Global Dairy Holdings Limited
環 球 乳 業 控 股 有 限 公 司

(Incorporated in the Cayman Islands with limited liability)

(Stock code: 01007)

PROPOSED ISSUANCE OF US$ SETTLED RMB SENIOR GUARANTEED NOTES

This announcement is made by the Company pursuant to Rule 13.09(1) of the Listing Rules.

The Company proposes to conduct an international offering of the Proposed Notes Issue to certain institutional investors in Asia and Europe.

The Notes are proposed to be guaranteed by the Subsidiary Guarantor. As at the date of this announcement, the principal amount, certain terms and conditions of the Proposed Notes Issue are yet to be finalised. The pricing of the Proposed Notes Issue, including the aggregate principal amount, will be determined through a book building exercise conducted by BofA Merrill Lynch and Macquarie as the joint lead managers and joint bookrunners. BofA Merrill Lynch is acting as the sole global coordinator in connection with the Proposed Notes Issue. Upon finalising the terms of the Notes, it is expected that the Company and the Subsidiary Guarantor will enter into the Purchase Agreement with BofA Merrill Lynch and Macquarie.

The completion of the Proposed Notes Issue is subject to, among others, market conditions and investor interest. If the Notes are issued, the Company intends to use the net proceeds from the Notes to finance a portion of the second stage of its vertical integration plan in China and the balance for working capital and general corporate purposes. The Company may adjust the foregoing plans in response to the changing market conditions and circumstances and thus, may reallocate the use of proceeds from the Proposed Notes Issue.

Approval in-principle has been obtained for the listing of the Notes on the SGX-ST. Admission of the Notes to the Official List of the SGX-ST and quotation of the Notes on the SGX-ST are not to be taken as an indication of the merits of the Company or the Notes. The SGX-ST assumes no responsibility for the correctness of any of the statements made, opinions expressed or reports contained in this announcement. No listing of the Notes has been or will be sought in Hong Kong.

As no binding agreement in relation to the Proposed Notes Issue has been entered into as at the date of this announcement, the Proposed Notes Issue may or may not materialise. Investors and shareholders of the Company are urged to exercise caution when dealing in the securities of the Company. A further announcement in respect of the Proposed Notes Issue will be made by the Company should the Purchase Agreement be signed.

This announcement is made by the Company pursuant to Rule 13.09(1) of the Listing Rules.

THE PROPOSED NOTES ISSUE

Introduction

The Company proposes to conduct an international offering of the Proposed Notes Issue to certain institutional investors in Asia and Europe. In connection with the Proposed Notes Issue, the Company will provide such investors with certain recent corporate and financial information regarding the Group and some of such information may not have previously been made public. An extract of information to be provided to the institutional investors is attached to this announcement and will be available on the Company's website *(www.global-dairy.com.cn)* at the same time when such information is released to the institutional investors.

The Notes are proposed to be guaranteed by the Subsidiary Guarantor. The pricing of the Proposed Notes Issue, including the aggregate principal amount, will be determined through a book building exercise conducted by BofA Merrill Lynch and Macquarie as the joint lead managers and joint bookrunners. BofA Merrill Lynch is acting as the sole global coordinator in connection with the Proposed Notes Issue.

As at the date of this announcement, the principal amount, certain terms and conditions of the Proposed Notes Issue are yet to be finalised. Upon finalising the terms of the Notes, it is expected that the Company and the Subsidiary Guarantor will enter into the Purchase Agreement with BofA Merrill Lynch and Macquarie. The Company will make further announcement in respect of the Proposed Notes Issue upon the execution of the Purchase Agreement.

The Proposed Notes Issue will only be offered or sold outside the United States in reliance on Regulation S under the U.S. Securities Act. None of the Notes will be offered to the public in Hong Kong and none of the Notes will be placed with any connected persons of the Company.

Reasons for the Proposed Notes Issue

The Board believes that the Proposed Notes Issue represents a timely opportunity for the Group to supplement the funding of its business expansion plan. The Board also believes that the Proposed Notes Issue will further strengthen the liquidity position of the Group and provide long-term capital to the Group.

Proposed use of proceeds

The completion of the Proposed Notes Issue is subject to, among others, market conditions and investor interest. If the Notes are issued, the Company intends to use the net proceeds from the Notes to finance a portion of the second stage of its vertical integration plan in China and the balance for working capital and general corporate purposes. In this connection, it is currently anticipated that the second stage of the Company's vertical integration plan will include: (i) the development of approximately 25 smaller scale dairy farms in Wuchang and Zhaoyuan with a capacity of up to 700 dairy cows per farm and ancillary facilities such as milking stations and a transportation fleet; (ii) the acquisition or construction of a feed processing plant to support the Group's vertical integration plan; and (iii) the acquisition or construction of additional raw milk processing capacity to complement the Group's existing production facilities and support the expansion of our milk formula business.

The development of approximately 25 smaller scale dairy farms in Wuchang and Zhaoyuan and ancillary facilities such as milking stations and a transportation fleet is expected to be financed by the net proceeds from the Notes. It is expected that each of the farms in Wuchang and Zhaoyuan will house approximately 500 mature milkable dairy cows. The construction of these dairy farms is expected to commence in 2011 and these farms are expected to begin commercial production in 2012. The Board considers that the combined raw milk generated from these dairy farms construction will allow the Group to achieve a self-sufficient supply of raw milk required by its production of milk formula products and whole milk powder products. It is estimated that the total investment to develop these dairy farms will be approximately RMB650 million, which is intended to be utilised for the purchase of land and buildings, milking and transportation equipment and dairy cows.

Depending on the progress of and to support the development of its vertical integration plan, the Group may acquire or construct a cattle feed processing plant to meet the feed requirements for all its dairy farms. Assuming that the development of its 25 new dairy farms progress as anticipated, it is expected that the Group will start construction or acquire the cattle feed processing plant in 2011 and target for the plant to enter commercial production in 2012. The expected cost of investment is approximately RMB100 million, which is expected to be funded by the net proceeds from the Notes and internal cash of the Group.

In order to support the expansion of its milk formula business as well as to provide additional capacity to process the raw milk produced by its new dairy farms, the Group may also acquire or construct additional raw milk processing capacity in 2013. The Group expects to fund a portion of not less than RMB400 million investment of additional processing capacity by the net proceeds from the Notes and its internal cash.

The Company may adjust the foregoing plans in response to the changing market conditions and circumstances and thus, may reallocate the use of proceeds from the Proposed Notes Issue.

Listing

Approval in-principle has been obtained for the listing of the Notes on the SGX-ST. Admission of the Notes to the Official List of the SGX-ST and quotation of the Notes on the SGX-ST are not to be taken as an indication of the merits of the Company or the Notes. The SGX-ST assumes no responsibility for the correctness of any of the statements made, opinions expressed or reports contained in this announcement. No listing of the Notes has been or will be sought in Hong Kong.

Recent Development

In connection with the development of the dairy farm planned as part of the first stage of the vertical integration plan to expand the Group's business upstream into raw milk production, the Company's new wholly owned subsidiary, Wuchang Benniu, entered into a lease agreement on 22 March 2011 with Wuchang Pingfangdian pursuant to which Wuchang Benniu has agreed to lease 500 mu (approximately 83 acres) of land in Wuchang for a term of 30 years for RMB30,000 per year. The lease will expire on 21 March 2041 and is subject to customary termination provisions. Wuchang Benniu has the right to renew the lease after expiration for such further duration and upon such conditions as may be agreed with Wuchang Pingfangdian provided those terms are no less favorable than terms proposed by any other third party who offers to lease the land.

ABOUT THE COMPANY

The Group is a top ten domestic milk powder company in the PRC. The Group is principally engaged in production, marketing, and sale of medium-to-high and premium priced milk formula products in China. The Group's dairy products are classified into the following two main categories: milk formula products and whole milk powder products. The Group produces a full range of milk formula products and whole milk powder products for infants, children and adults.

GENERAL

Forward-looking statements in this announcement are based on current expectations. These statements are not guarantees of future events or results. Future events and results involve some risks, uncertainties and assumptions that are difficult to predict. Actual events and results could vary materially from the description contained herein due to many factors including changes in the market, changes in the business and financial condition of the Group, and changes in the capital markets in general.

As no binding agreement in relation to the Proposed Notes Issue has been entered into as at the date of this announcement, the Proposed Notes Issue may or may not materialise. Investors and shareholders of the Company are urged to exercise caution when dealing in the securities of the Company.

DEFINITIONS

In this announcement, the following expressions shall have the meanings set out below unless the context requires otherwise:

"Board"	the board of Directors of the Company
"BofA Merrill Lynch"	Merrill Lynch International, the sole global coordinator and one of the joint lead managers and joint bookrunners in respect of the offer and sale of the Notes
"Company"	Global Dairy Holdings Limited (環球乳業控股有限公司), a company incorporated in the Cayman Islands with limited liability, the shares of which are listed on the Main Board of the Stock Exchange
"Directors"	the directors of the Company
"Group"	the Company and its subsidiaries
"Hong Kong"	the Hong Kong Special Administrative Region of the PRC
"Listing Rules"	the Rules Governing the Listing of Securities on the Stock Exchange
"Macquarie"	Macquarie Capital (Singapore) Pte. Limited, one of the joint lead managers and joint bookrunners in respect of the offer and sale of the Notes
"Notes"	the US$ settled RMB senior guaranteed notes to be issued by the Company
"Offering"	offering of the Proposed Note issue to certain international investors in Asia and Europe
"Offering Memorandum"	the information memorandum to be despatched by the Company to certain institutional investors in connection with the Offering
"PRC"	the People's Republic of China
"Proposed Notes Issue"	the proposed issue of the Notes by the Company

"Purchase Agreement"	the agreement proposed to be entered into by and among the Company, the Subsidiary Guarantor, BofA Merrill Lynch and Macquarie in relation to the Proposed Notes Issue pursuant to which BofA Merrill Lynch and Macquarie act as the initial purchasers of the Notes
"Regulation S"	Regulation S under the U.S. Securities Act
"RMB"	Renminbi, the lawful currency of the PRC
"SGX-ST"	Singapore Exchange Securities Trading Limited
"Stock Exchange"	The Stock Exchange of Hong Kong Limited
"Subsidiary Guarantor"	the subsidiary of the Company that will be guaranteeing the Notes
"U.S. Securities Act"	the U.S. Securities Act of 1933, as amended, and the rules and regulations promulgated thereunder
"US$"	United States dollars, the lawful currency of the United States of America
"Wuchang Benniu"	Wuchang Benniu Muye Co., Ltd., a wholly owned subsidiary of the Company
"Wuchang Pingfangdian"	Wuchang Pingfangdian Tree Farm

By order of the Board
Global Dairy Holdings Limited
Zhao Yu
Executive Director and Chief Executive Officer

Hong Kong, 29 March 2011

As of the date of this announcement, the executive Directors are Mr Zhao Chuan Wen, Mr Zhao Yu, Mr Xia Yuan Jun, Mr Fu Chong and Mr Fong Pin Jan. The independent non-executive Directors are Mr Cheung Hok Fung Alexander, Ms Chan Wah Man Carman and Mr Zhang Zhou.

Global Dairy Holdings Limited
Extract of certain information from the Offering Memorandum

This extract is being published only for the purpose of facilitating equal dissemination of information to investors in Hong Kong and not for any other purposes.

Information in this extract may be updated or revised by the Company from time to time.

This extract does not constitute a prospectus, notice, circular, brochure or advertisement offering to sell any securities to the public in any jurisdiction, nor is it an invitation to the public to make offers to subscribe for or purchase any securities, nor is it calculated to invite offers by the public to subscribe for or purchase any securities.

This extract must not be regarded as an inducement to subscribe for or purchase any securities, and no such inducement is intended.

Neither the Company nor any of its affiliates, or advisers is offering, or is soliciting offers to buy, any securities in any jurisdiction through the publication of this extract.

Sections in the Offering Memorandum to be included in this extract:

1. Risk Factors
2. Use of Proceeds
3. Capitalization and Indebtedness
4. Selected Consolidated Financial Information and other Data
5. Management's Discussion and Analysis of Financial Condition and Results of Operations
6. History, Reorganization and Group Structure
7. Business
8. Regulatory Overview
9. Related Party Transactions
10. Description of Material Indebtedness and Other Obligations

You should carefully consider the risks and uncertainties described below and other information contained in this offering memorandum before making an investment decision. The risks and uncertainties described below may not be the only ones that we face. Additional risks and uncertainties that we are not aware of or that we currently believe are immaterial may also adversely affect our business, financial condition or results of operations. If any of the possible events described below occur, our business, financial condition or results of operations could be materially and adversely affected. In such case, we may not be able to satisfy our obligations under the Notes, and you could lose all or part of your investment.

Risks Relating To Our Business

We depend on third party suppliers of raw milk and other raw materials, and we may not be able to secure a stable supply of raw materials with acceptable quality or on acceptable terms.

The success of our business depends on our ability to obtain sufficient quantities of quality raw materials, such as raw milk, sucrose, whey powder, vegetable oil, mineral supplements, lactose, maltose, whey protein concentrate and various flavorings, on commercially acceptable terms and in a timely manner. For the years ended December 31, 2008 and 2009, the Daqing Dairy Group's total cost of purchases from its five largest suppliers, in aggregate, amounted to approximately 30.5% and 46.3%, respectively of the Daqing Dairy Group's total cost of purchases. For the years ended December 31, 2008, 2009 and 2010, the Group's total cost of purchases from its five largest suppliers, in aggregate, amounted to approximately 27.7%, 46.3% and 39.7%, respectively of the Group's total cost of purchases.

Raw milk is the primary raw material for the production of our products. We source our raw milk from selected milk collection centers which collect raw milk from dairy farms and individual dairy farmers in proximity to Daqing. For the years ended December 31, 2008 and 2009, the cost of purchases of raw milk for the Daqing Dairy Group represented approximately 60.9% and 33.9% of our total cost of purchases, respectively. For the years ended December 31, 2008, 2009 and 2010, the cost of purchases of raw milk for the Group represented approximately 64.0%, 33.9% and 48.7% of the Group's total cost of purchases, respectively.

We have non-exclusive raw milk supply agreements and framework supply agreements in respect of other raw materials which are generally for a term of one year. Both parties to the relevant non-exclusive raw milk supply agreement have the right to terminate the agreement if the agreement cannot be implemented due to the occurrence of any unforeseeable circumstances that prevent any of the parties to the agreement from performing the agreement. We also have the right to terminate the agreement if the raw milk supplied contains contaminants. The non-exclusive raw milk supply agreements specify the annual volume of raw milk that must be available to us and that we must purchase (subject to an upward or downward adjustment of 10%). Our supply of raw milk depends on the ability of the milk collection centers to obtain a sufficient and steady supply of quality raw milk from the dairy farms and individual dairy farmers. The supply, in turn, depends on their dairy cows producing sufficient milk. The supply and the price of raw milk depend on various factors which are beyond our control, such as seasonal factors which may affect the volume and quality of milk that dairy cows produce, environmental factors that may affect the quality and quantity of cattle feed which in turn affects the volume and quality of milk that dairy cows produce, and the overall demand for raw milk.

If the quantity and quality of our raw material supply substantially decreases or if the price of our raw material supply substantially increases, we may incur additional costs to acquire sufficient quantity of these materials to meet our production needs. We may not be able to pass on these additional costs to our customers. In addition, if we cannot identify alternative sources of quality raw materials when needed, at acceptable prices or at the required quantity and quality, or at all, the resulting loss of production volume may materially and adversely affect our ability to deliver products to our customers in a timely manner, or at all, and may materially and adversely affect our business, financial condition and operating results.

We rely on our distributors to distribute and market our products, and their failure to perform to our expectations may have a material adverse effect on our business, financial condition and operating results.

A substantial portion of our products are sold to consumers through our distributors. For the years ended December 31, 2008 and 2009, sales to those customers of the Daqing Dairy Group which are now our distributors, in aggregate, accounted for 74.7% and 69.1% of our total revenue, respectively. For the years ended December 31, 2008, 2009 and 2010, sales to our distributors, in aggregate, accounted for 71.7%, 69.1% and 85.5% of our total revenue, respectively.

Although we have entered into distribution agreements with our distributors, the distribution agreements are non-exclusive and are generally for a term of one year. The termination or non-renewal of such distribution agreements, the failure of a distributor to distribute our products in a timely manner or according to the terms of such distribution agreements, or at all, or our failure to further expand our distribution network may have a material adverse effect on our business, financial condition and operating results.

We provide suggested wholesale and retail selling prices of our products to our distributors. However, we do not have any direct control over the retail outlets where our products are sold. If our distributors do not strictly adhere to our pricing and distribution policies or the retail outlets fail to adhere to the policies set by our distributors, our sales of products and our development and expansion of our distribution network may be materially and adversely affected.

We rely on milk formula products and whole milk powder products as our primary types of products. If we fail to improve or maintain our market position or to diversify our product range and expand our product offerings, our business, financial condition and operating results may be materially and adversely affected.

Our products are classified into the following two main categories: milk formula products and whole milk powder products. For the years ended December 31, 2008 and 2009, the Daqing Dairy Group's revenue attributable to the sale of the Daqing Dairy Group's milk formula products and whole milk powder products, in aggregate, accounted for approximately 99.6% and 96.7%, respectively, of the Daqing Dairy Group's total revenue. For the years ended December 31, 2008, 2009 and 2010, our revenue attributable to the sale of our milk formula products and whole milk powder products, in aggregate, accounted for approximately 99.1%, 96.7% and 97.6%, respectively, of our total revenue. As a result, if we fail to improve or maintain our market position or to diversify our product range and expand our product offerings, our business, financial condition and operating results may be materially and adversely affected.

Our success depends on our ability to gain market acceptance and market share for our products and our growth strategy to achieve this may not prove successful.

Our success depends on our ability to offer products that satisfy consumer preferences and needs. In particular, consumer preferences and needs for milk formula products and whole milk powder products are constantly changing, and there can be no assurance that our current line of milk formula products and whole milk powder products will be able to satisfy changes in consumer preferences and needs or that we will be able to promptly and commercially develop and produce new products that satisfy such preferences and needs.

We intend to continue expanding our product offerings. However, we may not be able to obtain the regulatory approvals for new products required for us to market and sell such products. In addition, the development of new products may require more time, cost more and be less successful than we anticipate. We also intend to enhance our brand recognition nationwide by conducting various marketing campaigns, expand our distribution network in China by increasing the number of our distributors, increase the headcount of our sales and marketing team, and recruit additional product development experts in food technology. If the development or launch of our new products and/or our growth strategy of enhancing our brand recognition is not successful, we may not be able to recover expenses related to the above activities, and as a result, our business, financial condition and operating results may be materially and adversely affected.

Our growth plan relies on favorable demographic, consumer and economic trends in the PRC market, including the increasing acceptance of infant milk formula as a substitute for breast milk for infants. We cannot assure you that there will be no adverse change in our consumer demographics, including acceptance in the PRC of using infant milk formula as a substitute for breast milk.

Publicly available data suggest that breastfeeding has many health benefits for infants that cannot be replicated by dairy-based infant formula products. Additionally, popular literature, cultural pressure, government policies and medical advice in China generally promote the benefits of breastfeeding. For example, on August 1, 2007, China's Ministry of Health issued an Infant Feeding Strategy which promoted breastfeeding and requested all relevant local departments to publicize the benefits of breastfeeding through radio broadcasting, television and newspapers during World Breastfeeding Week, which took place in early August 2007. Thus, to the extent that private, public and government sources increasingly promote the benefits of breastfeeding, there could be a reduced demand for our products and our revenues could be adversely affected.

We may also fail to anticipate, identify or react to changes in consumer preferences and needs, and we cannot assure you that we will be able to gain market acceptance and market share for our products. Furthermore, our competitors may be able to introduce products that appeal to consumer preferences and needs more effectively or efficiently than us. While the relevant government authorities have indicated that they will support our growth strategy (including the provision of lands, development of dairy farms and dairy cows supply guarantees), we cannot assure you that government authorities will not change their policies or we can successfully enforce such indications against government authorities. As a result, our business, financial condition and operating results may be materially and adversely affected.

We intend to evaluate integration opportunities to expand our business upstream into raw milk production, which may fail to yield the intended benefits and could negatively impact our existing business.

We intend to evaluate integration opportunities to expand our business upstream into raw milk production by investing in dairy farms. Such investments carry various risks which may have a material adverse effect on our business, financial condition and operating results. The risks include:

- failure to identify suitable investment opportunities and incorrect assessment of the likely benefits, risks, commercial viability and technical feasibility of such investment opportunities;
- diversion of our management's time and effort and our resources from our existing business to explore and assess investment opportunities;
- lack of our experience in managing and operating such upstream business and inability to recruit management and technical personnel to manage such upstream business;
- lack of the involvement of the relevant municipal government authorities in identifying and making available pasture lands to us with a sufficiently long term at competitive rates; and
- outbreak of infectious animal diseases in cows such as mad cow disease (bovine spongiform encephalopathy).

With the consummation of our IPO, we commenced our two-stage strategy to realize our vertical integration plan. We intend to use the net proceeds from our IPO to implement the first stage of our vertical integration plan. The first stage of our vertical integration plan involves the construction of a dairy farm designed to raise dairy cows. We established a new wholly owned subsidiary, Wuchang Benniu, to develop and operate our dairy farm, which we currently plan to complete in 2012. Having reviewed and evaluated the progress of the first stage of our vertical integration plan, we intend to proceed with the second stage. We intend to use proceeds from this offering to finance a portion of the second stage which we currently anticipate will include: (i) the development of approximately 25 smaller scale dairy farms in Wuchang and Zhaoyuan with a capacity of up to 700 dairy cows per farm and ancillary facilities such as milking stations and a transportation fleet; (ii) the acquisition or construction of a feed processing plant to support our vertical integration plan; and (iii) the acquisition or construction of additional raw milk processing capacity to complement existing production facilities and support the expansion of our milk formula business and for general work capital.

In connection with the development of our first stage dairy farm, Wuchang Benniu and Wuchang Pingfangdian entered into a land lease agreement on March 22 2011 pursuant to which Wuchang Benniu has agreed to lease 500 mu (approximately 83 acres) of land in Wuchang with a term of 30 years. If Wuchang Pingfangdian breaches or terminates the agreement unilaterally, we may need to locate another piece of land for the dairy farm and such relocation may adversely affect our financial condition and results of dairy farm operation.

We cannot assure you that we will be able to achieve the expected production capacity from our vertical integration plan as the expected production capacity is subject to various factors, such as our ability to complete the acquisition or construction of the dairy farms within the expected time frame, our ability to purchase the numbers of dairy cows as anticipated under our vertical integration plan and our ability to obtain the necessary equipment and ancillary facilities required to operate the dairy farms as well as complement our expansion plan and our ability to finance those plans whether with internal cash or external resources.

If our intended upstream investment in raw milk production is fully realized, we believe that to a certain extent, our cost of sales may be reduced as we will no longer need to purchase raw milk from external sources. However, our profit margin is affected by various factors such as the scale of our operations, our cost of production as compared to our cost of purchases of raw milk if we were to source the raw milk supply externally, and the above risks associated with this vertical integration strategy. In view of this, our profit margin may not necessarily increase. There can be no assurance that such investment will achieve the intended commercial benefits or the level of economic returns that we expect, or at all.

Failure to obtain financing on reasonable terms could affect our continuing business operations and the execution of the our growth strategies; increased debt financing may have a material adverse effect on us.

To fund our continuing business operations, existing and future capital expenditure requirements, acquisition and investment plans and other funding requirements, we need sufficient internal sources of liquidity or access to external funding sources, including debt and equity financing. Our growth strategies, including our vertical integration plan (see "— We intend to evaluate integration opportunities to expand our business upstream into raw milk production, which may fail to yield the intended benefits and could negatively impact our existing business" and "Business — Business Strategies — Evaluate integration opportunities to expand our business upstream into raw milk production."), may require significant amounts of financing which we may not be able to obtain. Our ability to obtain external financing in the future is subject to a variety of uncertainties, including:

- obtaining the necessary regulatory approvals to raise financing in the domestic or international markets;
- our future financial condition, operating results and cash flow;
- political and social instability and the condition of the global and domestic financial markets;
- the regulatory environment;
- changes in the monetary policy of the PRC government with respect to bank interest rates and lending practices and conditions.

If adequate funding is not available to us on favorable terms, or at all, it may materially and adversely affect our ability to fund our operations, or develop or expand our business, which may in turn materially adversely affect our ability to repay the Notes. In addition, any future debt incurred by usmay:

- increase the our vulnerability to adverse economic and industry conditions, limit the our flexibility to react to changes in the sectors in which we operate, and place us at a competitive disadvantage in relation to competitors that have less debt;
- restrict the our ability to make additional capital expenditures;
- require us to dedicate a substantial portion of its cash flow to service debt payments; and
- subject us and our subsidiaries to restrictive financial and other covenants, including restrictions on the ability of us or our subsidiaries to declare dividends or incur additional indebtedness.

Any of these factors, alone or together, could materially and adversely affect our business, financial condition and results of operations.

Our gross profit margins fluctuated during each of the last three fiscal years, and if our gross margins decline in the future, our business, financial condition and operating results could be harmed.

The gross profit margins of the Daqing Dairy Group for our milk formula products for the years ended December 31, 2008 and 2009 were 57.3% and 53.5%, respectively and the gross profit margins of the Group for our milk formula products for the years ended December 31, 2008, 2009 and 2010 were 53.1%, 53.5% and 55.5%, respectively. The decrease in the gross profit margins of the Daqing Dairy Group and the Group for our milk formula products in the year ended December 31, 2009 as compared to those in the year ended December 31, 2008 was primarily due to the decline in the gross profit margin of the Emilon brand milk formula products by 3.7%. This decline resulted from changes in the sales mix of the Emilon brand product offerings, with more of the lower margin Emilon Bei Cong Series being sold compared to the higher margin Emilon Shuang Neng Series as target consumers in the higher priced market segment were more affected by the melamine incident in 2008, where several brands of milk formula and other dairy products in China were found to be contaminated with melamine, which poses health risks for consumers. This led some consumers within this target customer group, which generally have stronger purchasing power, to switch to imported brands of milk formula. The increase in the gross profit margin of the Group for our milk formula products for the year ended December 31, 2010 as compared to the year ended December 31, 2009 was primarily due to the introduction of our Shi Jia brand, which has a relatively higher gross profit margin of 71.8%. See "Management's Discussion and Analysis of Financial Condition and Results of Operations." If we cannot pass on to customers any increase in raw milk prices or sales rebates for our distributors, or if the proportion of lower margin products in our product sales mix increases as a result of changing consumer preferences and need, we may experience a decline in our gross profit margins, which may have a material adverse effect on our business, financial condition and operating results.

If operations at our manufacturing facilities are disrupted, our business, financial condition and operating results could be harmed.

Our revenue is dependent on the continued operations of our production facilities in Daqing and Wuchang, Heilongjiang, the PRC. Our manufacturing operations are subject to risks including, among other things, breakdown, failure or sub-standard performance of machinery and equipment, natural disasters, and failure to comply with all applicable PRC laws, regulations and standards such as environmental law and workplace safety law. The occurrence of any material operational problems at our manufacturing facilities in the future may have a material adverse effect on our business, financial condition and operating results. We do not maintain business interruption insurance. See "Risk Factors — We may not have adequate insurance coverage to cover potential liabilities or losses."

Substantial increases in the cost of purchases of coal may have a material adverse effect on our business, financial condition and operating results.

We consume coal for generating heat to dry milk during the production process of milk formula products and whole milk powder products. For the years ended December 31, 2008, 2009 and 2010, the cost of purchases of coal amounted to approximately RMB2.9 million, RMB8.2 million and RMB13.1 million, respectively, representing approximately 3.3%, 3.3% and 3.3% of our total cost of purchases, respectively, over the same periods. If the PRC government imposes restrictions on the use of coal, thereby disrupting our energy supply, or if we are otherwise unable to obtain adequate supply of coal to meet our production requirements, our operations may be disrupted and our production and delivery schedules may be materially and adversely affected. Any significant price increase of coal in the future may have an adverse effect on our profitability and operations. In addition, our ability to pass increased energy costs along to our customers may be limited by competitive pressure and customer resistance. We cannot assure you that we will be able to raise the prices of our products sufficiently to cover the increased costs resulting from interruptions to our operations or increases in the cost of coal.

We may not be successful in maintaining an effective quality control system at our manufacturing facilities.

The quality of our products is crucial to the success of our business. Our product quality depends significantly on the effectiveness of our quality control system, which, in turn, depends on a number of factors, including the design and implementation of our quality control policies and guidelines. Any significant failure or deterioration of our quality control system may seriously damage our product quality and have a material adverse effect on our reputation in the market among current or prospective customers, which may, in turn, lead to fewer orders in the future, harming our business, financial condition and operating results. See "Risk Factors — We may not have adequate insurance coverage to cover potential liabilities or losses."

Failure to fully utilize the production capacity of, or to operate, our new production facilities as anticipated may materially and adversely affect our business, financial condition and operating results.

We have recently completed the construction of the phase two production line at our Daqing production facilities and the new production line at our Changqing production facility. We currently expect the latter to commence operation in second quarter of 2011.

However, we cannot assure you that we will be able to utilize fully the additional production capacity because such utilization is dependent on a number of factors, including but not limited to our success in expanding our business and the amount of available raw milk. Demand for our products may not be as high as we expect or the new production lines may not function as anticipated, and we may consequently fail to realize the expected benefit from our investment in the new production facilities.

