commence full production in 2006. By increasing the proportion of in-house production and with production facilities located close to the market, the Group can save on long-haul transportation cost and promptly respond to changes in the market in particular of low temperature products, and in turn enhance efficiency and flexibility of its operations. The plant will also allow the Group to allocate more resources into developing secondary ice cream brands and adding to the more premium product series, such as the Super Sui Bian (超級隨變) series, thus expand the ice cream market share.

To optimize its capability to capture business opportunities in the other dairy products segment, the Group has signed a framework agreement with a Danish company, Arla Foods amba ("Arla Foods"), for a proposed joint venture to engage in the production, sales and distribution of high-quality milk powder and other dried dairy products in China. The proposed joint venture with Arla Foods will not only optimize the Group's product mix, but will also equip the Group to compete with international dairy enterprises which are currently major players in the high-end imported milk powder market.

Penetration of new markets
By consolidating its leading position in first-tier markets and expanding into second and third-tier markets, the Group is confident of further boosting economies of scale for its sales and distribution network.

In addition to heightening consumer awareness of its primary brand ***Mengniu*** through effective nationwide promotion and advertising campaigns, the Group's growth strategies also include developing secondary brands. By establishing joint ventures with sizeable local firms and integrating their proven sales channels with its own, the Group can quickly expand market share.

Enhancement of management strength
To further reduce production costs and expenses, the Group will seek to enhance its management strengths and operational efficiency. It will improve its management model by integrating enterprise management, formulating a centralized logistics supply chain distribution system, optimizing its inventory management system and further quantifying the accountability of different departments.

The Group believes that its employees are its important asset. To gain the most from this important asset, incentives are incorporated in our promotion and remuneration mechanisms to encourage outstanding performance and loyalty.

Partnership
The Group sees the need to constantly align its interests with those of its partners so as to create a win-win situation conducive to the healthy growth of the industry.

Dairy farmers and milk collection centers are the Group's important partners for it is only with the cooperation of milk suppliers that it can ensure it has a stable supply of quality raw milk and can expand milk sources. Apart from providing these partners with training and support in the form of loan guarantee, the Group also encourages and assists them in expanding their ranches and milk collection centers to enjoy better economies of scale while meeting the needs of the fast growing China dairy market.

The Group will introduce to its operation world-class technology and management systems, and work with international companies to enhance development, production and quality control of products. These moves will enable us to achieve our goal of quickly assuming a share of the high-end market and in turn accelerate internationalization of the Group.

HUMAN RESOURCES AND REMUNERATION OF EMPLOYEES
As at 31 December 2005, the Group had a total of approximately 29,000 employees (2004: 21,000) in China and Hong Kong. Total staff costs for the year was approximately RMB390.3 million, excluding remuneration for the Directors. The expenses totaled approximately RMB252.3 million in 2004.

The Group invests in continuing education and training programs that can help its management staff and employees improve their professional skills and knowledge. An internal vocational training center, Mengniu Commercial Study College, has been set up to develop and render training programs for staff.

Our employees receive competitive remunerations with performance-based bonuses in line with industry practice. Other staff benefits provided by the Group include a pension contribution plan and insurance schemes.

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

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

USE OF LISTING PROCEEDS

During 2005, the unused listing proceeds of RMB180 million as at the beginning of the year had been fully utilized for the development and expansion of the production capacity of the Group.

AUDIT COMMITTEE

The audit committee comprises three non-executive Directors, two of whom are independent. The current committee members are Mr. Zhang Julin (chairman), Mr. Jiao Shuge (alias Jiao Zhen) and Mr. Li Jianxin. The audit committee has reviewed with the management of the Company and the external auditors the accounting principles and practices adopted by the Company, and discussed auditing, internal control and financial report matters including the review of the annual results for the year ended 31 December 2005. All issues raised by the external auditors and the audit committee have been addressed by the senior management. The work and findings of the audit committee have been reported to the board of directors (the "Board").

COMPLIANCE WITH THE CODE ON CORPORATE GOVERNANCE PRACTICE

Save and except that one of the resolutions which was passed at the Company's annual general meeting held on 28 June 2005 by way of a show of hands rather than by poll as required by the Rules Governing the Listing of Securities on the Stock Exchange (the ''Listing Rules''), details of which had been disclosed in an announcement dated 11 July 2005, none of the Directors of the Company is aware of any information that would reasonably indicate that the Company was not at any time during the year in compliance with the Code on Corporate Governance Practice as set out in Appendix 14 to the Listing Rules. Please refer to the Corporate Governance Report in the annual report to be published by the Company for details.

COMPLIANCE WITH MODEL CODE

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers set out in Appendix 10 to the Listing Rules as the Company's code of conduct and rules governing dealings by all Directors in the securities of the Company ("Model Code"). Having made specific enquiry of all Directors of the Company, the Company confirms that, during the year, the Directors of the Company had strictly complied with the Model Code.

CLOSURE OF REGISTER

The register of members of the Company will be closed from 20 June 2006 to 23 June 2006, both days inclusive, during which period no transfer of shares of the Company can be registered. In order to qualify for the abovementioned final dividends, all transfers, accompanied by the relevant share certificates, must be lodged with the Company's branch share registrar, Computershare Hong Kong Investor Services Limited, at Shops 1712-16, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong for registration no later than 4:00 p.m. on 19 June 2006.

APPRECIATION

The Board would like to take this opportunity to express gratitude to our employees for their hard work and commitment to the Group. We also thank our shareholders, customers and banks for their continuous support.

By order of the Board
Niu Gensheng
Chief Executive Officer

Hong Kong, 10 April 2006

As at the date of this announcement, the executive directors are Mr. Niu Gensheng, Ms. Lu Jun, Mr. Yang Wenjun and Mr. Sun Yubin. The non-executive directors are Mr. Jiao Shuge (alias Jiao Zhen) and Mr. Julian Juul Wolhardt. The independent non-executive directors are Mr. Wang Huaibao, Mr. Zhang Julin and Mr. Li Jianxin.

"Please also refer to the published version of this announcement in The Standard."