We do not have an integrated, comprehensive and enterprise-wide management information system. As a consequence, we may not be able to manage our expansion and operations effectively, and our ability to operate our business efficiently may be hindered.

Although our management information system covers finance and inventories, we do not have an integrated, comprehensive and enterprise-wide management information system that enables us to review our production performance and production capacity, trace our customers' orders and assess our product delivery schedule on a real-time basis. In addition, we record our inventory levels based on our monthly stock-take. As such, we do not have real-time records which show the movement of our inventories at a particular point of time. As a consequence, we may not be able to manage our expansion and operations effectively, and our ability to operate our business efficiently may be hindered, which, in turn, may have a material adverse effect on our business, financial condition and operating results.

We did not comply with PRC regulations relating to the housing provident fund and may be required to make payment for the outstanding contributions for the housing provident fund.

The Regulations on Management of the Housing Provident Fund《住房公積金管理條例》, which were promulgated and became effective on April 3, 1999 and then amended on March 24, 2002, provide that enterprises in the PRC shall undertake to register with the relevant authorities and maintain the relevant accounts with designated banks in respect of the housing provident fund, and contribute to the housing provident funds at a rate of not less than 5% of the average monthly salaries paid to the employees in the previous year. Violation of the above-mentioned regulations may result in the imposition of fines or penalties, or other liability in severe cases.

Prior to April 2010, Daqing Dairy did not register with the relevant authority or maintain accounts with a designated bank in respect of the housing provident fund, or make any contributions to the housing provident fund. As such, Daqing Dairy has breached the Regulations on Management of the Housing Provident Fund《住房公積金管理條例》. The letter of confirmation issued by the housing provident fund management centers of Daqing (大慶市住房公積金管理中心) dated June 11, 2010 confirms that since the effective date of the Regulations on Management of the Housing Provident Fund《住房公積金管理條例》, the housing provident fund management center of Daqing (大慶市住房公積金管理中心) has been progressively implementing the regulations on private enterprises, foreign-invested enterprises and other non State-owned enterprises in Daqing and notes that a substantial number of these enterprises have not set up and contributed towards the housing provident funds and are currently taking steps to set up and contribute towards the housing provident funds. Given the progressive implementation approach of the housing provident fund management center of Daqing (大慶市住房公積金管理中心), while our legal department oversees and seeks to ensure our continued compliance with laws and regulations, Daqing Dairy did not register the housing provident fund with the relevant housing provident fund management center (住房公積金管理中心) immediately upon the effective date of these regulations.

Since its incorporation on August 7, 2008, Changqing Dairy has not registered with the relevant authority or maintained accounts with a designated bank in respect of the housing provident fund, or made any contributions to the housing provident fund. As such, Changqing Dairy has breached the Regulations on Management of the Housing Provident Fund《住房公積金管理條例》. On April 20, 2010, Changqing Dairy obtained a written confirmation from the housing provident fund management center (住房公積金管理中心) of Harbin's Wuchang office regarding the unpaid contributions from the date of incorporation of Changqing Dairy to April 20, 2010. According to such written confirmation, the housing provident fund management center (住房公積金管理中心) will not require Changqing Dairy to make any contribution payment in respect of the above unpaid contributions nor will any penalty or other form of administrative penalties be imposed on Changqing Dairy for the unpaid contributions to the housing provident fund.

Since April 2010, Daqing Dairy and Changqing Dairy have registered with, and made the relevant contributions to, the relevant housing provident fund management centers. In addition, Changqing Dairy has recently established Wuchang Benniu as its wholly owned subsidiary in the PRC on November 25, 2010. Wuchang Benniu has registered with the relevant provident fund management centers in March 2011. Wuchang Benniu will make the relevant contributions to such centers upon commencement of operation.

We estimate the amounts of outstanding contributions for the housing provident fund up to December 31, 2009 would amount to approximately RMB2.2 million. We believe that we have made full provisions for these contributions in the relevant accounts and such provision for this outstanding amount remains in our account as of December 31, 2010.

We may experience a shortage of labor and our labor costs may increase.

The dairy industry in China is labor intensive. For the years ended December 31, 2008 and 2009, the costs of direct labor expressed as a percentage of the Daqing Dairy Group's cost of sales amounted to approximately 1.3% and 1.1%, respectively, of our costs of sale. For the years ended December 31, 2008, 2009 and 2010, the costs of direct labor expressed as a percentage of our cost of sales amounted to approximately 1.2%, 1.1% and 1.0%, respectively, of our costs of sale. Labor costs in China have been increasing and may continue to increase in the future. We cannot assure you that we will not experience any shortage of labor. Our labor costs may continue to increase in the future. If we experience a shortage of labor, we may not be able to maintain or expand our production operations. If labor costs increase, our production costs will also increase and we may not be able to pass such increase to our customers due to competitive pricing pressures. In such circumstances, our business, financial condition and operating results may be materially and adversely affected.

We rely on our key management personnel and our ability to attract and retain qualified personnel. If we are unable to attract, motivate or retain such qualified personnel, our business may be materially and adversely affected.

The success of our business has been, and will continue to be, heavily dependent upon the continuing service of our key management personnel. In particular, we rely on the expertise and experience of Zhao Chuan Wen (our executive director and chairman, and the honorary director of Daqing Dairy), Zhao Yu (our executive director and chief executive officer, the sole executive director of Daqing Dairy and Changqing Dairy and the executive director and general manager of Wuchang Benniu), Xia Yuan Jun (our executive director and deputy chief executive officer and the general manager of Daqing Dairy and Changqing Dairy), Fu Chong (our executive director and chief operations officer) and Zhang Bing (our assistant general manager for production). They play a pivotal role in our daily operations and business strategies. If we lose the services of any of these key executives and cannot hire suitable replacements in a timely manner, our business, financial condition and operating results may be materially and adversely affected.

In addition, our success depends on our ability to attract and retain talented personnel, in particular, our team of management personnel. We may not be able to attract or retain all the personnel we need.

We may also need to offer superior compensation and other benefits to attract and retain key personnel and therefore cannot assure you that we will have the resources to fully achieve our staffing needs.

Our failure to attract and retain competent personnel and any increase in staffing costs to retain such personnel may have a negative impact on our ability to maintain our competitive position and to grow our business. As a result, our business, financial condition and operating results may be materially and adversely affected.

Our operating results are subject to seasonal fluctuation and other variations.

Sales of our products are subject to seasonality. We typically experience higher sales of milk formula products and whole milk powder products in the second half of the year compared to the first half. We believe that this seasonality factor mainly reflects an increase in purchase orders made by our distributors in the second half of the year to increase inventories in advance of the Chinese New Year in anticipation of higher demand around the holiday period. However, it is also possible that our distributors increase their purchases in the second half of the year to meet their sales targets so that they qualify for annual sales rebates. From time to time, we make visits to our distributors to monitor their inventory levels and are not aware of any significant instance of over-stocking of our products. However, if our distributors over-stock significantly and then on-sell our products to ultimate consumers at a price which is significantly below our suggested unit retail price or if the expiry period of the products that reach the ultimate consumers is significantly shorter than the expiry period of our competitors' products, our brand image, reputation, business, financial condition and operating results may be materially and adversely affected.

We are exposed to payment delays or defaults by our customers.

We generally sell our products to our direct customers on credit and these customers are generally required to pay by bank transfers within 30 days of the date(s) of invoice(s). Our trade receivables turnover (calculated by dividing the trade receivables balance for the period by revenue and multiplying by 365 days, to reflect the full year) for the years ended December 31, 2008, 2009 and 2010 was eight days, nine days and four days. There is no assurance that our customers will be able to meet their payment obligations on time or in full or that our trade receivables days will not increase. Any inability on the part of our customers to settle promptly and in full the amounts due to us may materially and adversely affect our business, financial condition and operating cash flow.

Our internal control policies and procedures may be inadequate or ineffective and our management will be required to devote substantial time to new compliance initiatives.

We have established risk management and internal control systems consisting of organizational framework policies, procedures and risk management methods that we believe are appropriate for our business operations. However, we cannot assure you that our risk management and internal control systems will be sufficiently effective to identify and prevent all such risks.

In preparation for our IPO, we implemented measures to enhance our internal controls. As some of our risk management and internal control policies and procedures are relatively new, we will require additional time to fully evaluate the effectiveness of, and ensure compliance with, these policies and procedures. Our risk management and internal control policies and procedures depend on their implementation by our employees. We cannot assure you that all of our employees will adhere to our policies and procedures. The implementation of such policies and procedures may involve human errors or mistakes. Moreover, our growth and expansion may affect our ability to implement and maintain stringent risk management and internal controls as our business evolves. As a newly public company, we need to document, review, test and, if appropriate, improve our internal controls and procedures. Implementing any appropriate changes to our internal controls might entail substantial costs in order to add personnel and modify our existing accounting systems, take a significant period time to complete, and distract our officers and employees from the operation of our business. These changes might not, however, be effective in maintaining the adequacy of our internal controls and could adversely affect our operating results and our ability to operate our business. Any material deficiency in our risk management and internal control policies or procedures may expose us to significant operational risk, which may, in turn, have a material adverse effect on our business, financial condition and operating results.

We face possible infringement of our trademarks and other intellectual property rights and possible counterfeiting of our products, and may inadvertently infringe third party intellectual property rights.

The production process of our products and the ingredients and the ingredient mix of our products may involve proprietary know-how, technology or data that may not be patentable. Details of the ingredients and contents of our dairy products are required by applicable laws and regulations in the PRC to be listed on the packaging of the products. We may not have protection against third parties who may copy our trade secrets and product formulae. In addition, we believe that our brand recognition and reputation have been vital to the success and growth of our business. We may not always be successful in securing protection for our trade secrets, product formulae, proprietary know-how, trademarks and other intellectual property rights. Protection under the PRC intellectual property laws and the enforcement of such laws may not be as effective as in other countries. In addition, we may need to resort to litigation in the future to enforce our intellectual property rights. Any such litigation may result in substantial costs and a diversion of our resources. Our failure to protect and enforce our intellectual property rights may have a material adverse effect on our business, financial condition and operating results.

Counterfeiting and imitation have occurred in the past in the PRC for many products. We cannot assure you that counterfeiting and imitation of our products will not occur in the future. If it does occur, we may not be able to detect it and deal with it effectively. Any occurrence of counterfeiting or imitation may impact negatively upon our reputation and brand name. In addition, counterfeit and imitation products may result in a reduction of our market share, decrease in our revenue and increase our administrative costs in respect of detection and prosecution.

During the course of our operations including our production process, we may inadvertently infringe third party intellectual property rights, as a result of which other parties may initiate litigation or other proceedings against us. Responding to and defending these proceedings may require substantial costs and diversion of resources, and the result of these proceedings is uncertain. Our reputation may also be materially and adversely affected. If any of our employees infringes any third party's intellectual property rights or violates his obligations of confidentiality to any third party during his employment with us, the employee may be held liable and we may also be held liable for the conduct of such employee. In particular, if any of our employees infringes any third party's intellectual property rights or violates his obligations of confidentiality to any third party (including his previous employer) and uses the information obtained to develop any of our products, we may be held liable for damages and may not be able to produce and sell such products in the future.

We may be subject to product liability claims if our products are found to be unfit for consumption or cause illness.

We may be subject to product liability claims if our products are found to be unfit for consumption or cause illness. Products may be rendered unfit for consumption or cause illness due to contamination of ingredients, whether intentional or not, and illegal tampering. The occurrence of such problems may result in recalls of our products and significant damage to our brand reputation.

We cannot assure you that such incidents will not occur in the future. We may incur legal liabilities and have to compensate consumers for any loss or damage they suffer in respect of valid product liability claims and, in addition, we may also be subject to administrative or other government sanctions or penalties. In addition, adverse publicity from these types of concerns, whether valid or not, may discourage customers from purchasing our products. If customers lose confidence in our brand, we may experience long-term decline in our sales, which may have a material adverse effect on our business, financial condition and operating results.

We may not have adequate insurance coverage to cover potential liabilities or losses.

We do not maintain insurance on our properties, machinery, equipment, inventories, third party liability, product liability or business interruption insurance, except for work-related injury insurance for employees as required under the applicable PRC law. We or our directors or senior management may be exposed to claims for which no insurance policies have been maintained by us, including any claims that may be made against us if our products are found to have been contaminated with melamine, estrogen hormones or any other contaminants that cause harm to the consumers of our products. In addition, although we maintain insurance on our motor vehicles, there may be circumstances for which we would not be covered adequately or at all. If we incur substantial losses or liabilities and our insurance coverage is unavailable or inadequate to cover such losses or liabilities, our business, financial condition and operating results may be materially and adversely affected.

Delivery delays or poor handling by distributors and transport and logistics operators may have a material adverse effect on our business, financial condition and operating results.

In general, we rely on transport and logistics operators to deliver our products to our distributors. Delivery disruptions for various reasons beyond our control, including weather conditions, political turmoil, social unrest and strikes, may result in delayed or lost deliveries. The perishable nature of our dairy products may also mean that poor handling by transport operators may result in damage to our products, which may have a material adverse effect on our business, financial condition and operating results.

We have a limited operating history under our controlling shareholder.

We have a limited operating history under Zhao Yu's leadership as Daqing Dairy was not acquired until July 25, 2008. Consequently, the historical financial information in this offering memorandum may not provide a meaningful basis for investors to evaluate our historical business, our operations or our business prospects, and our operating results during the years ended December 31, 2008, 2009 and 2010 may not be indicative of our future performance.

We maintain inventories of raw materials and finished products which have limited shelf life.

Our finished products have a shelf life of 18 months and our raw materials have an average shelf life of between 12 and 24 months. Our inventory levels are based, in part, on our expectations regarding future sales. While we do not currently maintain large inventory levels for long periods, we may in future periods experience inventory build up if our sales decrease for any reason. Any significant shortfall in sales may result in higher inventory levels of raw materials and finished products than we require, thereby increasing our risk of inventory spoilage and corresponding inventory write-downs and write-offs, which may materially and adversely affect our results of operations.

We might face an inventory write-down if milk powder inventory continues to increase and milk powder prices continue to decline.

Due to the decline in the consumption of dairy based products in the PRC as a result of the melamine incident in 2008 and the significant increase in milk powder imports, there has been a nationwide inventory build-up of domestically produced milk powder in the PRC. According to the Dairy Industry Association of China, as a result of the melamine incident, surplus milk powder inventory in the PRC as of April 6, 2009 was estimated at 300,000 metric tons. Such inventory build up has caused a significant decline in milk powder prices. If milk powder inventory continues to rise and the milk powder prices continue to fall, we might face significant inventory write-down which will adversely affect our financial results.

We may experience problems with product quality or product performance, or the perception of such problems, which could adversely affect our reputation or result in a decrease in customers and revenue, unexpected expenses and loss of market share.

Our operating results depend, in part, on our ability to deliver high quality products in a timely and cost-effective manner. Our quality control and food safety management systems are complex. If the quality of any of our products deteriorates, it could result in shipment delays, order cancellations, customer returns, customer complaints, loss of goodwill and harm to our brand and reputation.

Any quality problems associated with the raw milk produced by the suppliers would also affect our product quality and lead to negative publicity against us, adversely affecting our reputation and brand, and causing a decrease in sales of our products and a loss of market share.

We depend on the national and local governments to support our industry and us.

The government plays a significant role in the economy of the PRC in general and, the dairy industry in particular. Governmental authorities provide support for the development of the dairy industry by, among other things, providing land, space and equipment for dairy farms, financing dairy farms, waiving compliance with otherwise applicable regulations, and reducing or eliminating tax obligations. Changes in governmental policies supportive of the development of this industry or failure to maintain good relations with governmental authorities may require us to incur expenses we are otherwise not required to incur. We may not have sufficient funds to pay such additional expenses and even if we do, our profitability may be reduced.

Risks Relating To Our Industry

We operate in a highly competitive market.

We consider the dairy market in which we operate to be highly competitive and we expect the competition to continually increase. Our competitors include producers of milk formula products and milk powder products. Many of our competitors sell products that are similar to ours, and our ability to compete against them is significantly dependent on our ability to distinguish our products from those of our competitors and demonstrate our product quality. According to the Euromonitor Report, leading global dairy product companies, such as Mead Johnson (Guangzhou) Ltd., International Nutrition Co Ltd, Nestle (China) Ltd, Shanghai Wyeth Nutritional Co Ltd and Abbott Nutrition International (China), collectively account for almost 40% of the total market share by sales value in the market in China in 2009. Consumers may increasingly shift their purchases of infant milk formula from domestically sourced products to internationally sourced products for various reasons, such as the melamine incident in 2008. Any such shift could increase our competition and reduce our market share and sales. The market has yet to see a domestic milk powder manufacturer capable of competing with the leading global brand producers in China. In addition, consumer preferences and needs may change quickly and frequently, creating opportunities for new competitors to enter our market and for existing competitors to take away our market share. For instance, the impact of the global financial crisis in late 2008 and most of 2009 led to a decrease in the consumption of dairy products in the PRC as consumers likely became more cautious in their consumption of non-necessities such as milk powder for adults. The recent incident relating to hormone-tainted milk formula products in China may undermine consumers' confidence in domestic milk formula products, in particular, pediatric milk formula products, and consumers may avoid their purchase of domestic brand milk formula products in the PRC.

This prompted further competition between leading global brands producers and domestic milk powder manufacturers in China. Many of our existing and potential competitors may have competitive advantages over us in terms of financial, technical and marketing resources. We cannot assure you that our existing or potential competitors will not provide products comparable or superior to those we provide or adapt more quickly than we do to evolving market trends or changing market requirements. It is also possible that significant consolidation of the dairy industry will occur among our competitors, which could result in an increase in the market share of some of our competitors. Our competitors may successfully expand their business upstream in raw milk production, which may enable them to better control the price and quality of the raw milk used to make their products, thereby enhancing their competitiveness. Increased competition may reduce our sales volume, prices and margins. As a result, our business, financial condition and operating results may be materially and adversely affected. We cannot assure you that we will be able to compete effectively against our existing and potential competitors.

Adverse publicity concerning milk formula and other dairy products may affect our business performance or damage our reputation, and their societal impact may lead to additional government regulations.

We are highly dependent on consumers' perception of the quality and safety of our products. As a result, adverse publicity about food safety concerns or contamination in dairy products or an outbreak of any illness or disease in cows in the PRC may lower public confidence in dairy products produced in the PRC, including our products. The occurrence of any of these events may have a material adverse effect on our business, financial condition and operating results.

In 2008, several brands of milk formula and other dairy products in China were found to be contaminated with melamine, which poses health risks for consumers. This led to a nationwide investigation into dairy products, particularly milk formula, for traces of melamine. After a number of domestically sourced infant formula products were found to contain melamine, consumers in the PRC have been shifting their purchase of infant milk formula from domestically sourced infant milk formula to internationally sourced infant milk formula, and as a result, internationally sourced infant milk formula brands experienced an increase in domestic sales of their products. See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Review of Historical Operating Results" for further information on the impact of the melamine incident in 2008 on our operating results.

In August 2010, three infants in Hubei, the PRC were reported to have experienced pubescent development, which was allegedly caused by the content of estrogen hormones found in a particular domestic brand milk formula product they consumed. This resulted in the Ministry of Health of the PRC launching an investigation into the above alleged claims. The clinical investigation conducted by the Ministry of Health of the PRC on the residue of milk powder consumed by these infants revealed that the milk formula products involved did not contain such estrogen hormones that caused these infants' pubescent development. Notwithstanding the above, the incident may undermine consumers' confidence in domestic milk formula products, in particular, pediatric milk formula products and consumers may avoid their purchase of domestic milk formula products in the PRC. This may, in turn, have an impact of the sales of domestic milk formula products in the PRC.

In February 2011, some manufacturers added leather protein powder to dairy products, which were produced from hydrolyzed leather scraps in tanneries, raising milk safety concerns similar to those raised by the melamine incident in 2008. The Ministry of Agriculture of the PRC said in an undated notice posted to the website of the State Council, China's Cabinet, that authorities will carry out 6,450 random checks on fresh milk this year. This incident may further undermine consumers' confidence in domestic milk formula products, thereby affecting the sales of such products in the PRC.

There have also been incidents in the past of milk formula contamination with E. sakazakii (Enterobacter sakazakii), a potentially fatal bacterium. These incidents of dairy product contamination negatively impacted domestic producers of dairy products. There can be no assurance that such incidents of contamination by melamine, E. sakazakii or any other contaminants in dairy products will not occur in the future.

In addition, any major outbreak of any illness or disease in cows such as mad cow disease (bovine spongiform encephalopathy) and bovine tuberculosis may lead to significant shortfalls in the supply of our raw milk and result in loss of consumer confidence in, and demand for, our dairy products. Adverse publicity about contamination, illness or disease in the dairy industry may lower public confidence in the dairy industry and increase governmental regulation of our industry, which may have a material adverse effect on our business, financial condition and operating results.

The PRC milk powder industry may not continue its historical growth rate, and a decline in the markets' growth could materially and adversely affect our business, financial condition and operating results.

According to the Euromonitor Report, the milk powder market in the PRC has grown from approximately RMB37,142 million in 2007 to approximately RMB42,062 million in 2009 in terms of retail sales value. However, there is no guarantee that the milk powder market in the PRC will continue to grow at such a rate in the future. The baby milk powder market in the PRC may experience slower growth in the future due to market saturation, which may impact the size and growth of the market for dairy products in the PRC in general. Growth in the milk powder market in the PRC may also be affected by changes in consumer preferences and needs. If the market experiences a slower or negative growth, our business, financial condition and operating results may be materially and adversely affected.

The PRC government food safety and food production laws and regulations may become more onerous, and our related certificates may be revoked, or may not be renewed or extended, which may materially and adversely affect our business, financial condition and operating results.

Domestic producers of dairy products are required to comply with certain food safety and food production laws and regulations. These laws and regulations establish standards on food and food additives, packaging and containers, and disclosure of information on packaging, as well as set out requirements on food safety, production, sites, facilities and equipment used for the transportation and sale of dairy products. For example, all the existing dairy product enterprises are required to re-apply the National Industrial Production Permit before the end of March 2011 according to the new requirements of inspecting infants formula power and dairy products' production conditions specified by the General Administration of Quality Supervision, Inspection and Quarantine of the PRC ("AQSIQ"), otherwise they will be suspended from producing dairy products and infant formula powder. Furthermore, pursuant to the Program Outline of Rectifying and Promoting the Dairy Industry (奶業整頓和振興規劃綱要) issued in November 7, 2008, all the dairy product enterprises are required to fulfil the standard which is listed in the GMP for the Dairy Product Enterprise (乳製品企業良好生產規範) within three years. Enterprises which fail to fulfil the above standard will be suspended from producing the dairy product. In addition, the infant milk power product enterprises are also required to implement HACCP Management System. See "Regulatory Overview" for further information. We believe that we are in compliance, in all material respects, with current applicable food safety and food production laws and regulations. However, if the PRC government increases the stringency of such laws or regulations, our production and sales costs may increase, and we may be unable to pass these additional costs on to our customers, which may materially and adversely affect our business, financial condition and operating results.

Our PRC legal advisers have also advised us that we have obtained, and are in compliance with, all relevant licenses and certificates, including the National Industrial Production Permit (全國工業產品生產許可證). These licenses and permits are subject to renewal or extension to carry on the business of food production and processing.

However, if any of our licenses or permits is revoked, not renewed or not extended, we may not be able to produce or process our products and our customers may lose confidence in our products, which may have a material and adverse effect on our business, financial condition and operating results**.**

We may be subject to higher compliance costs if PRC environmental protection laws and regulations become more onerous, which may materially and adversely affect our business, financial condition and operating results.

We operate in an industry that is subject to PRC environmental protection laws and regulations. These laws and regulations require enterprises which produce certain environmental waste to effectively manage and treat such waste prior to disposal. Enterprises that fail to comply with such requirements may be subject to fines. Daqing Dairy and Changqing Dairy have obtained the environmental protection approval upon completion of their project constructions. However, there can be no assurance that the PRC government will not change the existing laws or regulations or impose additional or stricter laws and regulations, compliance with which may increase our production costs in ways that may materially and adversely affect our business, financial condition and operating results.

Global market fluctuations and economic downturn may materially and adversely affect our business, financial condition and operating results.

The global financial crisis that unfolded in 2008 and continued in 2009 led to a slowdown in economic growth of the PRC. The adverse impact of the global crisis on the PRC economy may continue or be exacerbated in the future. A recession in the global economy, Asia or the PRC or uncertainties regarding future economic prospects of the PRC may affect consumer spending habits and have a material adverse effect on our business, financial condition and operating results. In particular, although the PRC economy has recorded one of the world's fastest growth rates in terms of GDP, we cannot assure you that such growth will be sustained and continue in the future. In addition, a slowdown in the economies of the United States, the European Union and certain Asian countries with which the PRC has important trade relationships or any future calamities may materially and adversely affect the economic growth of the PRC. If the PRC economy experiences a significant downturn, our business, financial condition, operating results and prospects may be materially and adversely affected.

Risks Relating To Conducting Business in the PRC

Any adverse change in the political and economic policies of the PRC government may materially and adversely affect our business, financial condition and operating results and may result in our inability to sustain our growth and expansion strategies.

Our operations are conducted in the PRC. Accordingly, our operating results, financial condition and prospects are, to a significant degree, subject to the economic, political and legal developments of the PRC.

The PRC economy has largely been a centrally planned economy, which differs from other developed economies of the world in many respects, including:

- its structure;

- the level of governmental involvement;
- the level of development;
- growth rate;
- the control of foreign exchange; and
- the allocation of resources.

As a result of these differences, our business may not develop in the same way or at the same rate as might be expected if the Chinese economy were similar to those of other developed countries. The PRC economy has been transitioning from a planned economy to a more market oriented economy. The PRC government has implemented economic reform measures emphasising utilization of market forces in the development of the PRC economy and is continuing to play a significant role in regulating industries by imposing industrial policies. We cannot, however, predict whether changes in the political, economic and social conditions and policies in the PRC, or in the relevant laws, rules and regulations, will have any material adverse effect on our current or future business, financial condition and operating results.

Inflation in China may have a material adverse effect on our business, financial condition and operating results.

While the PRC economy has experienced rapid growth, such growth has been uneven among various sectors of the economy and in different geographical areas of the country. Rapid economic growth can lead to growth in the money supply and inflation. If prices for our dairy products rise at a rate that is insufficient to compensate for the rise in our costs, our business, financial condition and operating results may be materially and adversely affected. To control inflation in the past, the PRC government has imposed controls on bank credits, limits on loans for fixed assets and restrictions on State bank lending. Such an austere policy can lead to a slow down in the economic growth and may materially and adversely affect our business, financial condition and operating results.

In recent years, the PRC government undertook various measures to alleviate the effects of inflation, especially with respect to key commodities. On January 15, 2008, the PRC National Development and Reform Commission announced national price controls on various products, including milk. Similarly, the PRC government may conclude that the prices of infant formula or our other products are too high and may institute price controls that would limit our ability to set prices for our products as we might wish. The PRC government has also encouraged local governments to institute price controls on similar products. Such price controls could adversely affect our future results of operations.

There are uncertainties regarding the interpretation and enforcement of PRC laws, rules and regulations.

Our operations are conducted in the PRC. The PRC legal system is based on written statutes and thus prior court decisions can only be cited as reference. Since the late 1970s, the PRC government has been developing a comprehensive system of laws, rules and regulations in relation to economic matters, such as foreign investment, corporate organization and governance, commerce, taxation and trade.

However, due to the fact that these laws, rules and regulations have not been fully developed, and because of the limited volume of published cases and their non-binding nature, the interpretation and enforcement of these laws, rules and regulations involve some degree of uncertainties with respect to the outcome of any legal action that may be taken against us in the PRC.

PRC regulations relating to acquisitions of PRC companies by offshore holding companies may limit our ability to acquire PRC companies and may materially and adversely affect the implementation of our acquisition strategies as well as our business and prospects.

The Provisions on the Mergers and Acquisitions of Domestic Enterprises by Foreign Investors 《關於外國投資者併購境內企業的規定》 issued by six PRC ministries and commissions, effective from September 8, 2006 which was revised by MOFCOM on June 22, 2009, as amended (the "M&A

Provisions"), provide rules with which foreign investors must comply should they seek to (i) purchase the equities of the shareholders of a domestic non-foreign-funded enterprise, or subscribe to the increased capital of a domestic non-foreign-funded enterprise, and thus change the domestic non-foreign-funded enterprise into a foreign-funded enterprise, or (ii) set up a foreign-funded enterprise to acquire assets from a domestic enterprise, or assets from a domestic enterprise and set up a foreign-funded enterprise by contribution of the acquired assets. The M&A Provisions stipulate that the business scope upon acquisition of a domestic enterprise must conform to the Foreign Investment Industrial Guidance Catalogue (2007 version)《外商投資產業指導目錄》(2007 年修訂) issued by the National Development and Reform Commission of the PRC (中華人民共和國國家發展和改革委員會) ("NDRC") and MOFCOM. The M&A Provisions also provide the takeovers procedures for equity interests in domestic enterprises.

Our PRC legal advisers have advised us that there are uncertainties as to how the M&A Provisions will be interpreted or implemented. If we decide to acquire a PRC enterprise, we cannot assure you that we or the owners of such PRC enterprise can successfully complete all necessary approval requirements under the M&A Provisions. This may restrict our ability to implement our acquisition strategies and may materially and adversely affect our business and prospects.

We face uncertainty with respect to indirect transfers of equity interests in PRC resident enterprises by their non-PRC holding companies

Pursuant to the Notice on Strengthening Administration of Enterprise Income Tax for Share Transfers by Non-PRC Resident Enterprises《關於加強非居民企業股權轉讓所得企業所得稅管理的通知》, or SAT Circular 698, issued by State Administration of Taxation on December 10, 2009 with retroactive effect from January 1, 2008, where a foreign investor transfers its indirect equity interest in a PRC resident enterprise by disposing of its equity interests in an overseas holding company, and such overseas holding company is located in a tax jurisdiction that (i) has an effective tax rate of less than 12.5% or (ii) does not tax foreign income of its residents, the foreign investor must report such indirect equity transfer to the competent PRC tax authorities with jurisdiction over the PRC resident enterprise. The PRC tax authorities have generally relied on the "substance over form" principle to disregard the corporate existence of the overseas holding company if such corporate existence lacks a reasonable commercial purpose and was established primarily for the purpose of evading PRC taxes. As a result, gains derived from such indirect transfers may be subject to PRC withholding tax at a rate of up to 10%. SAT Circular 698 also provides that, where a non-PRC resident enterprise transfers its equity interests in a PRC resident enterprise to its related parties at a price lower than the fair market value, the relevant PRC tax authorities have the power to make a reasonable adjustment with respect to the taxable income of the transaction.

There exists uncertainty as to the application of SAT Circular 698. For example, while the term "indirect transfer" is not clearly defined, it is understood that the relevant PRC tax authorities have jurisdiction regarding requests for information over a wide range of foreign entities having no direct contact with China. Moreover, the relevant PRC authorities have not yet promulgated any formal announcements or formally declared or stated how to calculate the effective tax rates in foreign tax jurisdictions, or how to report such an indirect transfer to the competent PRC tax authorities. Neither has there been any formal governmental announcement on how to determine the existence of such an abusive arrangement to evade PRC taxes. As a result, we may become at risk of being taxed under SAT Circular 698 upon any future transfer of indirect equity interests in a PRC resident enterprise. We may be required to allocate significant resources to comply with SAT Circular 698 or to establish that we should not be taxed under SAT Circular 698, which may have a material adverse effect on our financial condition and results of operations.

Implementation of the PRC Labor Contract Law and other labor-related regulations in China may materially and adversely affect our business, financial condition and operating results.

The PRC Labor Contract Law《中華人民共和國勞動合同法》and the PRC Labor Contract Law Implementation Rules《中華人民共和國勞動合同法實施條例》took effect on January 1, 2008 and September 18, 2008, respectively. These labor laws and rules impose additional stringent requirements on employers in relation to entering into fixed term employment contracts, hiring of temporary employees and dismissing employees. Pursuant to the PRC Labor Contract Law, since January 1, 2008, we have been required to enter into non-fixed term employment contracts with employees who have worked for us for more than 10 years or, unless otherwise provided in the PRC Labor Contract Law, for whom a fixed term employment contract has been concluded for two consecutive terms. We may not be able to efficiently terminate non-fixed term employment contracts under the PRC Labor Contract Law without cause unless there exist special circumstances as stipulated in the PRC Labor Contract Law Implementation Rules as well as other PRC laws for the termination of employment contracts by the employer. We are also required to make severance payments to fixed term contract employees when the term of their employment contracts expire, unless such employee voluntarily rejects an offer to renew the contract in circumstances where the conditions offered by the employer are the same as or better than those stipulated in the current contract. The amount of severance payment is equal to the monthly wage of the employee multiplied by the number of full years that the employee has worked for the employer, except: (i) where the term of service is more than six months but less than a year, the amount of severance payment shall be calculated as a full year of service; (ii) where the term of service is less than six months, the employer shall pay half a month's wage to the employee as severance payment; and (iii) where the employee's monthly wage is more than three times the average monthly wage of the proceeding year announced by the local relevant PRC government. The calculation of severance payment will be based on a monthly wage equal to three times the average monthly wage multiplied by the number of years of service which cannot exceed a maximum of 12. A minimum wage requirement has also been incorporated into the PRC Labor Contract Law. Liability for damages, fines or other administrative penalties may be imposed for any material breach of the PRC Labor Contract Law. In addition, under the Regulations on Paid Annual Leave for Employees《職工帶薪年休假條例》, which became effective January 1, 2008, employees who have continuously worked for more than one year are entitled to paid holidays ranging from five to 15 days, depending on their length of service. Employees who agree to waive their holiday time at the request of their employers must be compensated with three times their normal daily salaries for each holiday waived. As a result of these PRC laws, rules and regulations, our labor costs have increased. There can be no assurance that any disputes, work stoppages or strikes will not arise in the future. Furthermore, there can be no assurance as to whether there will be additional or new labor laws, rules and regulations in the PRC, which may lead to potential increases in our labor costs and future disputes with our employees. In such circumstances, our business, financial condition and operating results may be materially and adversely affected.

Failure to comply with the regulations of the State Administration of Foreign Exchange of the PRC ("SAFE") relating to the establishment of special purpose vehicles by our controlling shareholder may materially and adversely affect our business operations, limit our ability to inject capital into our PRC subsidiaries, limit the ability of our PRC subsidiaries to distribute profits to us or subject us to fines.

On October 21, 2005, SAFE issued the Notice on Issues Relating to the Administration of Foreign Exchange in Fund-raising and Reverse Investment Activities of Domestic Residents Conducted via Offshore Special Purpose Companies《國家外匯管理局關於境內居民通過境外特殊目的公司融資及返程投資外匯管理有關問題的通知》, which became effective November 1, 2005. The notice requires PRC residents to register with the local SAFE branch in the following circumstances: (i) before establishing or controlling any company (referred to in the notice as a "special purpose vehicles") outside the PRC for the purpose of capital financing; (ii) after contributing their assets or shares of a domestic enterprise into overseas special purpose vehicles, or raising funds overseas after such contributions; and (iii) after any major change in the share capital of the special purpose vehicles without any round-trip investment being made.

As our controlling shareholder is not a PRC resident, the notice would not have a material and adverse effect on our business operations in general as well as the offering. However, if the SAFE promulgates clarifications or regulations in the future requiring our controlling shareholder to comply with such foreign exchange registration requirements in all material respects in connection with our investments and financing activities. If our controlling shareholder or we fail to comply with the relevant SAFE requirements, such failure may subject our controlling shareholder or us to fines and legal sanctions, restrict our ability to inject capital into our subsidiaries in the PRC or limit the ability of our subsidiaries in the PRC to distribute profits to us, thereby, materially and adversely affecting our business, financial condition and operating results.

PRC regulation of loans and direct investment by offshore holding companies to PRC entities may delay or prevent us from using proceeds we receive from this offering to make loans or additional capital contributions to our PRC subsidiaries.

In utilizing the proceeds we receive from this offering in the manner described in "Use of Proceeds," as an offshore holding company of our PRC subsidiaries, our Company may make loans to our PRC subsidiaries, may establish new PRC subsidiaries and make capital contributions to these new PRC subsidiaries or may make additional capital contributions to our PRC subsidiaries by utilizing the proceeds we receive from this offering. However, most of these uses are subject to PRC regulations and approvals. For example: (i) capital contributions to a PRC subsidiary, whether an existing or newly established subsidiary, must be approved by the PRC Ministry of Commerce or its local counterparts; (ii) loans by us to a PRC subsidiary to finance their activities cannot exceed statutory limits and must be registered with SAFE, or its local branches, because the subsidiary is a foreign-invested enterprise; and (iii) loans by us to our consolidated affiliated entity, which is a domestic PRC entity, must be approved by the National Development and Reform Commission and must also be registered with SAFE or its local branches.

Furthermore, on August 29, 2008, SAFE promulgated the Notice on Relevant Business Operations Issues Concerning Improving the Administration of the Payment and Settlement of Foreign Exchange Capital of Foreign-Funded Enterprises《關於完善外商投資企業外匯資本金支付結匯管理有關業務操作問題的通知》 ("Notice 142") which regulates the conversion by a foreign-invested enterprise of foreign currency into Renminbi by restricting how the converted Renminbi may be used. Notice 142 requires that the Renminbi funds converted from the foreign currency capital of a foreign-invested enterprise may only be used for purposes within the business scope approved by the applicable governmental authority and may not be used for equity investments within the PRC unless specifically provided for otherwise. In addition, SAFE strengthened its supervision over the flow and use of the Renminbi funds converted from the foreign currency capital of a foreign-invested enterprise. The use of such Renminbi capital may not be changed without SAFE's approval, and may not, in any case, be used to repay or prepay Renminbi loans if such loans are outstanding. Violations of Notice 142 will result in severe penalties, such as heavy fines as set out in the relevant foreign exchange control regulations.

We cannot assure you that we will be able to obtain the necessary government registrations or approvals on a timely basis, if at all, with respect to our future plans to use the U.S. dollar proceeds we receive from this offering for our expansion and operations in China. If we fail to receive such registrations or approvals, our ability to use the proceeds of this offering and to capitalize our PRC operations may be negatively affected, which could materially and adversely affect our liquidity and ability to fund and expand our business.

We rely principally on dividends paid by our subsidiaries to fund our cash and financing requirements, and any limitation on the ability of our PRC subsidiaries to pay dividends to us and service our debt obligations could have a materially adverse effect on our ability to conduct our business

We are a holding company incorporated in the Cayman Islands and operate our core business primarily through our subsidiaries in the PRC. Therefore, the availability of funds to pay dividends to our shareholders and to service our indebtedness, including the Notes, depends on payments received from these subsidiaries. If our subsidiaries incur any debts or losses, such indebtedness or loss may impair their ability to pay dividends or other distributions to us. As a result, our ability to pay dividends or other distributions and to service our indebtedness will be restricted.

PRC laws, rules and regulations require that dividends be paid only out of the accumulated profit calculated according to PRC accounting standards, which differ from generally accepted accounting principles in other jurisdictions, including IFRS. PRC laws, rules and regulations also require

PRC-incorporated enterprises, such as our subsidiaries in the PRC, to set aside part of their net profit as statutory reserves. These statutory reserves are not available for distribution as dividends. In addition, restrictive covenants in bank credit facilities, convertible bond instruments or other agreements that we or our subsidiaries may enter into in the future, if any, may also restrict the ability of our PRC subsidiaries to make distributions to us. Therefore, these restrictions on the availability and usage of our major source of funding may impact our ability to pay dividends to our shareholders and to service our indebtedness.

We may be deemed to be a PRC tax resident under the PRC Enterprise Income Tax Law《中華人民共和國企業所得稅法》issued on March 16, 2007 which took effect on January 1, 2008 ("EIT Law") and this may subject us to PRC taxation on our worldwide income, require us to withhold taxes on interest we pay on the Notes and require holders of the Notes to pay taxes on gains realized from the sale of the Notes

We are a holding company incorporated in the Cayman Islands and operate our core business primarily through our subsidiaries in the PRC. Under the EIT Law, enterprises established outside China whose "de facto management bodies" are located in China are considered "resident enterprises" and will generally be subject to a uniform 25% PRC Enterprise Income Tax ("EIT") on their worldwide income. Under the Implementing Rules of the PRC Enterprise Income Tax Law《中華人民共和國企業所得稅法實施條例》issued on December 6, 2007 which took effect on January 1, 2008 ("EIT Rules"), "de facto management bodies" are defined as bodies that have material and overall management control over the business, personnel, accounts and properties of an enterprise. Substantially all of our management is currently based in China and may remain in China. Therefore, we may be treated as a PRC resident enterprise for EIT purposes. If we are deemed to be a PRC resident enterprise, we would be subject to the PRC enterprise income tax at the rate of 25% on our worldwide income. Furthermore, we may be obliged to withhold PRC income tax generally at a rate of 10% on payments of interest and other amounts on the Notes to investors that are non-resident enterprises, because the interest and other amounts may be regarded as being derived from sources within China. In addition, any gain realized by such investor that is non-resident enterprises from the transfer of the Notes may be regarded as being derived from sources within China and accordingly may be subject to a 10% PRC withholding tax.

Fluctuations in foreign exchange rates and changes in foreign exchange regulations may materially and adversely affect our business, financial condition, operating results and our ability to remit payments to service our indebtedness denominated in foreign currencies.

Our revenue and expenditures are denominated in Renminbi, which is currently not a freely convertible currency. However, we will require foreign currencies to, among other things, service our indebtedness denominated in foreign currencies. As a result, we are exposed to risks associated with fluctuations in the exchange rates of foreign currency.

The value of Renminbi depends, to a large extent, on the PRC domestic and international economic, financial and political developments and governmental policies, as well as the currency's supply and demand in the local and international markets. Since 1994 till 2005, the conversion of Renminbi into foreign currencies, including Hong Kong and US dollars, has been based on rates set by the PBOC in light of the previous day's interbank foreign exchange market rates in China and the then current exchange rates on the global financial markets. The official exchange rate for the conversion of Renminbi into the U.S. dollar was largely stable until July 2005. The PRC government has, with effect from July 21, 2005, reformed the exchange rate regime by permitting Renminbi to fluctuate within a narrow and managed band based on market supply and demand with reference to a basket of currencies. On July 21, 2005, this revaluation resulted in Renminbi appreciating against the US dollar and Hong Kong dollar by approximately 2%. The PRC government has since made further adjustments to the exchange rate system.

There can be no assurance that such exchange rate will not fluctuate widely against the U.S. dollar or any other foreign currency in the future. Since our income and profits are denominated in Renminbi, any appreciation of Renminbi will increase the value of dividends and other distributions payable by our PRC subsidiaries in foreign currency terms. Conversely, any depreciation of Renminbi will decrease the value of dividends and other distributions payable by our PRC subsidiaries in foreign currency terms. Fluctuation of the value of Renminbi will also affect the amount of our foreign debt service in Renminbi terms since we have to convert Renminbi into foreign currencies to service our indebtedness denominated in foreign currencies.

Acts of God, acts of war, terrorist attacks, epidemics, such as severe acute respiratory syndrome (SARS), H5N1 avian flu or H1N1 influenza, and other disasters, or a combination thereof, such as recently experienced in Japan, may affect our business.

Our business is subject to general and social conditions in the PRC and abroad. Natural disasters, epidemics, acts of God, acts of war and other disasters in the PRC or abroad, or a combination thereof, such as recently experienced in Japan, that are beyond our control may materially and adversely affect the economy, infrastructure and livelihood of the people of the PRC. Areas in the PRC are abroad are under the threat of flood, earthquake, tsunami, sandstorm, drought and other disasters. Our business, financial condition and operating results may be materially and adversely affected if these natural disasters occur. For instance, the March 2011 earthquake off the coast of Japan and the resulting tsunami, disaster at certain nuclear power plants in Japan and spread of radioactive material from the damaged nuclear power plants (which among other things may lead to concerns over radioactive contamination of water and food supplies) may cause damage or disruption to us, our employees, facilities, our distribution channels, markets, suppliers and customers, the occurrence of any of which may materially and adversely impact our business, revenue, cost of sales, financial condition and operating results or share price. The PRC National Nuclear Emergency Coordination Committee has announced that trace amounts of artificially produced radioactive iodine-131 have been found in northeastern Heilongjiang, which is assumed to have originated from the damaged Japanese nuclear power plants. The near and longer-term impact of the recent events in Japan on our company, our suppliers, or our customers is not yet fully quantifiable. Epidemics threaten people's lives and may materially and adversely affect their livelihoods as well as living and consumption patterns. The occurrence of an epidemic is beyond our control and there is no assurance that the outbreak of SARS, H5N1 avian flu or H1N1 influenza will not happen again. Any epidemic occurring in areas in which we operate, or even in areas in which we do not operate, may materially and adversely affect our business, financial condition and operating results. Potential war or terrorist attacks may also cause uncertainties and cause our business to suffer in ways that we cannot currently predict.

We cannot guarantee the accuracy of the facts, forecasts and statistics in this offering memorandum relating to the Chinese economy and the dairy industry in which we operate.

Certain facts, forecasts and other statistics in this offering memorandum relating to the Chinese economy and the dairy industry and market are in part derived directly or indirectly from various publicly available official sources generally believed to be reliable. We also engaged an independent party as an industry expert to collect and provide such information. While we have taken reasonable care to reproduce such information, we cannot guarantee the quality and reliability of such source material. None of us, the Sole Global Coordinator, the Joint Bookrunners, nor the Initial Purchasers or any of its or their respective affiliates, or advisors or any other parties involved in this offering of the Notes has independently verified these materials and, therefore, makes no representations as to the accuracy of such facts, forecasts and statistics, which may not be consistent with other information compiled within or outside the PRC and may not be complete or up-to-date. Due to possibly flawed or ineffective collection methods or discrepancies between published information and market practice and other problems, the facts and the statistics herein, including in the section entitled "Industry Overview" in this offering memorandum, may be inaccurate or may not be comparable to statistics produced by other sources. Further, there can be no assurance that they are stated or compiled on the same basis or with the same degree or accuracy as may be the case elsewhere. In all cases, prospective investors should give consideration as to how much weight or importance they should attach to or place on all such facts and statistics and should not place undue reliance on any of such information and statistics contained in this offering memorandum.

USE OF PROCEEDS

We estimate that the net proceeds from this offering, after deducting the Initial Purchasers' discount and other estimated expenses payable in connection with this offering, will be approximately US$ million. We intend to use the net proceeds from this offering as follows:

- to finance a portion of the second stage of our vertical integration plan which we currently anticipate will include: (i) the development of approximately 25 smaller scale dairy farms in Wuchang and Zhaoyuan with a capacity of up to 700 dairy cows per farm and ancillary facilities such as milking stations and a transportation fleet; (ii) the acquisition or construction of a feed processing plant to support our vertical integration plan; and (iii) the acquisition or construction of additional raw milk processing capacity to complement existing production facilities and support the expansion of our milk formula business; and
- the balance for working capital and general corporate purposes.

We may adjust the timing and amount of actual expenditures in implementing our vertical integration plan in response to future events or developments, such as changing market conditions, the outlook for our industry and where applicable, the historical results and outlook of potential acquisitions targets, the level of demand for our products, changes in social, political and economic conditions, and the regulatory environments in which we operate, and, thus, may reallocate the use of the proceeds. Pending application of the net proceeds of this offering, we intend to invest such net proceeds in "Temporary Cash Investments" as defined under "Description of the Notes."

CAPITALIZATION AND INDEBTEDNESS

The following table sets forth, as of December 31, 2010, the Group's consolidated bank balances and cash, short-term borrowings and capitalization on an actual basis. You should read this information in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and related notes included elsewhere. Except as otherwise disclosed in the table above and elsewhere in this offering memorandum, there have been no material changes in our capitalization since December 31, 2010.

	As at December 31, 2010	
	Actual	
	RMB	US$
	(in thousands)	
Bank balances and cash	1,265,224	191,701
Short-term borrowings	—	—
Long-term borrowings[1]		
Unsecured bank borrowings[2]	100,000	15,152
Capital and reserves		
Share capital	9	1
Reserves	1,590,997	241,060
Total equity	1,591,006	241,061
Total capitalization[3]	1,691,006	256,213

(1) Long-term borrowings exclude the current portion of long-term borrowings.

(2) All of the Group's borrowings in unsecured bank borrowings were incurred by the Company's subsidiaries.

(3) Total capitalization equals long term borrowings plus total equity.

SELECTED CONSOLIDATED FINANCIAL INFORMATION AND OTHER DATA

The selected consolidated statements of comprehensive income data and selected consolidated cash flows data for each of the years ended December 31, 2008, 2009 and 2010 and the selected consolidated statements of financial position data as of December 31, 2008, 2009 and 2010 for the Group, and the selected statements of comprehensive income data and the selected cash flows data for each of the years ended December 31, 2008 and 2009 for the Daqing Dairy Group set forth below (except for EBITDA data) have been derived from the consolidated financial statements for such years and as of such dates audited by Deloitte Touche Tohmatsu, Certified Public Accountants, and included elsewhere in this offering memorandum. Our financial statements have been prepared and presented in accordance with IFRS.

You should read the selected financial data below in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and the notes to those statements included elsewhere in this offering memorandum.

Selected Consolidated Statements of Comprehensive Income Data of the Daqing Dairy Group and the Group

The following table sets forth the selected consolidated statements of comprehensive income data of the Group for the years ended December 31, 2008, 2009 and 2010 and the Daqing Dairy Group for the years ended December 31, 2008 and 2009:

	The Daqing Dairy Group		The Group			
	Year ended December 31,					
	2008	2009	2008	2009	2010	2010
	RMB	RMB	RMB	RMB	RMB	US$
	(in thousands, except per share data and percentages)					
Revenue	433,316	510,035	197,369	510,035	921,886	139,680
Cost of sales	(217,284)	(270,631)	(110,357)	(274,137)	(443,655)	(67,220)
Gross profit	216,032	239,404	87,012	235,898	478,231	72,460
Other gains and losses	(16,929)	5,601	7,039	6,797	(968)	(147)
Selling and distribution expenses	(18,543)	(18,934)	(5,627)	(18,934)	(44,276)	(6,708)
Administrative expenses	(16,890)	(17,047)	(9,000)	(19,134)	(51,717)	(7,836)
Finance costs	(1,833)	(9,025)	(1,423)	(9,258)	(14,672)	(2,223)
Profit before taxation	161,837	199,999	78,001	195,369	366,598	55,546
Income tax expenses	(48,736)	(56,849)	(23,866)	(61,900)	(106,010)	(16,062)
Profit and total comprehensive income	113,101	143,150	54,135	133,469	260,588	39,484
Dividend			—	—	—	—
Earnings per share — basic			0.098	0.242	0.333	0.050
Other Financial Data						
EBITDA [(1)]	191,593	219,266	80,316	219,200	411,200	62,303
EBITDA margin [(2)]	44.2%	43.0%	40.7%	43.0%	44.6%	44.6%

(1) EBITDA for any period consists of profit from operating activities before fair value gains on the investment properties plus depreciation and amortization expenses. EBITDA is not a standard measure under IFRS. EBITDA is a widely used financial indicator of a company's ability to service and incur debt. EBITDA should not be considered in isolation or construed as an alternative to cash flows, net income or any other measure of financial performance or as an indicator of our operating performance, liquidity, profitability or cash flows generated by operating, investing or financing activities. EBITDA does not account for taxes, interest expense or other non-operating cash expenses. In evaluating EBITDA, we believe that investors should consider, among other things, the components of EBITDA such as sales and operating expenses and the amount by which EBITDA exceeds capital expenditures and other charges. We have included EBITDA because we believe it is a useful supplement to cash flow data as a measure of our performance and our ability to generate cash flow from operations to cover debt service and taxes. EBITDA presented herein may not be comparable to similarly titled measures presented by other companies. Investors should not compare our EBITDA to EBITDA presented by other companies because not all companies use the same definition. See "Management's Discussion and Analysis of Financial Condition and Results of Operations" for a reconciliation of our profit for the year/period under IFRS to our definition of EBITDA. Investors should also note that EBITDA as presented herein may be calculated differently from Consolidated EBITDA as defined and used in the Indenture governing the Notes. Interest expense excludes amounts capitalized. See the section entitled "Description of the Notes — Definitions" for a description of the manner in which EBITDA is defined for purposes of the Indenture governing the Notes.

(2) EBITDA margin is calculated by dividing EBITDA by revenue.

Selected Consolidated Cash Flow Information

The table below sets forth the selected cash flow information of the Group for the years ended December 31, 2008, 2009 and 2010 and the Daqing Dairy Group for the years ended December 31, 2008 and 2009 and:

	The Daqing Dairy Group		The Group			
	Year ended December 31,					
	2008	2009	2008	2009	2010	2010
	RMB	RMB	RMB	RMB	RMB	US$
	(in thousands)					
Cash and cash equivalents at beginning of the year................	49,867	68,499	23	68,520	183,972	27,875
Net cash from operating activities .	155,004	187,794	81,477	187,783	370,360	56,115
Net cash used in investing activities..................................	(224,445)	(144,285)	(72,160)	(463,057)	(9,700)	(1,470)
Net cash from financing activities .	88,073	70,000	59,180	390,726	720,592	109,181
Net increase in cash and cash equivalents	18,632	113,509	68,497	115,452	1,081,252	163,826
Cash and cash equivalents at end of the year, represented by bank balances and cash	68,499	182,008	68,520	183,972	1,265,224	191,701

Selected Consolidated Statements of Financial Position of the Group

The table below sets forth the selected consolidated statements of financial position of the Group as of December 31, 2008, 2009 and 2010:

	As of December 31,			
	2008	2009	2010	2010
		RMB		US$
		(in thousands)		
Non-current assets	401,803	596,738	580,321	87,927
Current assets	129,152	233,473	1,302,001	197,273
Current liabilities	457,973	503,841	168,356	25,509
Net current assets (liabilities)	(328,821)	(270,368)	1,133,645	171,764
Total assets less current liabilities	72,982	326,370	1,713,966	259,691
Capital and reserves				
Share capital	—	—	9	1
Reserves	54,135	302,472	1,590,997	241,060
Total equity	54,135	302,472	1,591,006	241,061
Non-current liabilities	18,847	23,898	122,960	18,630
Total equity and non-current liabilities	72,982	326,370	1,713,966	259,691

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with "Selected Consolidated Financial Information and Other Data" and our consolidated financial statements and the consolidated financial statements of the Daqing Dairy Group, including the notes thereto, included elsewhere in this offering memorandum. See "— Basis of Presentation" and "History, Reorganization and Group Structure — Reorganization — Acquisition of the entire equity interest in Daqing Dairy by Global Milk Singapore." The financial information in this discussion is based on the audited consolidated financial statements of the Group for the years ended December 31, 2008, 2009 and 2010 and the audited consolidated financial statements of the Daqing Dairy Group for the years ended December 31, 2008 and 2009 included elsewhere in this offering memorandum. Except where the context indicates otherwise, when we refer to "our revenues," "our sales," "our cost of sales," and other financial data and operating statistics for each of the last three fiscal years, we mean the consolidated revenues, sales, and cost of sales and other financial data and statistics of the Group. Our consolidated financial statements and those of the Daqing Dairy Group were prepared in accordance with IFRS.

The following discussion contains certain forward-looking statements that reflect our current views with respect to future events and financial performance which involve risks and uncertainties. These statements are based on assumptions and analyses made by us in light of our experience and perception of historical trends, current conditions and expected future developments, as well as other factors we believe are appropriate under the circumstances. Our actual results reported in future periods could differ materially from those discussed below. Factors that could cause or contribute to such differences include those discussed under "Risk Factors," and "Business" and elsewhere in this offering memorandum.

Overview of Our Operations

We are a top ten domestic milk powder company in the PRC. According to the Euromonitor Report, we ranked ninth among domestic brand owners and 15th among both foreign and domestic brand owners with a 1.5% market share in the milk powder market in China in terms of sales value in 2009. For the year ended December 31, 2008, the Daqing Dairy Group generated revenues of RMB433.3 million, and for the years ended December 31, 2009 and 2010, we generated revenues of RMB510.0 million and RMB921.9 million, respectively.

We are principally engaged in production, marketing, and sale of medium-to-high and premium priced milk formula products in China. Our dairy products are classified into the following two main categories: milk formula products and whole milk powder products.

We produce a full range of milk formula products and whole milk powder products for infants, children and adults. We believe our infant and pediatric milk formula products supply the balanced nutrition that infants and children need throughout various stages of childhood growth and development. In addition, we produce milk formula products fortified with various vitamins and essential minerals that provide supplements to meet special nutritional requirements for older children, adults, the elderly, and pregnant and lactating women. We believe that our broad range of products targets consumers of different income groups with different product value propositions.

Our main product category, milk formula products, consists of the Shi Jia 仕加 brand, the Emilon 愛美樂 brand and the Daqing 大慶 brand. Our Shi Jia brand consists of premium priced milk formula products that are intended to be suitable for infants and children at different growth stages as well as post-natal women. We market our Shi Jia brand to consumers with high disposable incomes in second-tier cities, particularly eastern coastal cities and certain third-tier cities. Our Emilon brand consists of medium-to-high priced milk formula products already defined up front catering to the changing nutritional needs of growing infants and children. We market our Emilon brand to consumers in second- and third-tier cities. We introduced our You Zhi Series under our Emilon brand in May 2010. The You Zhi Series is currently the most competitively priced product in the Emilon brand, which allows us to compete with smaller regional competitors more effectively, especially in third-tier and below cities. The Daqing brand has two distinct products: Daqing Milk Formula Series and whole milk powder products. Our Daqing Milk Formula Series is targeted at consumers of low-to-medium priced milk formula products, and is intended to be suitable for children, adults and the elderly. We market our Daqing Milk Formula Series to consumers in villages and counties near second- and third-tier cities, particularly in northeastern China. Our whole milk powder products are sold for general consumption, with our 25 kilogram whole milk powder sold to other dairy producers as well as food and beverages manufacturers. In addition, we produce a variety of ice cream products under our Qingru 慶乳 brand.

We primarily sell our milk formula products and whole milk powder products through an extensive network of over 140 distributors in China. Our distributors sell our milk formula products and whole milk powder products directly to retail outlets, such as children's and parenting specialty stores, smaller supermarkets and mom and pop shops in 21 provinces and Chongqing. We have entered into non-exclusive agreements with all of our current distributors, which are generally for a term of one year. For the year ended December 31, 2008, approximately 74.7% of the Daqing Dairy Group's sales were made to its distributors. For the years ended December 31, 2009 and 2010, approximately 69.1% and 85.5% of our Group's sales, respectively, were made to our distributors. In addition to our distribution network, we sell our milk formula products and whole milk powder products directly to department stores, shopping malls and supermarket chains in Daqing and the surrounding areas and other customers who purchase from us on an ad hoc basis. We also sell our whole milk powder directly to our customers such as food processing enterprises and we sell our ice cream products directly to retail outlets in Daqing and the surrounding areas.

Since the establishment of our production facility in Daqing in 1970, we have received various awards and certifications which have helped increase the brand recognition of our products. We source raw milk, the primary raw material for the production of our products, from selected milk collection centers which, in turn, collect raw milk from dairy farms and individual dairy farmers in proximity to Daqing.

We have two production facilities in Daqing and Wuchang. We currently expect the Changqing production facility located in Wuchang to commence operation in second quarter of 2011. The designed annual production capacity of our milk formula products and whole milk powder products was approximately 20,000 metric tons as of December 31, 2010. When the Changqing production facility commences operation, we anticipate that our designed annual milk powder production capacity of our milk formula products and whole milk powder products will be approximately 31,000 metric tons.

With the consummation of our IPO, we commenced a two-stage strategy to realize our vertical integration plan. We intend to use proceeds from the IPO to implement the first stage of our vertical integration plan. The first stage of our vertical integration plan includes the construction of a dairy farm designed to raise dairy cows. We established a new wholly owned subsidiary, Wuchang Benniu, to develop and operate our dairy farm, which we currently plan to complete in 2012. For this purpose, Wuchang Benniu entered into a lease agreement on March 22, 2011 with Wuchang Pingfangdian Tree Farm ("Wuchang Pingfangdian"), pursuant to which Wuchang Benniu has agreed to lease 500 mu (83 acres) of land in Wuchang for a term of 30 years for RMB30,000 per year. Having reviewed and evaluated the progress of the first stage of our vertical integration plan,we intend to proceed with the second stage. We intend to use the net proceeds from this offering to finance a portion of the second stage which we currently anticipate will include: (i) the development of approximately 25 smaller scale dairy farms in Wuchang and Zhaoyuan with a capacity of up to 700 dairy cows per farm and ancillary facilities such as milking stations and a transportation fleet; (ii) the acquisition or construction of a feed processing plant to support our vertical integration plan; and (iii) the acquisition or construction of additional raw milk processing capacity to complement existing production facilities and support the expansion of our milk formula business and for general work capital.

Basis of Presentation

This offering memorandum includes the following financial statements:

- consolidated financial information of the Group for the three years ended December 31, 2008, 2009 and 2010; and

- consolidated financial information of the Daqing Dairy Group for the two years ended December 31, 2008 and 2009.

We have included in this offering memorandum consolidated financial statements and selected financial data for both the Group and the Daqing Dairy Group because, Global Milk Singapore acquired Daqing Dairy on July 25, 2008, an acquisition that has been accounted for using the purchase accounting method in accordance with IFRS. See "History, Reorganization and Group Structure — Reorganization — Acquisition of the entire equity interest in Daqing Dairy by Global Milk Singapore." Accordingly, the consolidated financial information of the Group for the year ended December 31, 2008 did not incorporate the financial information of the Daqing Dairy Group during the period from January 1, 2008 to July 24, 2008. Therefore, in order to help you gain an understanding and increase the comparability of the historical results and related financial condition of our business for the years ended December 31, 2008, 2009 and 2010, we have included in this offering memorandum the consolidated financial information of the Daqing Dairy Group for the two years ended December 31, 2008 and 2009. However, the consolidated financial information of the Group differs from the consolidated financial information of the Daqing Dairy Group in the following principal respects:

- The fair value of Daqing Dairy upon acquisition by Global Milk Singapore was determined by calculating Daqing Dairy's carrying amount before the combination, which was RMB279.7 million, and making certain fair value adjustments of RMB44.3 million (inclusive of deferred tax impact of RMB19.0 million). As a result of the fair value adjustments, the Group's net assets at acquisition were approximately RMB44.3 million greater than Daqing Dairy's net assets as at July 24, 2008.

- The acquisition and its fair value adjustments have several effects on the Group's consolidated statement of comprehensive income. First, the discount on acquisition of RMB5.3 million was recognized as part of other gains and losses for the year ended December 31, 2008. As a result of the Group's fair value adjustment of property, plant and equipment, the Group recognized a greater depreciation expense than the Daqing Dairy Group. For the years ended December 31, 2009, the Group's depreciation of property, plant and equipment was RMB19.2 million, whereas the Daqing Dairy Group's depreciation of property, plant and equipment for the year ended December 31, 2009 was RMB15.7 million. Also, the RMB15.0 million fair value adjustment for the Emilon trademark is amortised on a straight line basis over a period of 10 years. The Group's amortization of trademarks, which is recognized as part of the administration expenses, was RMB0.6 million and RMB1.5 million for the years ended December 31, 2008 and 2009, respectively, whereas the Daqing Dairy Group's amortization of trademarks for the year ended December 31, 2009 was RMB20,000. As a result of the fair value adjustment for inventories, the Group's gross profit differed from that of the Daqing Dairy Group's gross profit for the year ended December 31, 2008 in part due to the actual selling price and cost of sales versus the estimated selling price and cost of sales used in the fair value adjustment. For the year ended December 31, 2009, the Group's release of prepaid lease payments was RMB0.7 million, whereas the Daqing Dairy Group's release of prepaid lease payments for the same period was RMB135,000, as a result of changes in the fair value of the prepaid lease payments for land use rights. For the year ended December 31, 2009, the Group's income tax expense was RMB61.9 million, whereas the Daqing Dairy Group's income tax expense for the year ended December 31, 2009 was RMB56.8 million, as a result of the Group's recognition of RMB5.1 million in deferred taxation in the year ended December 31, 2009 as part of the Group's fair value adjustment for deferred taxation. See "Related Party Transactions" and "— Operating results — Administrative Expenses".

- The level of debt at the Daqing Dairy Group level only reflects a portion of the total debt of the Group, which is fully consolidated at the Group level. See "— Liquidity and Capital Resources."

- The consolidated financial information of the Daqing Dairy Group represented the consolidated financial information of the Daqing Dairy Group for the two years ended December 31, 2008 and 2009 and of Changqing Dairy from the effective date of acquisition by Daqing Dairy on November 16, 2009 to December 31, 2009. However, the consolidated financial information of our Group for the years ended December 31, 2008, 2009 and 2010 incorporated the financial information of our Company and Global Milk Singapore from October 15, 2009 and January 1, 2008, respectively, and also the consolidated financial information of the Daqing Dairy Group from July 25, 2008 to December 31, 2010. The financial information of our Group and the Daqing Dairy Group have been prepared on different bases and lengths of periods and accordingly, the financial information of the Group and the Daqing Dairy Group are not directly comparable.

In addition, although Global Milk Singapore was incorporated on September 15, 2006, Global Milk Singapore did not commence its business operations until its acquisition of the entire equity interest of Daqing Dairy on July 25, 2008. The Group only had substantial business operations from July 25, 2008 and, as such, we do not discuss below a comparison of the Group's operating results for year ended December 31, 2009 compared with the year ended December 31, 2008.

Factors Affecting Our Operating Results and Financial Position

Our business, financial position and operating results, as well as the period-to-period comparability of our operating results, have been and will continue to be affected by a number of factors, some of which are beyond our control, including those set forth below.

Demand for Our Products

We generate our revenue primarily from the sale of milk formula products and whole milk powder products, with medium-to-high priced and low-to-medium priced milk formula products as our major products. In general, demand for our products reflects demand for milk powder products in China and, in particular, demand for milk formula products. This in turn depends on factors such as China's economic conditions, rate of urbanization, rate of increase in household disposable income and number of newborns each year. However, we can also be affected by these factors on smaller regional or economic scales because some of our products target consumers in different geographic locations in China with differing consumer purchasing power. In addition, brand recognition and customer loyalty can also affect demand for our products. We have a history of more than 40 years in the dairy industry in the PRC and we believe that our longstanding history in the PRC has contributed to our positive brand recognition and reputation, which have been instrumental to the success and growth of our business. We also believe that our commitment to providing quality products has generated brand loyalty among a segment of the consumer population, which further enhances the prospective success and growth of our business.

Pricing of Our Products

Market forces of supply and demand generally determine the pricing of our products. Our gross profits are principally derived from the price difference between the costs of raw milk, packaging materials, other raw materials and production costs we incur and the price at which we are able to sell our products to our customers.

The following table sets forth the Daqing Dairy Group's and our average sales revenue per metric ton for the products and periods indicated:

	The Daqing Dairy Group		The Group		
	Year ended December 31,				
	2008	2009	2008	2009	2010
	RMB (in thousands) per metric ton				
Milk formula products	61.5	54.6	59.1	54.6	61.6
Whole milk powder products	22.7	21.8	22.8	21.8	24.5
Others [(1)]	5.4	4.6	5.4	4.6	4.1

(1) The sale of other products represents the sale of our ice cream products.

We price our Emilon brand and Daqing brand milk formula products differently. In setting our pricing policy, we take into account current market trends, production costs, consumers' acceptable price range, the consumer groups at which the products are targeted, our competitors' prices, and the economic condition of the relevant regions. We provide our distributors with suggested wholesale and retail prices for our milk formula products and whole milk powder products. Depending on economic conditions, our distributors may, with our approval, increase the selling prices by up to 10% above our suggested selling prices. We generally will not adjust upwards the selling price of our products to our distributors if our distributors increase the selling prices of the products by up to 10% above our suggested selling prices with our approval. In general, our Emilon brand products have a higher average selling price and higher profit margins as they are designed for consumers of medium-to-high priced milk formula products, while our Daqing brand milk formula products are designed for consumers of low-to-medium priced milk formula products. The average sales revenue of the Daqing Dairy Group milk formula products declined from RMB61,500 per metric ton for the year ended December 31, 2008 to RMB54,600 per metric ton for the year ended December 31, 2009 primarily due to a higher sales growth rate of 37.7% for our Daqing brand, which has a lower average selling price, as compared with a sales growth rate of 11.3% for our Emilon brand. Our average selling price per metric ton of milk formula products increased to RMB61,600 for the year ended December 31, 2010 primarily due to the introduction of our Shi Jia brand during 2010.

Product Mix

The sales mix of our products affects our gross profit margins as different products have different selling prices and costs of sales. We believe that consumers have diverse needs and a preference for a wide selection of product offerings. In recognition of our consumers' interests, our product offerings include a wide range of products designed to meet diverse consumer preferences and needs. Since the acquisition of the Daqing Dairy Group, we have focused on promoting our milk formula products for infants and children. We have recently developed and launched our Shi Jia brand milk formula products which target at customers of premium priced milk formula products. The mix of products demanded by our customers varies depending on factors such as general economic conditions and consumer preferences. Our products are classified into two primary categories: milk formula products and whole milk powder products. Our milk formula products and whole milk powder products accounted for 92.4% and 5.2% of our revenue, respectively, for the year ended December 31, 2010. Our milk formula products and whole milk powder products include a full range of products for infants, children and adults. Our main product category, milk formula products, consists of the Shi Jia brand, the Emilon brand and the Daqing brand. The milk formula products in our Shi Jia brand are designed for consumers of premium priced milk formula products, those in our Emilon brand are designed for consumers of medium-to-high priced milk formula products, while those in our Daqing brand are designed for consumers of low-to-medium priced milk formula products. Recently, we introduced our You Zhi Series under our Emilon brand in May 2010. The You Zhi Series is currently the most competitively priced product in the Emilon brand, which allows us to compete with smaller regional competitors more effectively, especially in third-tier and below cities. Our whole milk powder products are sold under the Daqing brand. Our Daqing whole milk powder, packaged in 25 kilogram bags, is usually used as a raw material in dairy and other food products. In addition, we sell Daqing sweetened whole milk powder, which is suitable for all age groups (other than infants and toddlers below the age of three). See "Business — Products."

Production Capacity

Our sales volume is dependent on our production capacity. All of the milk formula products and whole milk powder products sold to our consumers are manufactured in our production plants under a strict quality control system. See "Business — Production." We have recently completed the construction of the phase two production line at our Daqing production facility and the production line at our Changqing production facility. The Changqing production facility was acquired as part of the acquisition of Changqing Dairy by the Daqing Dairy Group in November 2009. The designed annual production capacity of our milk formula products and whole milk powder products was approximately 20,000 metric tons as of December 31, 2010. We anticipate that, when production in the Changqing production facility comes online, our designed annual milk powder production capacity of our milk formula products and whole milk powder products will be approximately 31,000 metric tons. The volume of raw milk supply we require depends on the demand for our products. We believe that there is a sufficient number of raw milk collection centers in Heilongjiang from which we can purchase raw milk, and we therefore expect to be able to source sufficient raw milk for our production in 2011. Furthermore, we expect to have an internal raw milk supply from 2012 onwards once the dairy farms that are part of our vertical integration plan commence operations.

The following table sets forth the Daqing Dairy Group's and our sales volume and revenue of each product line for the periods indicated:

	The Daqing Dairy Group				The Group					
	Year ended December 31,									
	2008		2009		2008		2009		2010	
	Volume	Revenue	Volume	Revenue	Volume	Revenue	Volume	Revenue	Volume	Revenue
	(metric tons)	RMB (in thousands)	(metric tons)	RMB (in thousands)	(metric tons)	RMB (in thousands)	(metric tons)	RMB (in thousands)	(metric tons)	RMB (in thousands)
Milk formula products..	5,955.0	366,482	7,906.1	431,605	2,696.2	159,244	7,906.1	431,605	13,821.5	851,845
Whole milk powder products	2,866.3	65,034	2,829.8	61,671	1,591.5	36,345	2,829.8	61,671	1,975.1	48,320
Others [(1)]......................	331.5	1,800	3,659.3	16,759	331.5	1,800	3,659.3	16,759	5,352.3	21,721

(1) The sale of other products represents the sale of our ice cream products.

The sales volume of milk formula product by the Daqing Dairy Group increased by 32.8% from 5,955.0 metric tons for the year ended December 31, 2008 to 7,906.1 metric tons in the year ended December 31, 2009 as a result of the expansion of our distribution network. The sales volume of our milk formula products further increased by 74.8% to 13,821.5 metric tons in the year ended December 31, 2010 as a result of the expansion of our distribution network. Given the enlargement of our distribution network and the related increase in demand for our milk formula products and whole milk powder products in aggregate in 2009 and until March 2010, we sourced approximately 1,669 metric tons and 300 metric tons, respectively, of whole milk powder from 黑龍江金天然乳業有限責任公司

Heilongjiang Jintianran Dairy Co., Ltd.* The externally sourced whole milk powder product was sold under our Daqing brand in order to free up our milk powder production capacity to meet the demand for our milk formula products, which have higher profit margins. See also "Related Party Transactions."

Cost of Raw Materials

Raw milk is the primary raw material for the production of our products, representing 64.0%, 33.9% and 48.7% of our total cost of purchases for the years ended December 31, 2008, 2009 and 2010, respectively. Apart from raw milk, we purchase other raw materials and packaging materials for the production of our products. The cost of purchases of other raw materials represented 25.0%, 52.9% and 38.0% of our total cost of purchases, and the cost of purchases of packaging materials represented 11.0%, 13.2% and 13.3% of our total cost of purchases for the years ended December 31, 2008, 2009 and 2010, respectively. The other raw materials include sucrose, whey powder, vegetable oil, mineral supplements, lactose, maltose, whey protein concentrate and various flavorings. Apart from whey powder, lactose and whey protein concentrate, which are imported into China through domestic distributors, the other raw materials and packaging materials are sourced within China.

The price of raw milk is volatile and is influenced by a variety of factors such as geographic location, seasonal factors and the overall demand for raw milk. We have been able to meet our raw milk supply requirements by entering into non-exclusive raw milk supply agreements with milk collection centers which collect raw milk from dairy farms and individual dairy farmers in proximity to Daqing. These agreements are generally for a term of one year. The price of the raw milk we purchase is subject to negotiation between the suppliers and us at the time of purchase. If raw milk price increases and the selling prices for our products do not increase by an amount sufficient to offset the effects of such increase in the raw milk price, our profitablility will be adversely affected.

The amount of raw milk we purchased for our production decreased by 17.0% from 53,475 metric tons in the year ended December 31, 2008 to 44,363 metric tons in the year ended December 31, 2009 due to our strategy of focusing on milk formula products. The amount of raw milk we purchased increased by 70,966 metric tons in the year ended December 31, 2010 as a result of the commencement of operations at the phase two production line at our Daqing production facilities in May 2010. We expect that we will need to continue to increase the amount of raw milk we source to meet our growing needs. Going forward, with the anticipated increase in our milk powder production capacity as a result of the completion of the new production line at our Changqing production facility, we intend to proceed with the implementation of the second stage of our vertical integration plan, which is designed to increase raw milk production levels. We have been able to meet our packaging material supply requirements by generally entering into one-year supply contracts with packaging material suppliers. The packaging material supply contracts we entered into were generally based on the agreed prices stipulated in these agreements. Our costs for packaging materials are also dependent on the number of product lines we carry and the frequency with which we upgrade the packaging we use for our products. We intend to focus on ensuring that our product packaging appeals to rapidly changing consumer preferences.

Advertising and Promotion

We engage in promotion and advertising activities in order to develop consumer awareness of our products and brands as well as increase our market share. We have appointed advertising and public relations companies to implement various promotional activities for our products to penetrate further into the local milk formula market. During the years ended December 31, 2008, 2009 and 2010, these advertising and public relations companies launched a number of promotional activities to generate publicity for, and increase awareness of, our products, including advertisements on Central China Television (CCTV) and various television channels in Heilongjiang and Shandong, advertisements on buses, roadshows, as well as participation in the Confectionery and Alcohol Convention in the PRC. We intend to increase the scope of our promotional activities to include direct advertising campaigns on newspapers, magazines, the Internet and other media as well as participation in product promotional activities.

Tax

Our profits are affected by changes in tax rates, particularly the effective tax rates payable in China. PRC enterprise income tax is calculated based on taxable income determined under PRC tax laws and regulations. In accordance with the relevant tax laws and regulations in the PRC, the Group's subsidiaries in the PRC were subject to enterprise income tax of 25% with effect from January 1, 2008.

Seasonality

We experience seasonal fluctuations in our revenue. During the years ended December 31, 2008, 2009 and 2010, revenue generated in the first half of the year was generally lower than revenue generated in the second half of the year as we typically experience higher sales of milk formula products and whole milk powder products in the second half of the year compared to the first half. We believe this pattern of seasonality is formed mainly due to increases in purchases by our distributors in order to increase their inventories before the Chinese New Year in anticipation of higher demand around the holiday period.

As a result of the seasonality of our revenue, our operating results may fluctuate from quarter to quarter. An analysis of our interim performance may not be a good indicator of our full year results due to the seasonality of our sales.

The table below sets forth the revenue of the Daqing Dairy Group and the Group for the first and second of the year for each of the periods indicated:

	The Daqing Dairy Group				The Group					
	Year ended December 31,									
	2008		2009		2008		2009		2010	
	RMB (in thousands)	%	RMB (in thousands)	%	RMB (in thousands)	%	RMB (in thousands)	%	RMB (in thousands)	%
First half	189,609	43.8	212,192	41.6	—	—	212,192	41.6	373,867	40.6
Second half	243,707	56.2	297,843	58.4	197,369	100.0	297,843	58.4	548,019	59.4
Total	433,316	100.0	510,035	100.0	197,369	100.0	510,035	100.0	921,886	100.0

Quality Control and Consumer Perception

In July 2008, several infants in Gansu in the PRC were diagnosed with kidney stones after consuming milk powder products produced by a milk formula producer in the PRC that were contaminated with melamine. This led to a nationwide investigation into dairy products, particularly milk formula products, for traces of melamine. According to the investigation carried out by the AQSIQ in 2008 on the products of 109 milk formula product producers in the PRC, the products of 22 milk formula product producers in the PRC (which did not include us) were found to have been contaminated with melamine. The AQSIQ subsequently also carried out random sampling tests on the content of melamine in the products of various dairy product producers in the PRC, including us, which revealed that: (i) our Daqing Hi-Calcium and Hi-Iron Milk Formula for women (400 grams per box) and Daqing Multi-Vitamin Hi-Calcium Milk Formula (for the elderly and the middle-aged) (400 grams per box) under our Daqing Milk Formula Series; and (ii) our Follow-up Milk Formula (Stage 2) under our Emilon brand (400 grams per box), which were subject to the tests, passed the melamine tests. The PRC government has subsequently taken stringent measures to ensure safety of dairy products such as the recall, removal from retail shelves and destruction of the milk formula products that were contaminated with melamine. The AQSIQ has also sent officers to quality control departments of the milk formula product producers in the PRC to monitor their production processes and inspect the quality and safety of the finished products.

Our Emilon brand, which targets or is marketed to consumers of the middle-to-high income group in second- and third-tier cities, has been negatively affected by the melamine incident. As a result, some consumers within this target customer group who generally have stronger purchasing power switched to imported brands of milk formula products. While this slowed down the rate of revenue growth of our Emilon brand, sales of our Emilon brand products still increased despite the difficult market conditions. On the other hand, our Daqing Milk Formula Series recorded faster revenue growth as a result of the melamine incident, which led certain dairy companies in China that were affected by the melamine incident to exit the market. As consumers in rural areas in China generally have lower purchasing power, they had less ability to switch to imported brands as those are generally higher-priced products. As a result, consumers in these areas tended to switch to other unaffected domestic brands such as our Daqing Milk Formula Series, which targets or is marketed to consumers in villages and counties near second- and third-tier cities.

Critical Accounting Policies

We have identified below the accounting policies that we believe are the most critical to our audited consolidated financial information. These accounting policies require the most difficult, subjective or complex judgments of our management, often as a result of the need to make estimates about the effect of matters which are inherently uncertain. Certain accounting estimates are particularly sensitive because of their significance to our audited consolidated financial information. The estimates and associated assumptions are based on historical experience and various other factors that we believe are reasonable under the circumstances, the results of which form the basis of making judgements about matters that are not readily apparent from other sources. Actual results may differ from these estimates.

We review our estimates and underlying assumptions on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Our financial information has been prepared under the historical cost basis as explained in the accounting policies set forth below. Our financial information has been prepared in accordance with the following accounting policies which conform to IFRS. These policies have been consistently applied throughout the years ended December 31, 2008, 2009 and 2010. See the audited financial statements and related notes included elsewhere in this offering memorandum.

Revenue Recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods sold provided in the normal course of business, net of discounts and sales related taxes. Revenue from sale of goods is recognized when goods are delivered and legal title is passed. Interest income from a financial asset is accrued on a time basis, by reference to the principal outstanding and at the effective 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 on initial recognition.

Foreign Currencies

Our financial information is presented in the currency of the primary economic environment in which our company and our principal subsidiaries operate, namely Renminbi. In preparing the financial information, transactions in currencies other than the functional currency of that entity (foreign currencies) are recorded in the respective functional currency (i.e. the currency of the primary economic environment in which the entity operates) at the rates of exchange prevailing on the dates of the transactions. At the end of each reporting period, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the end of the reporting period. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are recognized in profit or loss in the period in which they arise.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax. The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated statement of comprehensive income because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

Deferred tax is recognized on temporary differences between the carrying amounts of assets and liabilities in the consolidated financial information and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognized for all taxable temporary differences and deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilized. Such assets and liabilities are not recognized if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

The carrying amount of deferred tax assets is reviewed at the end the reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered. Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realized, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities. Deferred tax for the year is recognized in profit or loss, except when it relates to items that are recognized in other comprehensive income or directly to equity, in which case, the deferred tax is also recognized in other comprehensive income or directly in equity.

Borrowing Costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, are capitalized as part of the cost of those assets. Capitalization of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalization. All other borrowing costs are recognized in profit or loss in the period in which they are incurred.

Property, Plant and Equipment

Property, plant and equipment, other than construction in progress, are stated at cost, less subsequent accumulated depreciation and subsequent accumulated impairment losses, if any.

Construction in progress represents property, plant and equipment in the course of construction for production, supply or administrative purposes are carried at cost, less any recognized impairment loss. Costs include professional fees and, for qualifying assets, borrowing costs capitalized in accordance with the Group's accounting policy. Such properties are classified to the appropriate categories of property, plant and equipment when completed and ready for intended use. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

Depreciation is recognized so as to write off the cost of property, plant and equipment, other than construction in progress, less their residual values over their estimated useful lives, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis.

An item of property, plant and equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in profit or loss.

Prepaid Lease Payments

Prepaid lease payments represent payments for leasehold land and are amortized over the lease terms on a straight-line basis. Prepaid lease payments which are to be amortized in the next twelve months or less are classified as current assets.

Business Combinations

Business combinations prior to January 1, 2010

The acquisitions of businesses under business combination were accounted for using the purchase method. The cost of the acquisition was measured at 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 that meet the conditions for recognition were recognized at their fair values at the acquisition date.

Goodwill arising on acquisition was recognized as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognized. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeded the cost of the business combination, the excess was recognized immediately in profit or loss. Business combinations achieved in stages were accounted for as separate steps. Goodwill was determined at each step. Any additional acquisition did not reflect the previously recognized goodwill.

Business combinations on or after January 1, 2010

Acquisitions of businesses are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of the assets transferred by the Group, liabilities incurred by the Group to former owners of the acquiree and the equity interests issued by the Group in exchange for control of the acquiree. Acquisition-related costs are recognized in profit or loss as incurred. At the acquisition date, the acquiree's identifiable assets, liabilities and liabilities assumed are recognized at their fair values at the acquisition date, except that:

- deferred tax assets or liabilities and liabilities or assets related to employee benefit arrangements are recognized and measured in accordance with IAS 12 "Income Taxes" and IAS 19 "Employee Benefits" respectively;
- liabilities or equity instruments related to share-based payment transactions of the acquiree or the replacement of an acquiree's share-based payment transactions with share-based payment transactions of the Group are measured in accordance with IFRS 2 "Share-based Payment"; and
- assets (or disposal groups) that are classified as held for sale in accordance with IFRS 5 "Non-current Assets Held for Sale and Discontinued Operations" are measured in accordance with that standard.

- Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree, and the fair value of the acquirer's previously held equity interest in the acquiree (if any) over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed. If, after assessment, the Group's interest in the fair value of the acquiree's identifiable net assets exceeds the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree and the fair value of the acquirer's previously held interest in the acquiree (if any), the excess is recognized immediately in profit or loss as a bargain purchase gain.

Where a business combination is achieved in stages, the Group's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date (i.e. the date when the Group obtains control) and the resulting gain or loss, if any, is recognized in profit or loss.

Changes in the value of the previously held equity interest recognized in other comprehensive income and accumulated in equity before the acquisition date are reclassified to profit or loss when the Group obtains control over the acquiree.

Goodwill

Goodwill arising on an acquisition of a business is carried at cost less any accumulated impairment losses and presented separately in the consolidated statements of financial position. For the purposes of impairment testing, goodwill arising from an acquisition is allocated to each of the relevant cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the acquisition. A cash-generating unit to which goodwill has been allocated is tested for impairment annually, and whenever there is an indication that the unit may be impaired. For goodwill arising on an acquisition in a year, the cash-generating unit to which goodwill has been allocated is tested for impairment before the end of that year. When the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated to reduce the carrying amount of any goodwill allocated to the unit first, 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 recognized directly in the profit or loss. An impairment loss for goodwill is not reversed in subsequent periods.

On disposal of the relevant cash-generating unit, the attributable amount of goodwill capitalized is included in the determination of the amount of profit or loss on disposal.

Trademarks

Trademarks acquired in a business combination are identified and recognized separately from goodwill where it satisfies the definition of an intangible asset and its fair values can be measured reliably. The costs of trademarks are their fair value at the acquisition date. Subsequent to initial recognition, the amount will be amortised on a straight line basis over its useful lives.

Gains and losses arising from derecognition of an intangible asset, measured as the difference between the net disposal proceeds and the carrying amount of the asset, are recognized in profit or loss when the asset is derecognized.

Impairment of Tangible and Intangible Assets other than Goodwill

At the end of each reporting period, we review the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognized as an expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior years. A reversal of an impairment loss is recognized as income immediately.

Inventories

Inventories are stated at the lower of cost and net realizable value. Cost is calculated using the weighted average method.

Description of Certain Consolidated Statement of Comprehensive Income Items

Revenue

We generate revenue primarily from the sale of milk formula products and whole milk powder products. Milk formula products and whole milk powder products are primarily sold to our distributors, although some products are sold directly to customers.

The table below sets forth the Daqing Dairy Group's and the Group's revenue by main product types for the periods indicated:

	The Daqing Dairy Group				The Group					
	Year ended December 31,									
	2008		2009		2008		2009		2010	
	RMB (in thousands)	%	RMB (in thousands)	%	RMB (in thousands)	%	RMB (in thousands)	%	RMB (in thousands)	%
Milk formula products:										
Shi Jia brand	—	—	—	—	—	—	—	—	43,395	4.7
Emilon brand...........	277,234	64.0	308,669	60.5	119,030	60.3	308,669	60.5	647,028	70.2
Daqing brand	89,248	20.6	122,936	24.1	40,194	20.4	122,936	24.1	161,422	17.5
Total	366,482	84.6	431,605	84.6	159,224	80.7	431,605	84.6	851,845	92.4
Whole milk powder products	65,034	15.0	61,671	12.1	36,345	18.4	61,671	12.1	48,320	5.2
Others [(1)]......................	1,800	0.4	16,759	3.3	1,800	0.9	16,759	3.3	21,721	2.4
Total	433,316	100	510,035	100	197,369	100	510,035	100	921,886	100

(1) The sale of other products represents the sale of our ice cream products.

Sales to the top five customers of the Daqing Dairy Group for the years ended December 31, 2008 and 2009 were RMB125.0 million and RMB82.4 million which accounted for 28.8% and 16.2%, respectively, of the Daqing Dairy Group's revenue during that year. Sales to the Group's top five customers were RMB57.1 million, RMB82.4 million and RMB67.5 million for the years ended December 31, 2008, 2009 and 2010, respectively, which accounted for approximately 28.9%, 16.2% and 7.3%, respectively, of our revenue during those periods. The decline in the percentage contribution of the top five customers of the Daqing Dairy Group and our top five customers over the three years ended December 31, 2008, 2009 and 2010 was a result of the Group expanding its distribution network to increased number of distributors in different geographic areas and reducing its concentration risk.

The Daqing Dairy Group's revenue and our revenue are presented net of any returned products and net of sales discounts. We have pre-set annual sales targets for our distributors. In each year, if the relevant distributor meets the pre-set annual sales target, we grant a sales rebate to the relevant distributor in an amount equivalent to 3% of the annual sales (including 17% VAT) from the relevant distributor (excluding the sales of our whole milk powder packaged in 25 kilogram bags). Although we do not have any quarterly sales target for our distributors, we grant quarterly sales rebates to our select distributors in an amount equivalent to 5% of the quarterly sales (including 17% VAT) from such distributor.

The amounts of both quarterly and annual sales rebates are deducted from the purchase price payable by the relevant distributor in subsequent orders. The quarterly and annual sales rebates effectively mean that we offer our milk formula products and whole milk powder products (excluding the sales of our whole milk powder packaged in 25 kg bags) at a discount of 5% off our unit selling price (including 17% VAT) of our milk formula products and whole milk powder products to those distributors to which we grant such rebates and that an additional 3% discount is offered if our distributors meet our pre-set annual sales targets.

Cost of Sales and Gross Margins

For the years ended December 31, 2008 and 2009, the Daqing Dairy Group's costs of sales were RMB217.3 million and RMB270.6 million, respectively. For the years ended December 31, 2008, 2009 and 2010, our costs of sales were RMB110.4 million, RMB274.1 million and RMB443.7 million, respectively. The main components of our cost of sales are purchases of raw materials, adjusted for movements in opening and closing inventory and manufacturing costs as at the end of each year.

The table below sets forth the purchases of raw materials by the Daqing Dairy Group and the Group for the periods indicated:

	The Daqing Dairy Group				The Group					
	Year ended December 31,									
	2008		2009		2008		2009		2010	
	RMB (in thousands)	%	RMB (in thousands)	%	RMB (in thousands)	%	RMB (in thousands)	%	RMB (in thousands)	%
Raw milk	116,752	60.9	83,419	33.9	56,492	64.0	83,419	33.9	195,201	48.7
Whole milk powder (1)	—	—	34,320	13.9	—	—	34,320	13.9	6,000	1.5
Packaging materials	23,845	12.4	32,568	13.2	9,728	11.0	32,568	13.2	53,493	13.3
Other milk formula ingredients (2)	46,468	24.2	86,267	35.1	18,857	21.4	86,267	35.1	132,836	33.2
Others (3)	4,745	2.5	9,533	3.9	3,154	3.6	9,533	3.9	13,176	3.3
Total purchases	191,810	100.0	246,107	100.0	88,231	100.0	246,107	100.0	400,706	100.0

(1) This comprises mainly whole milk powder packaged from Heilongjiang Jintianran Dairy Co., Ltd.* of RMB33.4 million and RMB6.0 million in 2009 and 2010 respectively. See "Related Party Transactions."

(2) Other milk formula ingredients comprise primarily whey powder, sucrose, vegetable oil and mineral supplements approved for use in the production of milk formula products.

(3) Others comprise primarily coal and other consumables.

The single largest component of our raw materials purchases was raw milk. Our raw milk is sourced from selected milk collection centers which, in turn, collect raw milk from dairy farms and individual dairy farmers in proximity to Daqing. The price of raw milk we purchase is subject to negotiation between the suppliers and us at the time of purchase which is in turn influenced by a variety of factors, including seasonal factors and the overall demand for raw milk. For the years ended December 31, 2008 and 2009, the Daqing Dairy Group's cost of purchases of raw milk amounted to RMB116.7 million and RMB83.4 million which accounted for approximately 60.9% and 33.9% of its total cost of purchases during those periods. For the years ended December 31, 2008, 2009 and 2010, our cost of purchases of raw milk amounted to RMB56.5 million, RMB83.4 million and RMB195.2 million, respectively, which accounted for approximately 64.0%, 33.9% and 48.7%, respectively, of our total cost of purchases during those periods.

The table below sets forth the Daqing Dairy Group's and the Group's gross margins by product type for the periods indicated:

	The Daqing Dairy Group		The Group		
	Year ended December 31,				
	2008	2009	2008	2009	2010
	%	%	%	%	%
Milk formula products:					
Shi Jia brand	—	—	—	—	71.8
Emilon brand	63.0	59.3	59.4	59.3	59.8
Daqing brand	39.7	39.0	34.3	39.0	33.8
Total	57.3	53.5	53.1	53.5	55.5
Whole milk powder products	10.2	18.4	8.9	18.4	3.6
Overall	49.9	46.9	44.1	46.3	51.9

The gross profit margin of the Daqing Dairy Group decreased from 49.9% for the year ended December 31, 2008 to 46.9% for the year ended December 31, 2009, primarily due to a decrease in the gross profit margins for milk formula products, which was partially offset by an increase in the gross profit margin for whole milk powder products. The gross profit margin of the Daqing Dairy Group for our milk formula products declined from 57.3% for the year ended December 31, 2008 to 53.5% for the year ended December 31, 2009 primarily due to the decline in the gross profit margin of the Emilon brand milk formula products by 3.7%. This decline resulted from changes in the sales mix of the Emilon brand product offerings, with more of the lower margin Emilon Bei Cong Series being sold compared to the higher-margin Emilon Shuang Neng Series as target consumers in the higher-end market segment were more affected by the melamine incident in 2008.

The gross profit margin of the Group increased to 51.9% for the year ended December 31, 2010 primarily due to the introduction of our Shi Jia brand, which had a higher gross profit margin of 71.8% in the year ended December 31, 2010 and the increase in contribution to our total revenue of higher-margin milk formula products, namely our Emilon and Shi Jia brands, from 60.5% in the year ended December 31, 2009 to 74.9% in the year ended December 31, 2010.

Other Gains and Losses

Other gains comprised mainly interest income earned from cash deposited with major banks and accrued interest income arising from a pre-acquisition loan granted to Changqing Dairy, the discount to fair value of the acquisition by the Daqing Dairy Group, gains on sales of scrap materials and foreign exchange differences. Other losses related to losses of a non-operating nature such as the disposal of fixed assets and loss on sale of raw materials. Other gains and losses for the Group differed from those of the Daqing Dairy Group because the Group's financial information for the year ended December 31, 2008 included a gain of RMB5.3 million from the discount on acquisition arising from the acquisition of the entire equity interest of Daqing Dairy. In addition, the Group's other gains and losses for the year ended December 31, 2009 consisted of unrealized exchange gains on loans from certain shareholders that were denominated in foreign currency.

The table below sets forth the Daqing Dairy Group's and the Group's other gains and losses for the periods indicated:

	The Daqing Dairy Group		The Group		
	Year ended December 31,				
	2008	2009	2008	2009	2010
	RMB (in thousands)				
Interest income	2,007	8,490	1,771	8,494	971
Discount of acquisition	—	—	5,268	—	—
Loss on disposals of property, plant and equipment	—	(250)	—	(366)	(590)
Impairment loss of property, plant and equipment [(1)]	(18,936)	—	—	—	—
Loss on sales of raw materials [(2)]	—	(2,890)	—	(2,890)	—
Gains on sales of scrap materials [(3)]	—	251	—	251	—
Exchange gains (losses)	—	—	—	1,308	(1,349)
Total	(16,929)	5,601	7,039	6,797	(968)

(1) Impairment loss of property, plant and equipment resulted from the impairment of the Daqing Dairy Group's standby production line which was scheduled for upgrades that exceeded its carrying value, prior to the acquisition by the Group.

(2) Loss on sales of raw materials resulted from the unbilled VAT on the Daqing Dairy Group's sale of RMB17.0 million worth of flavoring essence and generic package materials to Jintianran Dairy in 2009. See "Related Party Transactions."

(3) Gains on sales of scrap materials relates to the Daqing Dairy Group's sale of 3,388 cubic metres of boiler slag to 大慶市百信源商品混凝土有限公司 (Daqing City Baixinyuan Concrete Products Co., Ltd*, "Daqing Baixinyuan") for an aggregate consideration of approximately RMB251,000 pursuant to an agreement dated December 5, 2008.

Selling and Distribution Expenses

Selling and distribution expenses primarily consist of sales staff and welfare costs, freight and insurance costs and advertising and promotional expenses. We engage logistics companies to deliver our milk formula products and whole milk powder products to our customers' designated places. We use our own vehicles and transportation team to deliver our ice cream products to our customers and to deliver our milk formula products to our customers to whom we sell our products directly in Daqing. We bear the cost of delivering our products to our customers.

The table below sets forth additional details regarding the Daqing Dairy Group's and the Group's selling and distribution expenses for the periods indicated:

	The Daqing Dairy Group		The Group		
	Year ended December 31,				
	2008	2009	2008	2009	2010
	RMB (in thousands)				
Staff and welfare costs	1,266	2,079	743	2,079	4,031
Freight and insurance	2,564	3,465	1,273	3,465	6,774
Advertising and promotion	13,558	11,422	2,957	11,422	28,490
Others	1,155	1,968	663	1,968	4,981
Total	18,543	18,934	5,627	18,934	44,276

Administrative Expenses

Administrative expenses consist mainly of administrative staff and welfare costs, depreciation of property, plant and equipment, property related taxes and trademark usage fees. Depreciation relates primarily to property, plant and equipment and is calculated on a straight-line basis over the estimated useful lives of buildings of 20 years and for furniture fixtures and office equipment of five years. Administrative expenses of the Group differ from that of the Daqing Dairy Group as the former includes the amortization of the implied fair value of our "Emilon" brand trademark that the Group has indirectly acquired via the acquisition of the entire equity interest of the Daqing Dairy Group as well as other administrative expenses incurred by our Company.

The table below sets forth additional detail regarding the Daqing Dairy Group's and the Group's administrative expenses for the periods indicated:

	The Daqing Dairy Group		The Group		
	Year ended December 31,				
	2008	2009	2008	2009	2010
	RMB (in thousands)				
Staff and welfare costs	4,278	5,629	2,095	5,629	7,981
Depreciation	1,432	3,462	1,163	3,462	5,297
Property usage taxes	1,528	2,259	627	2,259	4,774
Trademark usage fees	5,926	—	1,858	—	—
Amortization of trademark	—	20	625	1,520	1,520
Professional fees related to the IPO	—	—	—	—	21,570
Others	3,726	5,677	2,632	6,264	10,575
Total	16,890	17,047	9,000	19,134	51,717

Finance Cost

Finance cost primarily consists of interest on bank loans and a finance lease on certain motor vehicles and a processing fee on a short term loan from Kenmoore Mezza9 Ltd, Venstar Investments Pte. Ltd., 2G Capital Pte Ltd, NF Capital Partners Limited, Magic Carpet Fund III, Providence SOGF Limited, Blooming Global Holdings Limited, Broad Idea Investment Limited, Lee Yong Miang and Chua Keng Woon (the "Pre-IPO Investors"). The finance costs of the Daqing Dairy Group differed from that of the Group as a result of the processing fee charged by the Group's investors for the extension of a bridge loan of S$21.0 million to our Company. The S$21.0 million bridge loan together with interest charged was fully repaid in November 2010.

The table below sets forth additional detail regarding the Daqing Dairy Group's and the Group's finance costs for the periods indicated:

	The Daqing Dairy Group		The Group		
	Year ended December 31,				
	2008	2009	2008	2009	2010
	RMB (in thousands)				
Interest on bank borrowings	1,710	9,025	1,386	9,025	5,815
Interest on loans from Pre-IPO Investors	—	—	—	233	8,857
Interest on finance lease	123	—	37	—	—
Total	1,833	9,025	1,423	9,258	14,672

Tax

We are not taxed on a consolidated basis. Our company was incorporated in the Cayman Islands in 2009 and is accordingly exempted from corporate tax in its country of incorporation. Global Milk Singapore is an investment holding company and has not to date generated any taxable income. In accordance with the relevant tax laws and regulations in the PRC, the Group's subsidiaries in the PRC were subjected to enterprise income tax of 25% with effect from January 1, 2008. The Group's consolidated tax expense was greater than that of the Daqing Dairy Group due to the provision for deferred tax liabilities on changes in the fair value of net assets acquired on the acquisition of Daqing Dairy and for withholding taxes on potential offshore dividends payable to our company.

The table below sets forth additional detail regarding the Daqing Dairy Group's and the Group's tax expenses for the periods indicated:

	The Daqing Dairy Group		The Group		
	Year ended December 31,				
	2008	2009	2008	2009	2010
	RMB (in thousands)				
PRC enterprise income tax	48,736	56,849	19,273	56,849	110,389
Deferred taxation	—	—	4,593	5,051	(4,379)
Total	48,736	56,849	23,866	61,900	106,010

Review of Historical Operating Results

The following discussion is based on the consolidated operating results of the Daqing Dairy Group for the years ended December 31, 2008 and 2009 and the consolidated operating results of the Group for the years ended December 31, 2009 and 2010.

The Group's operating results for the year ended December 31, 2010 compared to the Group's operating results for the year ended December 31, 2009

Revenue. Our revenue increased by 80.8% from RMB510.0 million for the year ended December 31, 2009 to RMB921.9 million for the year ended December 31, 2010. The increase was driven by a strong growth in the sales of our milk formula products across all ranges by RMB420.2 million and the growth in the sales of our ice cream products by RMB5.0 million, which was offset by a decline of RMB13.4 million in the sales of our whole milk powder products.

The growth in revenue of our milk formula products for the year ended December 31, 2010 was driven by the following factors:

(i) The growth in our distribution network from 67 direct distributors in the year ended December 31, 2009 to 143 direct distributors in the year ended December 31, 2010;

(ii) Launch of milk formula products for infants and post-natal mothers under the You Zhi Series under our Emilon brand and Shi Jia brand in May 2010. These new products contributed RMB183.7 million in revenue or 20% of our total revenue in the year ended December 31, 2010; and

(iii) The removal of capacity constraints faced in the year ended December 31, 2009 with the commencement of operations of the new phase two raw milk production lines at our Daqing facilities in May 2010.

Cost of sales. Our cost of sales increased by RMB169.6 million or 61.9% from RMB274.1 million for the year ended December 31, 2009 to RMB443.7 million for the year ended December 31, 2010. The percentage increase in our cost of sales for the year ended December 31, 2010 was lower than the percentage increase in revenue for the same period. This was primarily due to the change in product mix in favor of higher-margin milk formula products under our Emilon brand and Shi Jia brand, which resulted in lower cost of sales incurred per dollar of sales.

Gross profit. Our gross profit increased by RMB242.3 million or 102.7% from RMB235.9 million for the year ended December 31, 2009 to RMB478.2 million for the year ended December 31, 2010. Our gross profit margin increased from 46.3% for the year ended December 31, 2009 to 51.9% for the year ended December 31, 2010 primarily due to the introduction of our Shi Jia brand with higher gross profit margin of 71.8% in the year ended December 31, 2010 and the increase in contribution to our total revenue of the higher-margin milk formula products in Emilon brand and Shi Jia brand from 60.5% for the year ended December 31, 2009 to 74.9% for the year ended December 31, 2010.

Other gains and losses. Our other losses for the year ended December 31, 2010 amounted to RMB1.0 million which consisted of exchange losses of RMB1.3 million arising from exchange losses on a foreign currency denominated loan owing to Pre-IPO Investors that was repaid during the year and bank balances held in foreign currency, loss of disposal of property plant and equipment of RMB0.6 million, offset by interest income of RMB1.0 million.

Selling and distribution expenses. Our selling and distribution expenses increased by RMB25.4 million or 134.4% from RMB18.9 million for the year ended December 31, 2009 to RMB44.3 million for the year ended December 31, 2010. The increase was primarily due to an increase in advertising and promotional expenses by RMB17.1 million resulting from an advertising and marketing campaign on CCTV to increase brand awareness and to attract more potential distributors to our network. In addition, our staff and welfare costs increased by RMB2.0 million as we increased head counts in connection with the expansion of our distribution network and our freight and insurance cost increased by RMB3.3 million as a result of increased sales of our products.

Administrative expenses. Our administrative expenses increased by RMB32.6 million or 170.7% from RMB19.1 million for the year ended December 31, 2009 to RMB51.7 million for the year ended December 31, 2010. The increase was primarily due the professional fees we incurred in connection with our IPO, which amounted to RMB21.6 million, as well as the increase in administration staff costs, depreciation and additional property usage tax arising from Daqing Dairy amounting to RMB2.4 million, RMB1.8 million and RMB2.5 million, respectively.

Finance cost. Our finance cost increased by RMB5.4 million or 58.1% from RMB9.3 million in the year ended December 31, 2009 to RMB14.7 million in the year ended December 31, 2010. The increase was primarily due to the interest accrued from the second loan extended by the Pre-IPO Investors in January 2010 amounting to RMB8.9 million, offset in part by a decrease in the interest on bank borrowings as a result of lower outstanding bank loan balances in the year ended December 31, 2010 as compared to the corresponding period in 2009.

Income Tax Expense. Our income tax expense increased by 71.2% from RMB61.9 million for the year ended December 31, 2009 to RMB106.0 million for the year ended December 31, 2010. This increase was primarily due to an increase in profit, which was partially offset by a decrease in the effective tax rate from 31.7% to 28.9% for the year ended December 31, 2009 as compared to the year ended December 31, 2010. The effective tax rate decreased because no provision was made in 2010 for withholding tax on potential dividend distributions to the Group's offshore holding company as management decided to retain undistributed profits for the year ended December 31, 2010 for the purpose of expanding the business.

Profit for the year. Our profit for the year increased by 95.2% from RMB133.5 million for the year ended December 31, 2009 to RMB260.6 million for the year ended December 31, 2010, as a result of the factors discussed above, and our net profit margin increased from 26.2% to 28.3%.

The Daqing Dairy Group's operating results for the year ended December 31, 2009 compared to the Daqing Dairy Group's operating results for the year ended December 31, 2008

Revenue. The Daqing Dairy Group's revenue increased by 17.7% from RMB433.3 million for the year ended December 31, 2008 to RMB510.0 million for the year ended December 31, 2009, primarily as a result of the improved performance of our milk formula business. Revenue from the Daqing Dairy Group's milk formula products increased by 17.8% from RMB366.5 million for the year ended December 31, 2008 to RMB431.6 million for the year ended December 31, 2009, primarily due to the sales growth of the Daqing brand of 37.7% during the year ended December 31, 2009 and the sales growth of the Emilon brand of 11.3% during the year ended December 31, 2009. Our Emilon brand of milk formula products, which are targeted at consumers in the middle-to-high income group in the second- and third-tier cities in China, was negatively affected during the year ended December 31, 2009 as a result of the melamine incident that occurred in September 2008. As a result, some consumers within this target customer group switched to imported brands of milk formula products during the year ended December 31, 2009. While this resulted in a slower rate of the Daqing Dairy Group's revenue growth of the Emilon brand products during the year ended December 31, 2009, sales of the Daqing Dairy Group's Emilon brand products still increased despite the difficult market conditions.

As a result of the melamine incident, certain producers of milk products in China exited the market. As a result, the Daqing Dairy Group's revenue from the Daqing brand milk formula products grew by 37.7% in the year ended December 31, 2009 as compared to the year ended December 31, 2008.

Revenue from the Daqing Dairy Group's whole milk powder products decreased by 5.1% from RMB65.0 million for the year ended December 31, 2008 to RMB61.7 million for the year ended

December 31, 2009, primarily due to the diversion of more production resources towards fulfilling market demand for the Daqing Dairy Group's milk formula products. Revenue from products other than whole milk powder and milk formula products increased from RMB1.8 million for the year ended December 31, 2008 to RMB16.8 million for the year ended December 31, 2009, primarily due to growth of the Daqing Dairy Group's ice cream products, the production of which began in 2008.

Costs of Sales. The Daqing Dairy Group's costs of sales increased by 24.5% from RMB217.3 million for the year ended December 31, 2008 to RMB270.6 million for the year ended December 31, 2009, which was higher than the corresponding percentage increase in the Daqing Dairy Group's revenue. The rise in costs of sales was primarily due to an increase in the amount of whey powder and mineral supplements required for the production of milk formula products as a result of the shift in focus from whole milk powder products to milk formula products. This increase in cost of sales was partially offset by a reduction in the average purchase cost of raw milk from RMB2,150 per metric ton for the year ended December 31, 2008 to RMB1,880 per metric ton for the year ended December 31, 2009 and a reduction in the volume of raw milk consumed for production as a result of the shift from whole milk powder products, which requires more raw milk than milk formula products.

Gross profit. The Daqing Dairy Group's gross profit increased by 10.8% from RMB216.0 million for the year ended December 31, 2008 to RMB239.4 million for the year ended December 31, 2009. However, the Daqing Dairy Group's gross profit margin decreased from 49.9% for the year ended December 31, 2008 to 46.9% for the year ended December 31, 2009, due to a decrease in the gross profit margin of the Daqing Dairy Group's milk formula products. This decrease was partially offset by an increase in gross profit margin of the Daqing Dairy Group's whole milk powder products. The Daqing Dairy Group's gross profit margin for the Daqing Dairy Group's milk formula products declined 3.8% from 57.3% for the year ended December 31, 2008 to 53.5% for the year ended December 31, 2009. The decline in gross profit margin for the Daqing Dairy Group's milk formula products was primarily due to the decline in the gross profit margin for the Emilon brand milk formula by 3.7% during the year ended December 31, 2009, as a result of changes in the sales mix of the Emilon brand product offerings with more lower margin Emilon Bei Cong Series being sold compared to the higher margin Emilon Shuang Neng Series as target consumers in the higher priced market segment were affected by the melamine incident.

The impact of the cost increase for the Daqing brand milk formula products was mitigated by an increase in selling prices for certain Daqing Dairy Group's products under the Daqing brand since the last quarter of the year ended December 31, 2008. The gross profit margin of the Daqing Dairy Group's whole milk powder increased by 8.2% from 10.2% for the year ended December 31, 2008 to 18.4% for the year ended December 31, 2009, primarily due to the full year impact of an increase in the selling prices for the Daqing Dairy Group's Daqing sweetened whole milk powder since the last quarter of the year ended December 31, 2008 as well as a reduction in the average purchase cost of raw milk from RMB2,150 per metric ton for the year ended December 31, 2008 to RMB1,880 per metric ton for the year ended December 31, 2009.

Other Gains and Losses. The Daqing Dairy Group's other losses were RMB16.9 million for the year ended December 31, 2008 compared to the Daqing Dairy Group's other gains of RMB5.6 million for the year ended December 31, 2009. The Daqing Dairy Group's other losses of RMB16.9 million for the year ended December 31, 2008 was primarily due to an impairment loss recognized in respect of property, plant and equipment amounting to RMB18.9 million, due to our continuing plant renewal plan to replace older equipment, partially offset by interest income of RMB2.0 million. The Daqing Dairy Group's other gains of RMB5.6 million for the year ended December 31, 2009 were primarily due to interest income of RMB8.5 million, of which RMB8.1 million was due to interest income accrued on a loan provided to Changqing Dairy from January 1, 2009 to the date of its acquisition by the Daqing Dairy Group, which was partially offset by a loss on the sale of raw materials comprising generic packaging materials and food essence mainly related to the production of ice cream to a related company of RMB2.9 million. See "Related Party Transactions."

Selling and Distribution Expenses. The Daqing Dairy Group's selling and distribution expenses increased by 2.2% from RMB18.5 million for the year ended December 31, 2008 to RMB18.9 million for the year ended December 31, 2009, primarily due to an increase in staff and welfare expenses of RMB0.8 million due to an increase in sales personnel required to handle the expanded distribution network, an increase in freight and insurance expenses of RMB0.9 million in line with higher revenue for the year ended December 31, 2009 and an increase in other miscellaneous selling expenses of RMB0.8 million, partially offset by a reduction in advertising and promotion expenses of RMB2.1 million. The reduction in advertising and promotion expenses was primarily due to the scaling back of promotional activities such as free gifts and samples for the Emilon brand as such promotions would have limited effect in the aftermath of the melamine incident.

Administrative Expenses. The Daqing Dairy Group's administrative expenses increased by 0.6% from RMB16.9 million for the year ended December 31, 2008 to RMB17.0 million for the year ended December 31, 2009, which was lower than the corresponding increase in the Daqing Dairy Group's revenue, primarily due to an increase in staff and welfare expenses of RMB1.4 million as more management level positions were created in the year ended December 31, 2009 to handle the expansion of operations, an increase in depreciation expenses of RMB2.0 million and property related taxes arising from a full year of operations from the Daqing Dairy Group's newly completed staff canteen, warehouses and conference center in the second half of 2008 and a general increase in miscellaneous administrative expenses of RMB2.0 million. These increases were partially offset by the absence of trademark usage fees for the year ended December 31, 2009 pertaining to the "Daqing" trademark which we acquired from a related party in January 2009, as compared to RMB5.9 million of similar fees for the year ended December 31, 2008. See "Related Party Transactions."

Finance Costs. The Daqing Dairy Group's finance costs increased by 392.3% from RMB1.8 million for the year ended December 31, 2008 to RMB9.0 million for the year ended December 31, 2009, primarily due to interest costs arising from an increase in bank borrowings from RMB60.0 million to RMB200.0 million as at the end of the relevant periods.

Income Tax Expense. The Daqing Dairy Group's income tax expense increased by 16.6% from RMB48.7 million for the year ended December 31, 2008 to RMB56.8 million for the year ended December 31, 2009. This increase was primarily due to an increase in profit, which was partially offset by a decrease in the effective tax rate from 30.1% to 28.4% from the year ended December 31, 2008 to the year ended December 31, 2009 due to a decrease in non-deductible expenses for the year ended December 31, 2009.

Profit for the year. The Daqing Dairy Group's profit for the year increased by 26.6% from RMB113.1 million for the year ended December 31, 2008 to RMB143.2 million for the year ended December 31, 2009, as a result of the factors discussed above, and the Daqing Dairy Group's net profit margin increased slightly from 26.1% to 28.1%.

Liquidity And Capital Resources

We have funded our operations principally through cash generated from our operations and our capital expenditures through a combination of cash generated from our operations, bank borrowings, and the proceeds from our IPO.

Principal liquidity and capital requirements relate to costs and expenses related to the operation of our business and the operation of our production facilities, and capital expenditures for the upgrade of existing facilities and construction of new production facilities.

Cash Flows

The following discussion is based on the consolidated statements of cash flows of the Daqing Dairy Group for the years ended December 31, 2008 and 2009 and the Group for the years ended December 31, 2008, 2009 and 2010.

The following table summarizes the Daqing Dairy Group's and the Group's cash flows for the periods indicated:

	The Daqing Dairy Group		The Group		
	Year ended December 31,				
	2008	2009	2008	2009	2010
	RMB (in thousands)				
Net cash inflow from operating activities	155,004	187,794	81,477	187,783	370,360
Net cash used in investing activities	(224,445)	(144,285)	(72,160)	(463,057)	(9,700)
Net cash inflow from financing activities	88,073	70,000	59,180	390,726	720,592
Cash and cash equivalents at the end of period	68,499	182,008	68,520	183,972	1,265,224

Cash Flows Activities of the Group

Cash flows from operating activities

Our net cash inflow generated from operating activities for the year ended December 31, 2010 was RMB370.4 million, which was primarily due to the cash inflow of RMB409.6 million from operating cash flow before movement in working capital and working capital changes resulting in cash inflow of RMB58.8 million before adjusting for the income tax and interest paid of RMB86.2 million and RMB11.8 million respectively.

Our net cash inflow generated from operating activities for the year ended December 31, 2009 was RMB187.8 million which was slightly less than the Daqing Dairy Group's net cash flows from operating activities due to certain expenses incurred by the Company and Global Milk Singapore.

Our net cash inflow generated from operating activities for the year ended December 31, 2008 was RMB81.5 million. The difference between the operating cash flows of the Daqing Dairy Group and the Group for the year ended December 31, 2008 was primarily due to the Group having only generated revenues from production for the period from July 25, 2008, the date the Group acquired the Daqing Dairy Group, to December 31, 2008, whereas the Daqing Dairy Group generated revenues for the entire year ended December 31, 2008.

Cash flows from investing activities

Our net cash used in investing activities was RMB9.7 million for the year ended December 31, 2010, including cash used to acquire property, plant and equipment of RMB11.1 million, which was partially offset by a net cash inflow of RMB0.5 million arising from the sale of property, plant and equipment and interest income received of RMB1.0 million.

Our net cash used in investing activities for the year ended December 31, 2009 was RMB463.1 million. The difference between the cash flows from investing activities of the Daqing Dairy Group and the Group for the year ended December 31, 2009 was primarily due to the payment of RMB318.8 million by the Group to the previous shareholders of Daqing Dairy, which was owed in connection with the acquisition of Daqing Dairy.

Our net cash used in investing activities for the year ended December 31, 2008 was RMB72.2 million. The difference between the cash flows from investing activities of the Daqing Dairy Group and the Group for the year ended December 31, 2008 was primarily due the Group's net cash inflow of RMB93.1 million as a result of the Daqing Dairy acquisition while the Daqing Dairy Group paid RMB59.4 million for the purchase of property plant and equipment, most of which occurred prior to the acquisition of Daqing Dairy by the Group.

Cash flows from financing activities

Our net cash generated from financing activities for the year ended December 31, 2010 was RMB720.6 million, and consisted of proceeds raised from the IPO of RMB943.8 million, bank loans of RMB100.0 million, amount advanced from a related party of RMB50.0 million and loans from the Pre-IPO Investors of RMB44.9 million, offset by the repayment of bank borrowings of RMB200.0 million, the repayment of loans from the Pre-IPO Investors of RMB76.5 million, cash paid to Zhao Yu, our controlling shareholder, of RMB37.8 million, transaction costs attributable to the issue of new shares of RMB53.8 million and the repayment of an amount advanced by a related party of RMB50.0 million.

Our net cash generated from financing activities for the year ended December 31, 2009 was RMB390.7 million. The difference between the cash flows from financing activities of the Daqing Dairy Group and the Group for the year ended December 31, 2009 was primarily due to the subscription money received of RMB102.3 million from various investors, a capital injection by Zhao Yu, our controlling shareholder, of RMB114.9 million and the receipt of proceeds of RMB103.6 million from a loan provided by certain shareholders. The subscription money received relates to a subscription of 127,829 shares by the investors for an aggregate subscription price of RMB102.3 million and the capital injection by Zhao Yu relates to a subscription of 63,171 shares for an aggregate subscription price of RMB125.0 million (RMB114.9 million of which had been received as at December 31, 2009).

The loan of RMB103.6 million was a S$21 million bridge loan from certain of our shareholders, which while valued for the accounts as a RMB102.3 million loan, resulted in cash inflow of RMB103.6 million due to exchange fluctuations between the date of the loan and the date of cash was received by the Group. See "Related Party Transactions."

The Group's net cash generated from financing activities for year ended December 31, 2008 was RMB59.2 million. The difference between the cash flows generated from financing activities of the Daqing Dairy Group and the Group for the year ended December 31, 2008 was primarily due to the receipt of a RMB30.0 million loan by the Daqing Dairy Group prior to the acquisition of Daqing Dairy by the Group.

Cash Flows Activities of the Daqing Dairy Group

Cash flows from operating activities

The Daqing Dairy Group's net cash inflow generated from operating activities for the year ended December 31, 2009 was RMB187.8 million. This was primarily due to the cash inflow of RMB216.7 million arising from operating cash flows before movements in working capital and working capital changes resulting in a cash inflow of RMB24.9 million before adjusting for income tax and interest paid of RMB44.7 million and RMB9.0 million, respectively. Cash inflow from working capital changes was primarily due to a decrease in inventory of RMB23.4 million and an increase in trade and other payables of RMB13.2 million, partially offset by an increase in trade and other receivables of RMB11.8 million. The increase in trade and other receivables was primarily due to an increase in trade receivables, advances to suppliers and prepayments due to increases of sales and production. The increase in trade and other payables was due to an increase in advance payments from distributors who order our products.

The Daqing Dairy Group's net cash inflow generated from operating activities for the year ended December 31, 2008 was RMB155.0 million. This was primarily due to the cash inflow of RMB191.6 million arising from operating cash flows before movements in working capital and working capital changes resulting in a cash inflow of RMB16.0 million before adjusting for income tax and interest paid of RMB50.7 million and RMB1.8 million, respectively. Cash inflow from working capital changes was primarily due to a decrease in inventory and trade and other receivable of RMB1.5 million and RMB10.4 million, respectively, and increase in trade and other payables by RMB4.1 million due to better working capital management.

Cash flows from investing activities

The Daqing Dairy Group's net cash used in investing activities of RMB144.3 million for the year ended December 31, 2009 resulted from cash used to acquire property, plant and equipment of RMB125.3 million, which related to the construction of the phase two production line at our Daqing production facilities and the new production line at our Changqing production facility, and additional amounts advanced to Changqing Dairy prior to the acquisition of Changqing Dairy by the Daqing Dairy Group in November 2009 of RMB52.5 million, partially offset by a net cash inflow of RMB32.9 million arising from the acquisition of Changqing Dairy in November 2009, interest received of RMB0.4 million and proceeds from disposal of property, plant and equipment of RMB0.2 million.

The Daqing Dairy Group's net cash used in investing activities of RMB224.4 million for the year ended December 31, 2008 resulted from the use of RMB81.1 million to acquire property, plant and equipment relating to the construction of a staff canteen and ancillary facilities and from advances to Changqing Dairy prior to its acquisition by Daqing Dairy of RMB150.0 million, partially offset by proceeds from the sale of property, plant and equipment of RMB6.2 million and interest income received of RMB0.5 million.

Cash flows from financing activities

The Daqing Dairy Group's net cash generated from financing activities for the year ended December 31, 2009 was RMB70.0 million, and consisted of proceeds raised from bank loans of RMB160.0 million which was partially offset by the repayment of bank borrowings of RMB60.0 million and the repayment of an amount advanced by a third party of RMB30.0 million.

The Daqing Dairy Group's net cash generated from financing activities for the year ended December 31, 2008 was RMB88.1 million, and consisted of proceeds raised from a bank loan of RMB70.0 million and an amount advanced by a third party of RMB30.0 million, partially offset by the repayment of bank borrowings of RMB10.0 million and finance lease obligations with respect to motor vehicles amounting to RMB1.9 million.

Capital Resources

Working Capital

As of December 31, 2008, 2009 and 2010, the Group's aggregate cash and cash equivalents amounted to RMB68.5 million, RMB184.0 million and RMB1,265.2 million, respectively. As at December 31, 2010, we had committed, unutilized banking facilities of RMB200.0 million. In order to improve our working capital position, leverage ratio and operating cash flows going forward, we plan to seek longer term financing opportunities, including syndicated loans, the issuance of corporate debt securities, such as the Notes offered hereby, and equity and equity-linked financings. Our ability to service our debt obligations may be limited by our financial condition and results of operations and the liquidity of the international and domestic financial markets.

Capital Commitments

We had the following outstanding capital commitments as at December 31, 2010 in respect of the acquisition of property, plant and equipment contracted for but not provided for in our financial information:

	As at December 31, 2010
	RMB (in thousands)
Contracted, but not provided for	11,189
Authorized, but not contracted for	298,580
Total	309,769

As at December 31, 2010, we had capital commitments of RMB309.8 million primarily due to the investment in and construction of our dairy farm in Erhe Township, Wuchang in connection with the first stage of our vertical integration plan which was authorized by our board of directors in November 2010. We intend to use approximately HK$350.9 million (RMB295.2 million) of the net proceeds from our IPO to fund this project and we will satisfy the remaining capital expenditure requirements with internally generated cash flows. We currently expect that our first stage plan will involve: (i) the acquisition of the right to use the requisite parcel of land upon which we will construct our dairy farm, an office building and other ancillary facilities (in connection with which Wuchang Benniu has entered into a land lease agreement with Wuchang Pingfangdian Tree Farm on March 22, 2011 and which will involve payment of further license and permit fees for leasing, occupying and using such land to develop our dairy farm); (ii) the construction of our dairy farm, an office building and other ancillary facilities (including a bio-organic fertilizer and bio-gas power generation facility); (iii) the purchase of dairy cows; and (iv) related working capital for the operation of the farm.

Borrowings

At the close of business on December 31, 2010, the Group had outstanding indebtedness of approximately RMB100.0 million, consisting of long-term bank borrowings. Except as aforesaid or as otherwise disclosed herein, and apart from intra-group liabilities, the Group did not have any outstanding loan capital issued and outstanding or agreed to be issued, bank overdrafts, loans or other similar indebtedness, liabilities under acceptances or acceptable credits, debentures, mortgages, charges, hire purchases commitments, guarantees or other material contingent liabilities at the close of business on December 31, 2010.

Bank borrowings and other loans of the Daqing Dairy Group and the Group are set forth below for the periods presented:

	The Daqing Dairy Group		The Group			
	As at December 31,					
	2008	**2009**	**2008**	**2009**	**2010**	**2010**
	RMB	**RMB**	**RMB**	**RMB**	**RMB**	**US$**
			(in thousands)			
Borrowings due within one year						
Bank borrowings						
- Secured on assets of the Group	30,000	30,000	30,000	30,000	—	—
- Unsecured	30,000	170,000	30,000	170,000	—	—
Borrowings from Pre-IPO Investors	—	—	—	102,275	—	—
	60,000	200,000	60,000	302,275	—	—
Borrowings due over one year						
Bank borrowings						
- Unsecured	—	—	—	—	100,000	15,152
Total borrowings	60,000	200,000	60,000	302,275	100,000	15,152

The outstanding borrowings of the Group as of December 31, 2010 are repayable as follows

	Within one year	More than one year, but not exceeding two years	More than two years, but not exceeding five years	More than five years	Total
	RMB	**RMB**	**RMB**	**RMB**	**RMB**
			(in thousands)		
Bank debt at parent level	—	—	—	—	—
Bank debt at PRC subsidiary level	—	—	100,000	—	—
Total	—	—	100,000	—	100,000

The Daqing Dairy Group's borrowings

The Daqing Dairy Group had bank financing of RMB200.0 million as at December 31, 2009, consisting of three separate loans of RMB100.0 million, RMB30.0 million and an aggregate of RMB30.0 million raised by Daqing Dairy and RMB40.0 million raised by Changqing Dairy. Upon repayment of the loans raised by the Daqing Dairy Group, Daqing Dairy has obtained and drawn down a new loan of RMB30.0 million from a bank in June 2010 and another new loan of RMB30.0 million from a bank in May 2010, which are secured by guarantees provided by an independent party to the Group (the "Guarantor") as part of its business in return for fees. Each of these two new loans charges an interest rate of 0.4425% per month and has a repayment term of 36 months from June 2010 and May 2010, respectively. Upon repayment of the loan raised by Changqing Dairy, Changqing Dairy has obtained and drawn down a new loan of RMB40.0 million from a bank in May 2010, which is secured by a guarantee provided by the Guarantor. The new loan charges an interest rate of 0.4425% per month and has a repayment term of 36 months from May 2010. As a result of the above loan repayments and the drawdown of the new loans, the Daqing Dairy Group had RMB100.0 million of bank borrowings as at December 31, 2010. We believe that these loans will be repaid from the proceeds of additional loans we may incur or from our internally generated cash.

The Daqing Dairy Group raised three separate bank loans in 2008 from our principal bank in Daqing, amounting to RMB70.0 million in aggregate, all of which had been repaid in 2008 and 2009. The Daqing Dairy Group was also granted an interest free, unsecured advance of RMB30.0 million from a third party in December 2008, which was repaid in 2009.

For further information regarding the above borrowings, see "Related Party Transactions" and "Description of Material Indebtedness and Other Obligations."

The Group's borrowings

As at December 31, 2008, we had an advance outstanding from a third party of RMB30.0 million which we repaid in 2009. The Pre-IPO Investors granted the Company a three-month term loan for S$21.0 million (approximately RMB102.3 million) (the "First Pre-IPO Loan") that matured in February 2010. This was repaid in February 2010 by the Group through an assumption of debt agreement with Zhao Yu and Kenmoore. Subsequent to the repayment of the First Pre-IPO Loan, the Pre-IPO Investors extended a 18-month term loan to the Company amounting to S$15.75 million (approximately RMB76.51 million) on March 1, 2010. We have repaid this second loan from the Pre-IPO Investors with part of the proceeds from our IPO on November 1, 2010.

As at December 31, 2010, we had unutilized banking facilities of approximately RMB200.0 million.

Contingencies and Guarantees

During the years ended December 31, 2008, 2009 and 2010, we did not make any loan or provide any guarantee to milk collection centers, individual dairy farmers or dairy farms.

Except as described above, we did not have outstanding at the close of business on December 31, 2010 any loan capital (issued or agreed to be issued), bank overdrafts and liabilities under acceptances or other similar indebtedness, debentures, mortgages, charges or loans or acceptance credits or hire purchase commitments, finance lease commitments, guarantees, indemnities or other material contingent liabilities.

We are of the view that as of February 28, 2011, there has been no material change in our indebtedness and contingent liabilities since December 31, 2010.

Capital Expenditures

Our capital expenditures consist of purchases of property, plant and equipment, increases in construction in progress and additions to land use rights. For the years ended December 31, 2008, 2009 and 2010, our capital expenditures were RMB86.7 million, RMB128.2 million and RMB13.3 million, respectively.

Our capital expenditure of RMB13.3 million for the year ended December 31, 2010 was primarily due to acquisitions of plant and machinery and further additions to construction in progress of the new production line at our Changqing production facility amounting to RMB6.4 million in aggregate.

Our capital expenditures of RMB128.2 million for the year ended December 31, 2009 were primarily due to the purchase of additional machinery amounting to RMB66.1 million mainly for the phase two production line of our Daqing production facilities, the construction in progress of the factory building to house the new production line at our Changqing production facility amounting to RMB55.5 million and a trademark purchase of RMB0.2 million.

Our capital expenditures of RMB86.7 million for the year ended December 31, 2008 were primarily due to the construction in progress for our expanded warehouses, staff canteen, conference center and ancillary facilities as well as the upgrade of the boiler room.

With the proceeds from this offering, the Group intends to invest a portion of the net proceeds to implement the second stage of its vertical integration plan. The Group seeks to continuously manage its liquidity situation to ensure that it is adequate to meet its expansion plans. See "Business — Business Strategies — Evaluate integration opportunities to expand our business upstream into raw milk production" for further details.

Off-Balance Sheet Commitments And Arrangements

As at December 31, 2010, we had no off-balance sheet commitments and arrangements.

Market Risks

We are exposed to various types of market risks, including business risk, interest rate risk, foreign exchange risk, credit risk and liquidity risk.

Interest rate risk

Our fair value interest rate risk of the Group relates primarily to our fixed rate bank borrowings. These fixed-rate bank borrowings are primarily due within 36 months and the fair value interest rate risk is considered to be minimal. We currently do not have an interest rate hedging policy. However, the management monitors interest rate exposure and will consider hedging significant interest rate exposure should the need arise.

Our cash flow interest rate risk relates primarily to variable-rate bank balances. We believe that we are not exposed to significant interest rate risks attributable to variable-rate bank balances and thus, no sensitivity analysis to interest rate risk has been presented.

Foreign exchange rate risk

Our revenue and expenditures are denominated in Renminbi, which is currently not a freely convertible currency. Furthermore, most of our transactions are conducted in Renminbi, however, we undertake certain transactions denominated in Singapore dollars and US dollars and we will require foreign currencies for dividend payments (if any) to our shareholders. As a result, we are exposed to foreign currency fluctuations. Additionally, any appreciation of Renminbi may affect the value of, and any dividends payable on, our shares. We currently do not use any derivative contracts to hedge against its exposure to foreign currency risk. However, the Group manages its foreign currency risk by closely monitoring the movement of the foreign currency rate.

As at December 31, 2009, our Group had non-Renminbi denominated borrowings of S$21.0 million. On April 14, 2010, the Singapore dollar appreciated against the Renminbi from S$1.00 to RMB4.90 to S$1.00 to RMB4.96. If the Singapore dollar continues to appreciate against the Renminbi in the future, we may have to convert more Renminbi into Singapore dollars to repay the principal and interest amount of the above borrowings.

Fluctuations in exchange rates may adversely affect the value, translated or converted into Hong Kong dollars, of our net assets, earnings and any dividends we declare should such dividends be declared in Hong Kong dollars. The main operations of our business are carried on in China, and the amount of dividend our subsidiaries declare in our favour may be in fixed amount of Renminbi, therefore when there is exchange rates fluctuation, the amount of dividend may change as well.

The carrying amounts of the Group's foreign currency denominated monetary assets and monetary liabilities as at December 31, 2008, 2009 and 2010 were as follows:

	The Group					
	Liabilities			Assets		
	As at December 31,			As at December 31,		
	2008	2009	2010	2008	2009	2010
	RMB (in thousands)					
Singapore dollar [(1)] ..	65	204,640	—	13	523	550
US dollar [(2)]	—	—	—	8	1,441	2,483
Hong Kong dollar ...	—	—	—	—	—	9,897
Total	65	204,640	—	21	1,964	12,930

(1) At an exchange rate of S$1.00 to RMB4.87.

(2) At an exchange rate of US$1.00 to RMB6.83. This relates to the bank balances of the Company and Global Milk Singapore in US dollars.

For further information regarding our currency exchange risk and sensitivity analysis of such risk, see "Notes to the Financial Information — Financial Instruments" in our consolidated financial statements included elsewhere in this offering memorandum.

Inflation

We have not in the past been materially affected by inflation, but we can provide no assurance that we will not be affected by inflation in the future. See "Risk Factors — Inflation in China may have a material adverse effect on our business, financial condition and operating results" for further information.

Dividend Policy

Our shareholders are entitled to receive dividends declared by us. The payment and the amount of any dividends is at the discretion of our directors and will depend upon our future operations and earnings, capital requirements and surplus, general financial condition, contractual restrictions and other factors that our directors deem relevant. No dividend has been paid during the years ended December 31, 2008, 2009 and 2010 of the Group.

Cash dividends on our shares, if any, will be paid in Hong Kong dollars. Other distributions, if any, will be paid to our shareholders by any means which we consider legal, fair and practicable.

Recent Developments

In connection with the development of the dairy farm planned as part of the first stage of our vertical integration plan (see "Business — Business Strategies — Evaluate integration opportunities to expand our business upstream into raw milk production."), our new wholly owned subsidiary, Wuchang Benniu, entered into a lease agreement on March 22, 2011 with Wuchang Pingfangdian pursuant to which Wuchang Benniu has agreed to lease 500 mu (approximately 83 acres) of land in Wuchang for a term of 30 years for RMB30,000 per year (the "Land Lease"). The lease will expire on March 21, 2041 and is subject to customary termination provisions. We have the right to renew the lease after expiration for such further duration and upon such conditions as may be agreed with Wuchang Pingfangdian provided those terms are no less favorable than terms proposed by any other third party who offers to lease the land.

Pursuant to the new circular issued by the AQSIQ on November 1, 2010, we are required to re-apply for the National Industrial Production Permit according to the new requirements of inspecting infants formula power and dairy products' production conditions before March 1, 2011, otherwise the existing dairy product enterprises will be suspended from producing dairy products and infant formula powder. The AQSIQ in a press conference further announced that the deadline has been extended to the end of March, 2011. On March 25, 2011, our Daqing Dairy production facilities passed the re-examination test and received the requisite production permit re-issued by the Quality and Technical Supervision Bureau of Heilongjiang (黑龍江省質量技術監督局). On the same date, the Changqing production facility has also successfully passed an in-depth inspection and obtained the requisite production permit from the Quality and Technical Supervision Bureau of Heilongjiang.

Non-GAAP Financial Measures

We use certain non-GAAP data, such as EBITDA, to provide additional information about our operating performance as we believe that it is a useful measure for certain investors to assess our operating performance, operating cash flow and historical ability to meet debt service and capital expenditure requirement. EBITDA refers to our earnings before the following items:

- interest income/expense;
- amortization of intangible assets;
- non-operating income/expense;
- income tax expense; and
- depreciation.

EBITDA is not a standard measure under IFRS and should not be considered as an alternative to cash flows from operating activities, a measure of liquidity or an alternative to net income as indicators of our operating performance or any other measures of liquidity, profitability or cash flows derived in accordance with IFRS. Investors should also note that EBITDA as presented herein may be calculated differently from Consolidated EBITDA as defined and used in the Indenture governing the Notes. Interest expense excludes amounts capitalized.

As a measure of our operating performance, we believe that the most directly comparable IFRS measure to EBITDA is profit for the year. We operate in a capital intensive industry. We use EBITDA in addition to profit for the year because profit for the year includes many accounting items associated with capital expenditures, such as depreciation and amortization. These accounting items may vary between companies depending on the method of accounting adopted by a company. Funds depicted by this measure may not be available for debt service due to covenant restrictions, capital expenditure requirements and other commitments.

The following table reconciles our operating profit under IFRS to our definition of EBITDA for the periods indicated:

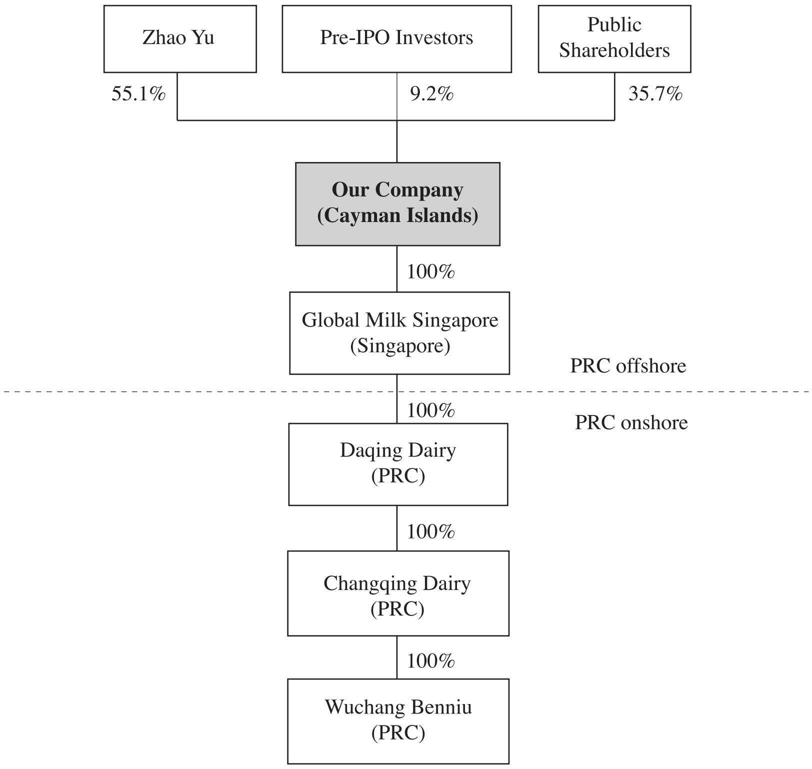
	The Daqing Dairy Group		The Group		
	Year ended December 31,				
	2008	2009	2008	2009	2010
	RMB (in thousands)				
Profit and total comprehensive income for the year	113,101	143,150	54,135	133,469	260,588
Adjustments:	78,492	76,116	26,181	85,731	150,612
Interest income	(2,007)	(8,490)	(1,771)	(8,494)	(971)
Finance costs	1,833	9,025	1,423	9,258	14,672
Other gains and losses excluding interest income	18,936	2,889	(5,268)	1,697	1,939
Income tax expenses	48,736	56,849	23,866	61,900	106,010
Depreciation[(1)]	10,859	15,688	7,033	19,195	26,338
Amortization of intangible assets	—	20	625	1,520	1,520
Release of prepared lease payment	135	135	273	655	1,104
EBITDA	191,593	219,266	80,316	219,200	411,200

(1) Depreciation represents depreciation expense in cost of goods sold, selling and marketing costs and administrative expenses.

You should not consider our definition of EBITDA in isolation or construe it as an alternative to profit for the periods indicated or as an indicator of operating performance or any other standard measure under IFRS. Our EBITDA measures may not be comparable to similarly titled measures used by other companies.

Our Current Group Structure

The following chart shows our group structure as of the date of this offering memorandum:



History And Development

History and development of Daqing Dairy, our principal operating subsidiary

Daqing City Animal Husbandry Trade Joint Company's dairy factory* (大慶市牧工商聯合公司乳品廠) ("Daqing Joint Company Dairy Factory"), the predecessor of Daqing Dairy, was established by Daqing City Animal Husbandry Trade Joint Company* (大慶市牧工商聯合公司) on December 1, 1970 as its factory unit. On April 23, 1981, the factory unit became a PRC State-owned enterprise under the name Daqing Joint Company Dairy Factory. Its initial scope of business was the production and sale of milk powder (as its principal product) and malted milk products, ice creams and popsicles (as its ancillary products). On October 26, 1984, Daqing Joint Company Dairy Factory was renamed as "Daqing Dairy Factory."

In October 1997, Daqing Dairy Factory's first capital restructuring was approved. The first capital restructuring was undertaken as one of the first steps to transfer the State-owned interest in Daqing Dairy Factory to non State-owned persons and to denationalize Daqing Dairy Factory.

In connection with the first capital restructuring, Daqing Dairy Factory changed its name to 大慶乳品有限責任公司 (Daqing Dairy Products Co., Ltd*) ("Daqing Dairy Products"), the registered capital of Daqing Dairy Products was increased, and 74.65% of its equity interest was beneficially State-owned and the remaining 25.35% was beneficially owned by the then 664 employees, including three individual shareholders who represented the 664 employees (the "employee shareholder representatives").

In 1998, Daqing Dairy Products, Daqing Dairy Products was denationalized when the State-owned 74.65% interest was transferred to the then 543 employees (represented by the three employee shareholder representatives) of Daqing Dairy Products of Daqing Dairy Products.

The local government approached Zhao Chuan Wen, who is currently our chairman and executive director, in May 2006 to help put together a plan to reorganize the management of Daqing Dairy and elevate it out of its then financial situation.

In June 2006, through the liaison of and discussion with the local government, Daqing Dairy's directors appointed Zhao Chuan Wen as an honorary director to assist in revitalizing Daqing Dairy.

Having considered a number of options on June 30, 2006, the representatives of the employee-shareholders decided to dispose of the entire interest in Daqing Dairy and Daqing Dairy's board, with the assistance of Zhao Chuan Wen, began to look for suitable investors. As a transition arrangement to safeguard the interest of the employee-shareholders and to facilitate a smooth disposal by and payment of transfer consideration to the employee-shareholders, Zhao Chuan Wen agreed to pay the consideration to the employee-shareholders for the proposed disposal once a reasonable price has been agreed. In July 2006, all 543 employee-shareholders (other than four employee-shareholders) signed a transferring shareholders' name list signifying their willingness to dispose their entire interest for an aggregate consideration of approximately RMB3.38 million.

On April 6, 2007, to facilitate a transaction with the proposed investor, Cao Xue Jian, who only wanted to deal with a single responsible person for the transfer of the entire equity interest in Daqing Dairy instead of the Daqing Labor Union Committee and the three individual shareholders who held the entire equity interest in Daqing Dairy on behalf of 543 employee-shareholders at that time, Daqing Dairy's shareholders approved the transfer of its entire registered capital to Zhao Chuan Wen.

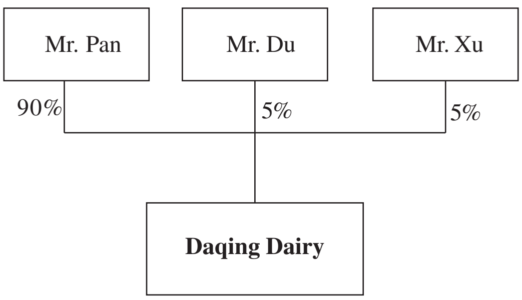
Zhao Chuan Wen (in his capacity as the sole shareholder of Daqing Dairy) passed the sole shareholder's resolutions on April 6, 2007 to approve (i) the transfer of the entire registered capital in Daqing Dairy from Zhao Chuan Wen to Cao Xue Jian, and (ii) the admission of seven individuals as new shareholders of Daqing Dairy. Zhao Chuan Wen transferred the legal and beneficial interests in the entire registered capital in Daqing Dairy from for the same consideration at which he had acquired those interests from the 543 employee-shareholders.

Also on the same day, April 6, 2007, in order to inject the capital and equipment required, the seven new shareholders resolved to increase the registered capital of Daqing Dairy from RMB17.31 million to RMB120 million, and injected cash, land use rights, equipment and machinery valued at RMB102.69 million into Daqing Dairy.

On November 30, 2007, the seven new shareholders approved the transfer from four of them of an aggregate of 80% of the registered capital of Daqing Dairy to Pan Xiao Feng. As a result, Daqing Dairy was owned 90% by Pan Xiao Feng, 5% by Du Wei, and 5% by Xu Zhong Jie.

Reorganization

The reorganization of the Group, which was effected in preparation for the IPO and pursuant to which our Company became the holding company of our Group, included the following major steps set forth below.



Incorporation of Global Milk Singapore

Global Milk Singapore was an investment vehicle incorporated in Singapore on September 15, 2006 as a private company limited by shares and it allotted and issued one ordinary share of S$1.00 to Abdul Jabbar Bin Karam Din as the first subscriber upon incorporation. On October 8, 2007, Abdul Jabbar Bin Karam Din transferred the single share in the issued capital of Global Milk Singapore to Zhao Yu.

Acquisition of the entire equity interest in Daqing Dairy by Global Milk Singapore

On December 26, 2007, the shareholders of Daqing Dairy, approved (i) the acquisition of the entire equity interest in Daqing Dairy by Global Milk Singapore; (ii) broaden Daqing Dairy's scope of business to "production, sale, import and export of "Da Qing" brand glucose metabolism-improving milk powder (A), milk and dairy products and frozen drinks and (iii) the conversion of Daqing Dairy from a domestic privately-owned enterprise to a wholly-foreign owned enterprise ("WFOE") upon completion of the acquisition. On the same day, the shareholders entered into an equity transfer agreement with Global Milk Singapore to transfer the entire equity interest in Daqing Dairy.

On July 16, 2008, the local MOFCOM approving the proposed acquisition of Daqing Dairy by Global Milk Singapore and the aggregate consideration for the acquisition of Daqing Dairy by Global Milk Singapore was approximately RMB318.78 million.

Daqing Dairy obtained the "Certificate of Approval for Establishment of Enterprises with Foreign Investment in the PRC (Shang Wai Zi Hei Zhao Wai Zi Han Zi [2008] No.104)"《中華人民共和國外商投資企業批准證書》商外資黑招外資函字 [2008]104號 issued by the Heilongjiang Provincial People's Government on July 25, 2008, which is the effective date of the acquisition of Daqing Dairy by Global Milk Singapore.

Incorporation of our Company

Our Company was incorporated in the Cayman Islands on October 15, 2009 as the holding company of our Group with an authorised share capital of HK$380,000 divided into 38,000,000 ordinary shares of HK$0.01 each. One ordinary share of HK$0.01 of the Company was allotted and issued fully paid to Codan Trust Company (Cayman) Limited on incorporation. On the same day, Zhao Yu acquired the single issued share in the capital of the Company and was appointed as the sole director of the Company.

Acquisition of Global Milk Singapore by the Company

On October 15, 2009, our Company and Zhao Yu entered into a sale and purchase agreement, pursuant to which we acquired from Zhao Yu the single ordinary share outstanding of Global Milk Singapore for a consideration of S$1.00, in exchange for which we issued 550 ordinary shares of HK$0.01 each in the capital of our Company to Mr. Zhao, credited as fully paid.

Establishment of Changqing Dairy and its acquisition by Daqing Dairy

Changqing Dairy was established in the PRC on August 7, 2008 as a sole shareholder limited liability company by Pan Xiao Feng, on the understanding with Zhao Yu that after we acquired Daqing Dairy, we will procure that Daqing Dairy to acquire Changqing Dairy from Mr. Pan in order to expand the production capacity of our Group. In this connection and for the purposes of funding the construction of the Changqing production facility, Daqing Dairy granted a loan facility of RMB250 million to Changqing Dairy on August 30, 2008. See "Related Party Transactions" for further details regarding this loan. Pursuant to an equity transfer agreement dated November 16, 2009, Mr. Pan transferred the entire registered capital in Changqing Dairy to Daqing Dairy and the consideration in respect of the acquisition of Changqing Dairy by Daqing Dairy was RMB10 million.

Investment in the Company prior to the IPO

Since our Company's incorporation until immediately prior to our IPO in October 2010, the Pre-IPO Investors and Zhao Yu have made various investments in our Company in the following manner:

- On November 1, 2009, Mr. Zhao transferred 10.3% of the entire issued share capital in our Company to Kenmoore for a consideration of approximately US$6.01 million pursuant to a share transfer agreement made between them. This investment was completed on November 18, 2009 and Kenmoore was registered as a shareholder in respect of 57 ordinary shares of HK$0.01each in the capital of our Company.

- On November 20, 2009, our Company entered into an investment agreement with the Pre-IPO Investors, Zhao Yu and Zhao Chuan Wen pursuant to which the Pre-IPO Investors extended to our Company a bridge loan of S$21 million (the "Bridge Loan") and invested a further sum of S$21 million to subscribe for 127,829 shares. We repaid the Bridge Loan amount (together with the applicable processing fees) on its maturity date, February 28, 2010, and we issued 127,829 shares to the Pre-IPO Investors on February 4, 2010.

- On November 20, 2009, Zhao Yu entered into a subscription agreement with our Company pursuant to which he subscribed for 63,171 shares for a consideration of RMB125.0 million, the full amount of which was paid by February 28, 2010. We issued 63,171 shares to Mr. Zhao on February 2010.

- On January 28, 2010, our Company entered into a second series funding agreement with the Pre-IPO Investors, Zhao Yu and Zhao Chuan Wen pursuant to which the Pre-IPO Investors extended to our Company a second loan of S$15.75 million (the "Second Loan") and invested a further sum of S$5.25 million to subscribe for 15,879 Shares. We issued 15,879 shares to the Pre-IPO Investors on March 24, 2010. After the consummation of our IPO in October 2010, we repaid the Second Loan amount (together with the applicable processing fees and accrued interests) to the Pre-IPO Investors.

Issuance of shares in the IPO

On October 28, 2010, our Company issued and sold to the public 252,620,000 new shares at a public offering price of HK$4.39 per share in our IPO on the Main Board of the Stock Exchange of Hong Kong.

Establishment of Wuchang Benniu to develop and operate our dairy farm

With the consummation of our IPO and in connection with a two-stage strategy to realize our vertical integration plan, our board of directors approved the investment in and construction of our own dairy farm by Changqing Dairy, in Erhe Township, approximately 30 km north-east of Wuchang, Heilongjiang, on November 18, 2010. We established Wuchang Benniu as its wholly owned subsidiary on November 25, 2010 to develop and operate our dairy farm which we currently plan to complete in 2012.

Overview

We are a top ten domestic milk powder company in the PRC. According to the Euromonitor Report, we ranked ninth among domestic brand owners and 15th among both foreign and domestic brand owners with a 1.5% market share in the milk powder market in China in terms of sales value in 2009. For the year ended December 31, 2008, the Daqing Dairy Group generated revenues of RMB433.3 million and for the years ended December 31, 2009 and 2010, we generated revenues of RMB510.0 million and RMB921.9 million, respectively.

We are principally engaged in the production, marketing, and sale of medium-to-high and premium priced milk formula products in China. Our dairy products are classified into the following two main categories: milk formula products and whole milk powder products.

We produce a full range of milk formula products and whole milk powder products for infants, children and adults. We believe our infant and pediatric milk formula products supply the balanced nutrition that infants and children need throughout various stages of childhood growth and development. In addition, we produce milk formula products fortified with various vitamins and essential minerals that provide supplements to meet special nutritional requirements for older children, adults, the elderly, and pregnant and lactating women. We believe that our broad range of products targets consumers of different income groups with different product value propositions.

Our main product category, milk formula products, consists of the Shi Jia 仕加 brand , the Emilon 愛美樂 brand and the Daqing 大慶 brand. Our Shi Jia brand consists of premium priced milk formula products that are intended to be suitable for infants and children at different growth stages as well as post-natal women. We market our Shi Jia brand to consumers with high disposable incomes in second-tier cities, particularly eastern coastal cities and certain third-tier cities in the PRC. Our Emilon brand consists of medium-to-high priced milk formula products catering to the changing nutritional needs of growing infants and children. We market our Emilon brand to consumers in second- and third-tier cities in China. We introduced our You Zhi Series under our Emilon brand in May 2010. The You Zhi Series is currently the most competitively priced product in the Emilon brand, which allows us to compete with smaller regional competitors more effectively, especially in third-tier and below cities. The Daqing brand has two distinct products: Daqing Milk Formula Series and whole milk powder products. Our Daqing Milk Formula Series is targeted at consumers of low-to-medium priced milk formula products, and is intended to be suitable for children, adults and the elderly. We market our Daqing Milk Formula Series to consumers in villages and counties near second- and third-tier cities, particularly in northeastern China. Our whole milk powder products are sold for general consumption, with our 25 kilogram whole milk powder sold to other dairy producers as well as food and beverages manufacturers. In addition, we produce a variety of ice cream products under our Qingru 慶乳 brand.

We have adopted a strict quality control system over our production processes, from sourcing of raw milk to production, and have adopted stringent quality standards designed to comply with applicable PRC government standards. This is evidenced by the various awards and certifications we have received, including the GMP certification we obtained for the phase one and phase two production lines at our Daqing production facilities in 2007 and 2010, respectively, and the HACCP Management System Certification (危害分析與關鍵控制點體系認證) for Daqing Dairy in December 2010. See "Business — Sales and Marketing — Branding and Product Positioning." In 2010, we obtained ISO9001:2008 certification for the design, production and sale of infant milk formula, dairy products (milk powder and liquid milk) and cold beverages. We test each batch of raw material supplied to us before use in production. We conduct periodical inspections of our finished products to ensure compliance with applicable PRC quality standards.

We primarily sell our milk formula products and whole milk powder products through an extensive network of over 140 distributors in China. Our distributors sell our milk formula products and whole milk powder products directly to retail outlets, such as children's and parenting specialty stores, smaller supermarkets and mom and pop shops in 21 provinces and Chongqing. We have entered into non-exclusive agreements with all of our current distributors, which are generally for a term of one year. We typically require our distributors to pay the full purchase price before we deliver our products to them. Our distributors are only permitted to sell our milk formula products and whole milk powder products in their designated distribution areas. If any of our distributors is in breach of the above term of the distribution agreements, we have the right to terminate the relevant distribution agreement.

In addition to our distribution network, we sell our products directly to department stores, shopping malls and supermarket chains in Daqing and the surrounding areas and other customers who purchase from us on an ad hoc basis. We also sell our whole milk powder (packaged in 25 kilogram bags) directly to our customers such as food processing enterprises. We intend to continue selling our milk formula products and whole milk powder products in Heilongjiang through our distributors and by way of direct sale, and in areas outside Heilongjiang through our distributors. For the years ended December 31, 2008, 2009 and 2010, approximately 71.7%, 69.1% and 85.5% of our sales, respectively, were made to our distributors. For the years ended December 31, 2008 and 2009, approximately 74.7% and 69.1% of the sales of the Daqing Dairy Group, respectively, were made to our distributors. We sell our ice cream products directly to retail outlets in Daqing and the surrounding areas.

The table below sets forth our revenue by product segment for the periods indicated:

	The Daqing Dairy Group [(1)]				The Group [(1)]					
	Year ended December 31,									
	2008		2009		2008		2009		2010	
	Revenue		Revenue		Revenue		Revenue		Revenue	
	RMB (thousands)	% of total	RMB (thousands)	% of total	RMB (thousands)	% of total	RMB (thousands)	% of total	RMB (thousands)	% of total
Milk formula products	366,482	84.6	431,605	84.6	159,224	80.7	431,605	84.6	851,845	92.4
Shi Jia brand	—	—	—	—	—	—	—	—	43,395	4.7
Emilon brand	277,234	64.0	308,669	60.5	119,030	60.3	308,669	60.5	647,028	70.2
Daqing brand	89,248	20.6	122,936	24.1	40,194	20.4	122,936	24.1	161,422	17.5
Others	—	—	—	—	—	—	—	—	—	—
Whole milk powder products	65,034	15.0	61,671	12.1	36,345	18.4	61,671	12.1	48,320	5.2
Others [(2)]	1,800	0.4	16,759	3.3	1,800	0.9	16,759	3.3	21,721	2.4
Total	433,316	100.0	510,035	100.0	197,369	100.0	510,035	100.0	921,886	100.0

(1) Global Milk Singapore acquired the entire equity interest in Daqing Dairy on July 25, 2008 pursuant to an equity transfer agreement dated December 26, 2007 entered into between Mr. Pan, Mr. Xu, Mr. Du and Global Milk Singapore. The operating results of the Daqing Dairy Group before the completion of the acquisition and of our Group after the completion of the acquisition are not directly comparable as they are two separate entities from an accounting perspective. The table above contains financial information from the consolidated financial statements of our Group and the consolidated financial statements of the Daqing Dairy Group.

(2) Revenue from the sale of other products in 2008, 2009 and 2010 represents the sale of our ice cream products. We produce a variety of ice cream products under our own Qingru brand. Our ice cream products are sold in different forms, such as ice cream cups, ice cream bars, ice cream cones and tubs of packaged ice cream, ranging from 75 gram to 4 kilogram per pack. The shelf life of our ice cream products is normally 18 months. We sell our ice cream products directly to retail outlets in Daqing and the surrounding areas. We collect sales payments in cash when the ice cream products are delivered.

Since the establishment of our production facility in Daqing in 1970, we have received various awards and certifications which have helped increase the brand recognition of our products. See “Business — Sales and Marketing — Branding and Product Positioning” for a description of some of our key awards and certifications.

We are located in Daqing in the west of Heilongjiang in the PRC. Daqing is in the central part of the Songnen Plain (松嫩平原) in Heilongjiang. Heilongjiang is located along the world's dairy belt region with a latitude of approximately 43 to 53 degrees, along with the Netherlands, Denmark and Hokkaido in Japan, a region known for geographic conditions suitable for dairy farming due to vast grasslands and a cool climate.

We source raw milk, the primary raw material for the production of our products, from selected milk collection centers which, in turn, collect raw milk from dairy farms and individual dairy farmers in proximity to Daqing.

We have appointed Wang Li Ying (王麗穎) as the manager of our quality control and product development department with responsibility for our overall quality control. Ms. Wang, is a graduate of 東北農業大學 (Northeast Agricultural University) with a Bachelor of Science degree in Food Science and Engineering. Before joining us in 2008, she had over six years of experience in the food industry.

Our quality control team closely monitors the implementation of our quality control system, which involves the following quality control measures:

- To ensure the raw materials we purchase do not contain contaminants which are harmful to human health, we test the content and quality of all raw milk delivered to us, including the level of protein, fat, antibiotics and impurities, and acidity to ensure compliance with the National Quality Standard for Raw Milk. We also test for the presence of melamine in the raw milk we use to ensure compliance with the applicable quality standards in the PRC. We also carry out sampling tests on other raw materials we purchase for use in our production process, such as sucrose, whey powder, vegetable oil, mineral supplements, lactose, maltose, whey protein concentrate and various flavorings, for bacteria content and physical and chemical properties before we accept and store them for use at a later stage in our production process of these raw materials. In addition, we check the raw materials and their product expiry dates before we use them in our production.

- we test our semi-finished products for the water content and the level of fat and impurities in accordance with our internal quality standards.

- We also carry out tests on the content and quality of our finished products, which include the level of protein, fat, sucrose, impurities, bacteria and antibiotics, to ensure compliance with the applicable quality standards in the PRC.

We provide our quality control staff members with compliance training to ensure proper implementation of our quality control procedures.

In October 2010, we completed our IPO and our shares became listed on the Hong Kong Stock Exchange.

Competitive Strengths

We believe that our historical success and future prospects are underpinned by a combination of competitive strengths including:

Access and proximity to strategic production location, quality raw milk sources and ideal dairy farming climate

A constant supply of high quality raw milk is critical to our business and demands. We believe that our location in Heilongjiang strengthens our ability to meet the growing raw material needs of our products.

We are located in Daqing in western Heilongjiang in the PRC. Daqing is in the central part of the Songnen Plain (松嫩平原) in Heilongjiang. Heilongjiang is located in the world's dairy belt at a latitude of approximately 43 to 53 degrees, along with the Netherlands, Denmark and Hokkaido, Japan, a region known for geographic conditions suitable for dairy farming due to vast grasslands and a cool climate. These favorable conditions facilitate the production of quality milk in dairy cows and provide unique advantages and potential to the development of the dairy industry. According to the China Dairy Statistical Report, (i) the raw milk output of Heilongjiang ranked second in China in 2009 in terms of volume; and (ii) Daqing ranked fifth among prefectural-level cities in China in raw milk output and produced approximately 1.3 million metric tons of raw milk in 2009, which represented approximately 25% of the total raw milk output in Heilongjiang in 2009 in terms of volume.

We source raw milk from selected milk collection centers which collect raw milk from dairy farms and individual dairy farmers near Daqing. As dairy farms and individual dairy farmers do not have all necessary milking facilities, most dairy cows are milked at milk collection centers which are equipped with the milking facilities. As such, it is the general industry practice that dairy product manufacturers source raw milk directly from milk collection centers which collect fresh milk from dairy cows rather than dairy farms and individual dairy farmers.

We have non-exclusive raw milk supply agreements with over 15 milk collection centers in Daqing, which we believe provide us with a sufficient and stable supply of high quality raw milk. We test the content and quality of all raw milk shipments delivered to us, including the levels of protein, fat, antibiotics and impurities, and acidity and reject shipments if they do not comply with the National Quality Standards for Raw Milk (中華人民共和國國家標準生鮮牛乳收購標準), We believe that our strategic location in Daqing enables us to obtain a sufficient and stable supply of high quality raw milk to meet our growing needs and increase our production output.

The Dairy Product Industrial Policies (2009 Version) 《乳製品工業產業政策(2009年修訂)》 released by the Ministry of Industry and Information Technology of the PRC (中華人民共和國工業和信息化部) and the NDRC on June 26, 2009, impose admission conditions on investments in dairy products in Heilongjiang including: (i) the distance between newly built dairy processing facilities and any existing dairy processing facilities must be at least 100 km; and (ii) all newly built dairy processing facilities must have a daily raw milk processing capability of over 300 metric tons. We believe that these admission restrictions limit the entry of new competitors to the dairy industry in Daqing and Wuchang where our production facilities are located, and increase our competitiveness in these areas.

Wide range of milk formula products and whole milk powder products, and effective product positioning capabilities

Our product offerings include a wide range of products designed to meet diverse consumer preferences and needs and different products have different selling prices and costs of sales. We believe that our ability to modify our product offerings effectively in a timely manner enables us to position our products advantageously within the competitive market as it evolves.

We produce a wide range of milk formula products and whole milk powder products which enable us to maintain a broad consumer base. Our milk formula products include the Shi Jia brand, which is intended to supply the nutritional needs of an infant or a child in the first few months and throughout the various stages of childhood growth and development, and provide nutritional supplements for post-natal women, and the Emilon brand, which is intended to supply the nutritional needs of an infant or a child in the first few months and throughout the various stages of childhood growth and development, as well as provide nutritional supplements for pregnant and lactating women. In addition, our Daqing Milk Formula Series of products come in varying combinations of vitamins, essential minerals and other supplements designed to meet the specific nutritional requirements of children, adults and the elderly. We also produce whole milk powder products for personal consumption and industrial use, such as a raw material in dairy and other food products. For more information on our range of products, see "Business — Products."

We believe that: (i) our broad range of products enables us to better target consumers across different income groups with different product value propositions, thereby satisfying their particular needs; and (ii) our ability to improve and expand our product offerings has been a key factor contributing to the rapid growth in our revenue and will continue to play an important role in the future.

Stringent quality control standards and high quality products

We have adopted stringent quality control standards designed to comply with applicable PRC government regulations. We test raw milk supplied to us on-site for its content before use in our production. We conduct periodical inspection on our finished products to ensure compliance with the applicable quality standards in the PRC.

We have adopted a strict quality control system over our production, from sourcing of raw milk to production. In 2010, we obtained ISO9001:2008 certification for the design, production and sale of infant milk formula, dairy products (milk powder and liquid milk) and cold beverages. This certification demonstrates that we have an effective quality management system that shows our commitment to quality and our ability to consistently provide products that meet customers' requirements. In addition, we obtained GMP certification for the phase one and phase two production lines at our Daqing production facilities in 2007 and 2010, respectively, and the HACCP Management System Certification (危害分析與關鍵控制點體系認證) for Daqing Dairy in December 2010. We have obtained various awards and certifications in respect of our products. For further details, see "Business — Sales and Marketing — Branding and Product Positioning."

Within each of our production facilities, we have adopted stringent quality control systems to monitor our product quality at various inspection points, including testing the initial intake of raw milk and other raw materials, testing semi-finished products and finished products and enforcing sanitation and hygiene standards for staff and equipment. For further details, see "Business — Quality Control."

We believe that our various awards and certifications for quality products and our melamine-free test results attest to our strict adherence to being "'green', healthy and safe", which we have adopted as the principal themes of our product image.

Strong brand recognition and extensive distribution network

We believe that our longstanding history in the milk powder market in the PRC has contributed to our positive brand recognition and reputation, which has enabled us to be sensitive to changing consumer preferences and needs and to introduce new products which gain market acceptance. This has been instrumental to the success and growth of our business. We also believe that our commitment to providing quality products has generated brand loyalty among a segment of the consumer population, which further enhances the prospective success and growth of our business. In addition to our strong brand recognition, we have also established an extensive distribution network in various parts of China to increase the circulation of our products. We primarily sell our milk formula products and whole milk powder products through an extensive network of over 140 distributors in China as at December 31, 2010. Our distributors sell our milk formula products and whole milk powder products directly to retail outlets, such as children's and parenting specialty stores, smaller supermarkets and mom and pop shops in 21 provinces and Chongqing. We have non-exclusive distribution agreements with all of our current distributors. These agreements are generally for a term of one year. Under these agreements, our distributors may distribute other brands of dairy products. We believe that this enables us to select distributors with extensive experience in the distribution of international and domestic brand milk formula products and that such experience and credentials, in turn, facilitate the promotion of our milk formula products and whole milk powder products and provide broad coverage of our distribution network.

Experienced senior management team

Our senior management has strong and extensive experience in the PRC dairy industry, and is dedicated to the product development, production and marketing of dairy products and the development and operation of our dairy farm.

Product development

Xia Yuan Jun, our executive director and deputy chief executive officer, is primarily responsible for overseeing product development as well as assisting Zhao Yu, our chief executive officer, in executing the overall business strategies, facilitating business development, and managing the operations of our Group. He has over 20 years of experience in the dairy industry. Before joining our Group, Mr. Xia held managerial positions in 黑龍江省完達山乳業股份有限公司 (Heilongjiang Wondersun Dairy Co., Ltd*) and 西安銀橋生物科技有限公司 (Xi'an Yinqiao Biological Science and Technology Co. Ltd*), both of which are PRC dairy companies. Mr. Xia was nominated as one of the "Ten Outstanding Technology Persons" in the Chinese dairy processing industry (首屆中國乳品加工業"十大傑出科技人物") on August 7, 2004.

Production

Zhang Bing is the assistant general manager (production) of Daqing Dairy's production department primarily responsible for managing the Daqing production facilities. He joined us in March 2009 as the deputy assistant general manager of Daqing Dairy's production department before his promotion to his current position in September 2009. He pursued his studies at 佳木斯市聯合職工大學 (Jiamusi Employee University*) in disciplines relating to Food Engineering between September 1990 and July 1993. He has over eight years of experience in the dairy industry.

Operations and business development

Fu Chong is our executive director and chief operations officer. He is primarily responsible for the overall operations, strategic and business development of our Group. Prior to joining our Group, he held various managerial positions including general manager of development department, general manager of information center, chief information officer and member of the group's strategies management committee with 內蒙古伊利實業集團股份有限公司 (Inner Mongolia Yili Industrial Group Co., Ltd.), a dairy company in the PRC, from July 1995 to July 2005.

Development and operation of our dairy farm

We appointed Gao Feng (高峰) in March 2010 as an executive officer of our Group primarily responsible for developing our dairy farm business. He was also appointed as the supervisor of Wuchang Benniu on November 19, 2010. Mr. Gao has more than 20 years of experience in the dairy, cattle husbandry and veterinarian industries. He studied at 黑龍江八一農墾大學 (Heilongjiang Bayi Agricultural University) in disciplines relating to veterinary. He also completed an Advanced Livestock Management training at the same university in December 1994. Prior to joining our Group, Mr. Gao held various positions with numerous dairy and cattle husbandry companies including 黑龍江省八五一一農場 (Heilongjiang 8511 Farm*), 黑龍江省和平牧場 (Heilongjiang Heping Farm*), 黑龍江省和平乳品廠 (Heilongjiang Heping Dairy Factory*), 黑龍江省八五八農場 (Heilongjiang 858 Farm*) and 黑龍江農墾完達山牧業有限公司 (Heilongjiang Agricultural Wondersun Livestock Co., Ltd.*).

Business Strategies

Our business objective is to become a leading vertically integrated producer of dairy products in China with a broad range of product offerings and a strong focus on medium-to-premium priced milk formula products. To achieve this objective, we have formulated the following business objectives:

Expand our product offerings

The PRC dairy industry is still developing and we expect demand for dairy products to grow. Our current product offerings comprise various milk formula products and whole milk powder products, each designed to address specific customer preferences and needs. We intend to continue improving and expanding our product offerings by launching new products with an emphasis on new pediatric milk formula products, which are suitable for infants and children at different growth stages. We have recently developed and launched a new series of milk formula products, which are marketed to consumers of premium priced milk formula products, namely three new milk formula products for infants at different growth stages under our Shi Jia Jia You Bao Bao Series 仕加嘉友寶寶系列 and two new milk formula products for post-natal women under our Shi Jia S'Plan Series 仕加斯普恩系列.

We believe that the expansion of our product portfolio will build on the success of our existing product offerings by targeting consumers' new or changing needs and broadening our target consumer base. In addition, we expect that our new pediatric milk formula products targeting customers of premium priced milk formula products will yield a higher profit margin compared to our other existing products.

Enhance our brand recognition nationwide

We believe that our longstanding history and commitment to providing quality products have contributed to increased brand recognition, loyalty and reputation, which have been instrumental to the success and growth of our business. In recent years, our strong brand recognition has helped to make us one of the leading producers of milk formula products and whole milk powder products in northeastern China.

To tap into the successful product positioning of our Emilon brand 愛美樂配方奶粉系列 and to leverage the success of our regional brand recognition, we intend to enhance our brand recognition nationwide by conducting direct advertising campaigns on nationwide and local television channels, newspapers, magazines, internets and other media as well as participating in product promotional activities. We also plan to increase the frequency and reach of our promotional activities and seminars.

Reinforce and expand our distribution network in the PRC

We intend to explore opportunities in areas of the PRC where there will be demand for our products, which are not currently covered by our distribution network. We plan to appoint more distributors throughout the PRC and to increase our product coverage through our distributors by expanding sales through different retail sales channels, with a particular focus on children's and parenting specialty stores. To support our plan to expand our distribution network in China, we also intend to increase our sales and marketing staff who serve as a point of contact between us and our distributors. We believe this expansion will enable us to further penetrate the PRC milk formula market.

Furthermore, while we managed to expand our distribution network from 67 distributors as at December 31, 2009 to 143 distributors as at December 31, 2010, such expansion was mainly implemented through our continued appointment of new distributors. With the recent launch of our products under the Shi Jia brand, we intend to market these products in the second- and third-tier cities in the PRC, particularly the eastern coastal cities and explore the sale of these products in the first-tier cities through new distribution network activities which are expected to involve increased marketing expense. We intend to undertake the following new distribution network expansion activities to implement the above strategy:

- establish new distribution channels to distribute our products under our Shi Jia S'Plan Series through health supplement chain stores;
- establish new distribution channels through children's and parenting speciality stores, maternity stores and other women related channels to distribute our products under the Shi Jia Jia You Bao Bao Series in first-, second- and third-tier cities, particularly eastern coastal cities of the PRC, based on joint promotion activities with owners of these channels such as membership programmes which enable consumers of our products to enjoy various benefits for purchasing our products at these distribution channels;
- increase our presence in each sales region by establishing logistics distribution centers and after sales service centers to conduct product training courses for our distributors;

- conduct joint promotion activities on print and traditional media, road shows and other activities to support our distributors in new sales regions in order to expansion the reach of our distribution channels; and
- attend trade shows to secure more distributors.

Evaluate integration opportunities to expand our business upstream into raw milk production

We believe that in the wake of several food safety incidents which resulted in greater public focus on quality, tightening government regulation and introduction of government policies encouraging consolidation in the dairy industry, the milk formula and milk powder industry will experience consolidation. This consolidation may benefit us but may also create more formidable competitors. To position ourselves better in this evolving competitive environment, we intend to evaluate integration opportunities to expand our business upstream in raw milk production, including constructing and acquiring dairy farms.

- *The first stage of our vertical integration plan*

The first stage of our vertical integration plan involves the construction of a dairy farm. We currently expect that we will require approximately RMB350.0 million to fund this project which will include: i) the acquisition of the right to use the requisite parcel of land upon which we will construct our dairy farm, an office building and other ancillary facilities (in connection with which Wuchang Benniu has entered into a land lease agreement with Wuchang Pingfangdian Tree Farm on March 22, 2011 and which will involve payment of further license and permit fees for leasing, occupying and using such land to develop our dairy farm); (ii) the construction of our dairy farm, an office building and other ancillary facilities (including a bio-organic fertilizer and bio-gas power generation facility); (iii) the purchase of dairy cows; and (iv) related working capital for the operation of the farm. We intend to use approximately HK$350.9 million (RMB295.2 million) of the net proceeds from the IPO to fund this project and we will satisfy the remaining capital expenditure requirements with internally generated cash flows.

On November 25, 2010, we established a new wholly owned subsidiary, Wuchang Benniu to develop and operate our first stage dairy farm which is designed to raise dairy cows. For this purpose, Wuchang Benniu entered into a lease agreement on March 22, 2011 with Wuchang Pingfangdian Tree Farm, pursuant to which Wuchang Benniu has agreed to lease 500 mu (approximately 83 acres) of land in Wuchang for a term of 30 years for RMB30,000 per year.

We expect that our first stage dairy farm will be completed in 2012 and will have a capacity of up to 10,000 dairy cows.

- *The second stage of our vertical integration plan*

Having reviewed and evaluated the progress of the first stage of our vertical integration plan, we intend to proceed with the second stage. We intend to use proceeds from this offering to finance a portion of the second stage which we currently anticipate will include: (i) the development of approximately 25 smaller scale dairy farms in Wuchang and Zhaoyuan with a capacity of up to 700 dairy cows per farm and ancillary facilities such as milking stations and a transportation fleet; (ii) the acquisition or construction of a feed processing plant to support our vertical integration plan; and (iii) the acquisition or construction of additional raw milk processing capacity to complement our existing production facilities and support the expansion of our milk formula business.

We expect to finance the development of approximately 25 smaller scale dairy farms in Wuchang and Zhaoyuan and ancillary facilities such as milking stations and a transportation fleet with the net proceeds from this offering. We expect that each of these farms will house approximately 500 mature milkable dairy cows. We expect to commence construction of these dairy farms in 2011 and these farms are expected to begin commercial production in 2012. We believe the combined raw milk generated from these dairy farms construction will allow us to achieve a self-sufficient supply of raw milk required by our production of milk formula products and whole milk powder products. We currently estimate that the total investment to develop these dairy farms will be approximately RMB650 million, which we intend to utilize for the purchase of land and buildings, milking and transportation equipment and dairy cows.

Depending on the progress of and to support the development of our vertical integration plan, we may acquire or construct a cattle feed processing plant to meet the feed requirements for all our dairy farms. Assuming that the development of our 25 new dairy farms progress as anticipated, we currently expect to start construction or acquire the cattle feed processing plant in 2011 and we target for the plant to enter commercial production in 2012. The expected cost of investment is approximately RMB100 million. We currently intend to fund a portion of this investment with the net proceeds from this offering and our internal cash.

In order to support the expansion of our milk formula business as well as to provide additional capacity to process the raw milk produced by our new dairy farms, we may acquire or construct additional raw milk processing capacity in 2013. We currently expect to fund a portion of the not less than RMB400 million investment of the additional processing capacity with the net proceeds from this offering and our internal cash.

We may adjust the timing, amount of actual expenditures and the way we fund the implementation of our vertical integration plan in response to future events or developments, such as changing market conditions, the outlook for our industry and where applicable, the historical results and outlook of potential acquisitions targets, the level of demand for our products, changes in social, political and economic conditions, and the regulatory environments in which we operate, and, thus, may reallocate the use of the proceeds. Pending application of the net proceeds of this offering, we intend to invest such net proceeds in “Temporary Cash Investments” as defined under “Description of the Notes.”

We will review and evaluate the progress of this part of the second stage of our vertical integration plan before determining the timing and scale of the rest of our second stage plan. We believe that our vertical integration strategy will enable us to secure a self-sufficient supply of raw milk for our production and greatly reduce our dependence on external sources for raw milk in the future. This will allow us to better control the quality and cost of the raw milk we use and to ensure the stability and sufficiency of our raw milk supply which in turn will enhance our competitiveness in terms of pricing.

Recent Developments

In connection with the development of the dairy farm planned as part of the first stage of our vertical integration plan (see “— Business Strategies — Evaluate integration opportunities to expand our business upstream into raw milk production.”), our new wholly owned subsidiary, Wuchang Benniu, entered into a lease agreement on March 22, 2011 with Wuchang Pingfangdian pursuant to which Wuchang Benniu has agreed to lease 500 mu (approximately 83 acres) of land in Wuchang for a term of 30 years for RMB30,000 per year (the “Land Lease”). The lease will expire on March 21, 2041 and is subject to customary termination provisions. We have the right to renew the lease after expiration for such further duration and upon such conditions as may be agreed with Wuchang Pingfangdian provided those terms are no less favorable than terms proposed by any other third party who offers to lease the land.

Pursuant to the new circular issued by the AQSIQ on November 1, 2010, we are required to re-apply for the National Industrial Production Permit according to the new requirements of inspecting infants formula power and dairy products’ production conditions before March 1, 2011, otherwise the existing dairy product enterprises will be suspended from producing dairy products and infant formula powder. The AQSIQ in a press conference further announced that the deadline has been extended to the end of March, 2011. On March 25, 2011, our Daqing Dairy production facilities passed the re-examination test and received the requisite production permit re-issued by the Quality and Technical Supervision Bureau of Heilongjiang (黑龍江省質量技術監督局). On the same date, the Changqing production facility has also successfully passed an in-depth inspection and obtained the requisite production permit from the Quality and Technical Supervision Bureau of Heilongjiang.

Products

Overview

We are principally engaged in the production, marketing and sale of medium-to-high and premium priced milk formula products in China. Our dairy products are classified into the following two main categories: milk formula products and whole milk powder products.

Our milk formula products and whole milk powder products accounted for 80.7% and 18.4% of our revenue, respectively, for the year ended December 31, 2008, 84.6% and 12.1% of our revenue, respectively, for the year ended December 31,2009 and 92.4% and 5.2% of our revenue, respectively, for the year ended December 31, 2010.

Our milk formula products and whole milk powder products include a full range for infants and children.

Milk Formula Products

Our main product category, milk formula products, is divided into the following series:

- Shi Jia brand 仕加配方奶粉系列 — products in our Shi Jia brand, which we launched in June 2010, are designed for consumers of premium priced milk formula products;
- Emilon brand 愛美樂配方奶粉系列 — products in our Emilon brand are designed for consumers of medium-to-high priced milk formula products. Our Emilon brand is the largest contributor to our revenue, generating 70.2% of the total revenue for the year ended December 31, 2010; and
- Daqing brand 大慶牌配方奶粉系列 — products in our Daqing Milk Formula Series are designed for consumers of low-to-medium priced milk formula products.

A milk formula product consists of milk powder blended with various ingredients to meet the nutritional needs of persons of different age groups.

Our infant and pediatric milk formula products aim to supply the balanced nutrition that an infant or a child needs in the child's first few months and throughout the various stages of childhood growth and development.

Our infant and pediatric milk formula products include various vitamins and essential minerals. In addition, certain of our infant and pediatric milk formula products include various combinations of precursors of docosahexaenoic acid (DHA) and arachidonic acid (ARA) (being alpha-linolenic acid (亞麻酸) and linoleic acid (亞油酸)), beta-carotene (胡蘿蔔素), nucleotides (核苷酸), galacto lactulose (低聚果糖), polyfructose (多聚果糖), choline (膽堿) and casein phosphopeptides (CPP) (酪蛋白磷酸肽). These ingredients are intended to strengthen infants' and children's immune systems, support brain, vision and bone development and promote the growth of beneficial intestinal microflora.

For older children, adults, the elderly, pregnant and lactating women, we produce milk formula products fortified with various combinations of calcium, zinc, iron and other ingredients to help facilitate bone growth in pre-adults and prevent osteoporosis later in life, strengthen the immune system, support general growth and development, and provide supplements in meeting nutritional requirements.

Shi Jia Brand 仕加配方奶粉系列

The products in our Shi Jia brand 仕加配方奶粉系列 were launched in June 2010 and are designed for consumers of premium priced milk formula products. We have two different product lines catering for changing nutritional requirements of infants and children, and providing nutritional supplements for post-natal women.

Shi Jia Jia You Bao Bao Series 仕加嘉友寶寶系列

Our Shi Jia Jia You Bao Bao Series 仕加嘉友寶寶系列 is divided into three stages for infants and toddlers:

- Stage 1 Infant Milk Formula is suitable for newborn infants up to six months of age;
- Stage 2 Follow-up Milk Formula is suitable for infants and toddlers from six to 12 months of age; and
- Stage 3 Growing-up Milk Formula is suitable for toddlers from 12 to 36 months of age.

Our Shi Jia Jia You Bao Bao Series 仕加嘉友寶寶系列 includes ingredients intended to strengthen infants' and children's immune systems, enhance their digestive system and support brain and vision development.

Shi Jia S'Plan Series 仕加斯普恩系列

Our Shi Jia S'Plan Series 仕加斯普恩系列 is divided into two stages for post-natal women:

- Stage 1 Post-natal Milk Formula is suitable for post-natal women from the date of giving birth up to 42 days after giving birth; and
- Stage 2 Post-natal Milk Formula is suitable for post-natal women for the period after 42 days of giving birth.

Our Shi Jia S'Plan Series 仕加斯普恩系列 includes ingredients intended to provide nutritional supplements for post-natal women which replenish their nutritional reserves, enhance the recovery of their immune systems, the reproduction of body cells, support their brain functions and enhance their memory.

For the year ended December 31, 2010, our revenue attributable to the sale of our Shi Jia brand was RMB43.4 million, which accounted for 4.7% of our total revenue. The sales volume of our Shi Jia brand for the year ended December 31, 2010 was 284 metric tons.

Emilon Brand 愛美樂配方奶粉系列

The products in our Emilon brand 愛美樂配方奶粉系列 were first launched in April 2007 and are designed for consumers of medium-to-high priced milk formula products. We have three different product lines with different specifications and characteristics to cater for the changing nutritional requirements of infants and children as follows:

Emilon Shuang Neng Series
愛美樂雙能系列

Our Emilon Shuang Neng Series 愛美樂雙能系列 was launched in April 2007 and is divided into three stages for infants and toddlers:

- Stage 1 Infant Milk Formula is suitable for newborn infants up to six months of age;
- Stage 2 Follow-up Milk Formula is suitable for infants and toddlers from six to 18 months of age; and
- Stage 3 Growing-up Milk Formula is suitable for toddlers from 12 to 36 months of age.

Our Emilon Shuang Neng Series includes ingredients intended to strengthen infants' and toddlers' immune systems and to enhance their digestive system.

Emilon Bei Cong Series
愛美樂倍聰系列

Our Emilon Bei Cong Series 愛美樂倍聰系列 was launched in December 2008 and is divided into three stages for infants and children:

- Stage 1 Infant Milk Formula is suitable for newborn infants up to six months of age;
- Stage 2 Follow-up Milk Formula is suitable for infants and toddlers from six to 36 months of age; and
- Stage 3 Young Children Milk Formula is suitable for children from three years of age onwards.

In addition to providing for infants' and children's overall nutritional requirements, the products in our Emilon Bei Cong Series include ingredients which are intended to support infants' and children's brain, vision and bone development and to enhance their memory.

Emilon You Zhi Series
愛美樂優智系列

Our Emilon You Zhi Series 愛美樂優智系列 was launched in May 2010 and is divided into three stages for infants and children:

- Stage 1 Infant Milk Formula is suitable for newborn infants up to six months of age;
- Stage 2 Follow-up Milk Formula is suitable for infants and toddlers from six to 36 months of age; and
- Stage 3 Young Children Milk Formula is suitable for children from three years of age onwards.

In addition to providing infants' and children's overall nutritional requirements, the products in our Emilon You Zhi Series include ingredients which are beneficial to infants' and children's digestive systems, and are intended to support their brain, vision, bone and immune system development.

We have a special milk formula product, Emilon Mama 愛美樂媽媽奶粉 under our Emilon You Yun Xi Tong Series 愛美樂優孕系統配方系列, for pregnant and lactating women, designed to ensure a sufficient supply of nutrition for developing foetuses or breastfed infants and to provide nutritional supplements for post-natal women. This series was launched in 2009.

Emilon You Yun Xi Tong Series 愛美樂優孕系統配方系列

For the year ended December 31, 2010, our revenue attributable to the sale of our Emilon brand was RMB647.0 million, which accounted for 70.2% of our total revenue. The sales volume of our Emilon brand for the year ended December 31, 2010 was 9,053 metric tons.

Daqing Milk Formula Series 大慶牌配方奶粉系列

The products in our Daqing Milk Formula Series 大慶牌配方奶粉系列 were launch in May 2009 and are designed for consumers of low-to-medium priced milk formula products and are suitable for children, adults and the elderly.

Our Daqing Milk Formula Series for infants and children is divided into three stages:

- Stage 1 Infant Milk Formula is suitable for newborn infants up to six months of age;
- Stage 2 Follow-up Milk Formula is suitable for infants and toddlers from six to 36 months of age; and
- Stage 3 Young Children Milk Formula is suitable for children from three years of age onwards.

Our Daqing Milk Formula Series for infants and children includes ingredients intended to strengthen infants' and children's immune systems, to enhance their digestive system, to support their brain and vision development and to enhance their memory. The other products in our Daqing Milk Formula Series are suitable for older children, adults and the elderly, and include ingredients that are intended to be used in meeting their nutritional requirements.

For the year ended December 31, 2010, our revenue attributable to the sale of our Daqing Milk Formula Series was RMB161.4 million, which accounted for 17.5% of our total revenue. The sales volume of our Daqing Milk Formula Series for the year ended December 31, 2010 was 4,484 metric tons.

Whole Milk Powder Products

Whole milk powder is made from pasteurised milk after evaporation and drying, without the addition of other ingredients, other than, in the case of certain whole milk products, the addition of sucrose. Our Daqing whole milk powder 大慶牌全脂奶粉, packaged in 25 kilogram bags, is generally used as a raw material in dairy and other food products (such as milk formula, yoghurt, condensed milk, ice cream, biscuits and cakes). Our Daqing sweetened whole milk powder 大慶牌全脂甜奶粉 is made of our whole milk powder with added sucrose and is suitable for all age groups (other than infants and toddlers below the age of three).

In November 2010, we launched Daqing Classic Milk Powder products, which are made from our whole milk powder with the addition of sucrose and repackaged in 16 25g-sachets. The Daqing Classic Milk Powder product is suitable for all age groups (other than infants and toddlers below the age of three).

Our whole milk powder products are sold under the Daqing 大慶 brand.

For the year ended December 31, 2010, our revenue attributable to the sale of our whole milk powder products was RMB48.3 million, which accounted for 5.2% of our total revenue. The sales volume of our whole milk powder products for the year ended December 31, 2010 was 1,975 metric tons.

Sales And Marketing

Branding and Product Positioning

We believe that our brand recognition and reputation have been vital to the success and growth of our business. Since the establishment of our production facility in Daqing in 1970, we have received various awards and certifications which have helped increase the brand recognition of our products. Some of our key awards and certifications include the following:

Awards/certifications	Year of award/ Certification	Key issuing institution/authority
”Green” Food Product Certification	2007	China Green Food Development Center
National Quality Assurance Food Products	1999	China Food Industry Association
Provincial Advanced Enterprise on Quality Control Management	1999	Quality Control Management Association of Heilongjiang
Famous Trademark in Heilongjiang	1999	Heilongjiang Provincial Administration For Industry & Commerce
Famous Brand in Heilongjiang for the Year 1996 (Daqing Milk Powder)	1996	Heilongjiang Quality Supervision and Inspection Association Heilongjiang Quality Control Management Association and the Consumers’ Association of Heilongjiang
China National Advanced Enterprise (Quality and Efficiency Type)	1995	China Food Industry Association
Advanced Enterprise on Technical Supervision for the Year 1990	1991	People’s Government of Daqing

We have also adopted “green, healthy and safe” as the principal themes of our product image, which we believe encourages consumers to view our products as natural and high quality.

We have marketed our milk formula products under three brands. The products in our Shi Jia brand marketed to consumers of premium priced milk formula products and are intended to be suitable for infants and children at different growth stages as well as post-natal women. We intend to target our Shi Jia brand at consumers in second- and third-tier cities, particularly eastern coastal cities and certain third-tier cities in the PRC.

The products in our Emilon brand are designed for consumers of medium-to-high priced milk formula products catering for the changing nutritional requirements of growing infants and children. We market our Emilon brand at consumers in second- and third-tier cities. The products in our Daqing Milk Formula Series are targeted at consumers of low-to-medium priced milk formula products and are intended to be suitable for children, adults and the elderly. We market our Daqing Milk Formula Series to consumers in villages and counties near second- and third-tier cities. We believe that this product differentiation has enabled us to highlight the unique aspects of our various milk formula products and raise their profile as quality products. In addition, we believe that the product positioning of our Shi Jia brand, Emilon brand and Daqing Milk Formula Series aptly covers consumers in different geographical locations with different consumer purchasing power.

Sales and Distribution

Milk Formula Products and Whole Milk Powder Products

Sale through distributors

We primarily sell our milk formula products and whole milk powder products through an extensive network of over 140 distributors in China. Our distributors sell our milk formula products and whole milk powder products to directly to retail outlets, such as children's and parenting specialty stores, smaller supermarkets and mom and pop shops in 21 provinces and Chongqing. We have business relationships of at least one to three years' duration with our five largest distributors during the years ended December 31, 2008, 2009 and 2010.

The map below shows the coverage of our distribution network as at December 31, 2010:

The table below sets forth the number of our distributors by provinces and cities in the PRC:

	As of December 31,		
	2008	**2009**	**2010**
Northeastern Region (1)	14	33	49
Central Region (2)	2	16	36
Southeastern Region (3)	3	15	42
Southwestern Region (4)	—	3	16
Total	19	67	143

(1) Northeastern Region refers to Heilongjiang, Jilin and Liaoning.

(2) Central Region refers to Hebei, Shanxi, Shaanxi, Shandong, Hunan, Hubei, Henan and Tianjin.

(3) Southeastern Region refers to Zhejiang, Jiangxi, Anhui, Guangdong, Guangxi, Jiangsu and Fujian.

(4) Southwestern Region refers to Sichuan, Chongqing, Yunnan, Guizhou and Gansu.

In 2009 and 2010, we continued to focus and expand our existing distribution network in Heilongjiang and increased our product coverage in other areas in the PRC which were not previously covered by our distribution network. Furthermore, we believe that our advertising campaign on China Central Television (CCTV) has also increased our brand recognition in these areas and enabled us to attract more distributors from these areas. This led to an expansion of our distribution network in 2009 and 2010 in other provinces beyond Heilongjiang and an increase in our distributors from 19 in 2008 to 67 and 143 in 2009 and 2010, respectively.

For each of the years ended December 31, 2008 and 2009, approximately 74.7% and 69.1% of the Daqing Dairy Group's sales, respectively, were made to the Daqing Dairy Group's distributors. For each of the years ended December 31, 2008, 2009 and 2010, approximately 71.7%, 69.1% and 85.5% of our sales, respectively, were made to our distributors. See "Risk Factors — We rely on our distributors to distribute and market our products, and their failure to perform to our expectations may here a material adverse effect on our business, financial condition and operating results."

We have non-exclusive distribution agreements with all of our current distributors. These agreements are generally for a term of one year. Under these agreements, our distributors may distribute other brands of dairy products. We consider that the non-exclusive nature of the distribution agreements enables us to select distributors with extensive experience in the distribution of international and domestic brand milk formula products and that such experience and credentials, in turn, facilitate the promotion of our milk formula products and whole milk powder products and provide broad coverage of the distribution network. Our distributors are only permitted to sell our milk formula products and whole milk powder products in their designated distribution areas under the distribution agreements.

We have pre-set annual sales targets for our distributors. In each year, if a distributor meets the pre-set annual sales target, we grant a sales rebate to the distributor in an amount equivalent to 3% of the annual sales (including 17% VAT) generated by the distributor (excluding the sales of our whole milk powder packaged in 25 kilogram bags). Although we do not set any quarterly sales target for our distributors, we grant quarterly sales rebates to our select distributors in an amount equivalent to 5% of the quarterly sales (including 17% VAT) of the relevant distributor.

In general, we require our distributors to pay the full purchase price before we deliver our products to them. Sales payments are normally settled through bank transfers. We recognize our sales to the distributors when we deliver our products to them and the title to such products passes to them without recourse.

We assign district sales managers for each geographical region and sales representative to each distributor to: (a) assist our distributors in promoting our milk formula products and whole milk powder products; (b) evaluate their distribution activities and monitor their compliance with our product management policies; (c) exchange information relating to market developments and changes in consumer preferences and needs; (d) visit our distributors in order to monitor their inventory levels and carry out on-site inspections; and (e) solicit consumer feedback. We have set monthly sales targets for our district sales managers. If they meet their monthly sales targets and comply with our sales policy (including no excessive sales of our products to any distributor), they are entitled to commissions ranging from 0.01% to 0.03% of sales (including 17% VAT) to the distributors for which they are responsible. We consider that our direct distribution arrangements with experienced distributors with own distribution networks and sales channels provide us an efficient and effective distribution structure and at the same time offer a higher level of profit for the parties involved in the distribution chains, which, in turn, incentivizes our distributors to promote sales of our milk formula products and whole milk powder products.

Direct sale

We also sell our whole milk powder (packaged in 25 kilogram bags) directly to our customers, such as food processing enterprises, and our milk formula products and other whole milk powder products directly to supermarkets and other retail chain stores in Daqing and other customers who purchase from us on an ad hoc basis. We entered into non-exclusive agreements with these supermarkets and other retail chain stores. The direct sale of our milk formula products and whole milk powder products in Daqing enables us to maximise our profitability where the additional costs involved to sell our milk formula products and whole milk powder products directly are relatively low.

In general, we grant credit terms of up to 30 days for direct sales of our milk formula products and whole milk powder products. Sales payments are normally settled through bank transfers. We do not offer any discount and rebates to these customers to whom we directly sell our products.

Our top five customers during the years ended December 31, 2008 for the Daqing Dairy Group and the years ended December 31, 2009 and 2010 for the Group comprised distributors and supermarkets.

Sales and Marketing Activities

Our district sales managers serve as a point of contact between us and our distributors. Our district sales managers regularly visit our distributors to collate from our distributors information on inventory levels and carry out on-site inspections in order to ensure that the distributors comply with our operational guidelines and procedures. Our district sales managers will prepare a report on their on-site inspections every quarter. This enables us to monitor our distributors' compliance with our operational guidelines and procedures more effectively. In addition, our district sales managers also exchange information with our distributors relating to market development and changes in consumer preferences and needs. We also put in place a toll-free customer service line which enables our customers to contact us directly on product-related enquiries. This enables us to obtain market information and feedback on consumer preferences and needs.

The sale of our products is subject to seasonality. We typically experience higher sales of milk formula products and whole milk powder products in the second half of the year compared to the first half. We believe that this mainly reflects an increase in purchase orders made by our distributors in the second half of the year to increase inventories in advance of the Chinese New Year in anticipation of higher demand around the holiday period. It is also possible that our distributors increase their purchases in the second half of the year to meet their sales targets so that they qualify for annual sales rebates. From time to time, we make visits to our distributors to monitor their inventory levels and are not aware of any significant instance of over-stocking of our products. For further information, see "Risk Factors — Our operating results are subject to seasonal fluctuation and other variations" and "Business — Seasonality."

We have also appointed advertising and public relations companies to implement various promotional activities for our products to further penetrate the local milk formula market. During the years ended December 31, 2008, 2009 and 2010 of the Group, these advertising and public relations companies launched a number of promotional activities to generate publicity for, and increase awareness of our products, including advertisements on Central China Television (CCTV) and various television channels in Heilongjiang and Shandong, advertisements on buses, roadshows, as well as participation in the Confectionery and Alcohol Convention in the PRC (糖酒會). We intend to increase the scope of our promotional activities to include direct advertising campaigns on nationwide and local television channels, newspapers, magazines, internets and other media as well as participation in product promotional activities.

Our advertising and promotion expenses represented approximately 1.5%, 2.2% and 3.1% of our revenue for each of the years ended December 31, 2008, 2009 and 2010, respectively.

Counterfeit Products

We have a unique bar code printed on each of our products. We did not experience any known instances of counterfeiting of our products during the years ended December 31, 2008, 2009 and 2010 of the Group, and we believe our anti-counterfeiting measures are currently appropriate and sufficient to protect our brands.

Raw Materials and Suppliers

Raw Milk

Raw milk is the primary raw material for the production of our products. Our raw milk is sourced from selected milk collection centers which, in turn, collect raw milk from dairy farms and individual dairy farmers in proximity to Daqing. We have at least one to two years of business relationship with our five largest raw milk suppliers during the years ended December 31, 2008, 2009 and 2010 of the Group. We have non-exclusive raw milk supply agreements with over 15 milk collection centers, which provide us with sufficient and stable supply of high quality raw milk. A majority of the current milk collection centers with whom we have entered into raw milk supply agreements are privately-owned entities. These agreements are generally for a term of one year. Both parties to the relevant non-exclusive raw milk supply agreement have the right to terminate the agreement if the agreement cannot be implemented due to the occurrence of any unforeseeable circumstances that prevent any of the parties to the agreement from performing the agreement. We test the content and quality of all raw milk delivered to us, which include the level of protein, fat, antibiotics and impurities, and acidity and reject it if it does not comply with the National Quality Standards for Raw Milk (中華人民共和國國家標準生鮮牛乳收購標準), as we did in 2008, 2009 and 2010. Our agreements with our raw milk suppliers provide that we have the right to terminate the raw milk supply agreements if the raw milk supplied contains contaminants.

At the milk collection centers, dairy cows are milked daily using milking equipment. To maintain freshness, milk collected from the cows is quickly stored and chilled at a temperature between 3°C and 6°C. Shortly thereafter, the milk collection centers arrange for trucks to deliver the stored and chilled raw milk to our production facilities. We normally process and use all raw milk delivered to us on the same day of delivery after we have tested and accepted the content and quality of the raw milk. We generally make payments in cash to the milk collection centers within 10 days after we have received the delivery of 10 days of accumulated raw milk supply from the milk collection centers. The price of the raw milk we purchase is subject to negotiation between the supplier and us at the time of purchase. The price of raw milk is influenced by a variety of factors, including seasonal factors and the overall demand for raw milk. For each of the years ended December 31, 2008, 2009 and 2010, the cost of purchases of raw milk represented approximately 64.0%, 33.9% and 48.7% of our total cost of purchases, respectively.

During the years ended December 31, 2008, 2009 and 2010, we did not experience any shortage of supply of raw milk that affected our normal operation.

Other Raw Materials

Apart from raw milk, we purchase other raw materials and packaging materials for the production of our dairy products.

The other raw materials include sucrose, whey powder (乳清粉), vegetable oil, mineral supplements, lactose, maltose, whey protein concentrate (乳清濃縮蛋白) and various flavorings. We carry out sampling tests on the quality of these raw materials delivered to us, including testing for bacteria content and both physical and chemical properties before we accept and store them for use at a later stage. As these raw materials generally have product expiry dates, we check the raw materials and their product expiry dates before we use them in our production. Apart from whey powder, lactose and whey protein concentrate, which are imported into China through domestic suppliers, the other raw materials and packaging materials are sourced within China.

In general, we have entered into framework supply agreements with suppliers of raw materials and packaging materials for a term of one year, and such agreements are renewable by agreement between both parties on a yearly basis. The agreements with our raw material suppliers generally provide that our raw material suppliers shall compensate us for losses we suffer as a result of defective raw materials supplied to us. During the years ended December 31, 2008, 2009 and 2010, we did not experience any shortage of supply of such raw materials and packaging materials that affected our normal operation. In general, the prices of the other raw materials are based on market prices and the prices of packaging materials are based on the agreed prices as stipulated in the framework supply agreements in respect of the packaging materials.

Production

Production Facilities

We have two production facilities in Daqing and Wuchang. We currently expect the Changqing production facility located in Wuchang to commence operation in second quarter of 2011.

Our Daqing production facilities have a total area of approximately 188,447 sq.m. and 23 buildings (with a total gross floor area of approximately 40,174 sq.m.) for use such as production lines, warehouses, carports, offices, a research and development center (including a quality testing room and a precision instrument analysis room), a boiler plant, a laundry room, a guardhouse, staff quarters, a conference center and staff canteen. Phase one of our Daqing production facilities consists of two production lines for milk formula products and whole milk powder products and one production line for ice cream products, whereas phase two of our Daqing production facilities consists of one production lines for milk formula products and whole milk powder products. In total it houses three production lines for milk formula products and whole milk powder products and one production line for ice cream products.

Our Changqing production facility has a total area of approximately 60,000 sq.m. and eight buildings (with a total gross floor area of approximately 22,575 sq.m.) for use such as production lines, warehouses, offices, guardhouses, a research and development center (including a quality testing room), a boiler plant and a staff canteen. It houses a production line for our milk formula products and whole milk powder products.

We have obtained various National Industrial Production Permit (全國工業產品生產許可證) in respect of the products produces by Daqing Dairy. These licenses and certificates are subject to renewal or extension to carry on the business of food production and processing. Pursuant to the new circular issued by the General Administration of Quality Supervision, Inspection and Quarantine of the PRC ("AQSIQ") on November 1, 2010, we are required to re-apply the National Industrial Production Permit according to the new requirements of inspecting infants formula power and dairy products' production conditions before March 1, 2011, otherwise the existing dairy product enterprises will be suspended from producing dairy products and infant formula powder. The AQSIQ in a press conference further announced that the deadline has been extended to the end of March, 2011. On March 25, 2011, our Daqing Dairy production facilities passed the re-examination test and received the requisite production permit re-issued by the Quality and Technical Supervision Bureau of Heilongjiang (黑龍江省質量技術監督局). On the same date, the Changqing production facility has also successfully passed an in-depth inspection and obtained the requisite production permit from the Quality and Technical Supervision Bureau of Heilongjiang.

We have also obtained the GMP certification in respect of the phase one production lines at our Daqing production facilities for the production of our milk formula products and whole milk powder products in 2007. We have also obtained, in the end of 2010, the GMP certification for the phase two production line at our Daqing production facilities in respect of the production of our milk formula products and whole milk powder products. In addition, we have obtained the HACCP Management System Certification (危害分析與關鍵控制點體系認證) for Daqing Dairy in respect of the production of our milk formula products and whole milk powder products in December 2010.

We intend to apply for such GMP certification and HACCP Management System Certification (危害分析與關鍵控制點體系認證) in respect of the new production line at our Changqing production facility in the near future.

Global Milk Singapore acquired Daqing Dairy on July 25, 2008. Since this acquisition, we have focused on promoting our milk formula products for infants and children. Our production and sales operations were suspended from June 2006 to March 2007 pending installation of new equipment and machinery at the production facility.

Our utilization rate for our Daqing phase one production lines for milk formula products and milk powder products was high in 2009 and the preceding months in 2010 before the commencement of operations of our Daqing phase two production line for milk formula products and whole milk powder products at our Daqing production facilities in May 2010. Given the enlargement of our distribution network and the related increase in demand for our milk formula products and whole milk powder products in 2009 and 2010, we sourced approximately 1,669 metric tons and 300 metric tons of whole milk powder (packaged in 25 kilogram bags), respectively, from Jintianran Dairy. The externally sourced whole milk powder product met our quality standards and requirements, and all of it was sold. In 2009, we produced approximately 1,293 metric tons of whole milk powder. We have recently constructed the phase two production line at our Daqing production facilities and the new production line at our Changqing production facility. We do not expect that we will need to externally source whole milk powder after these additional production lines become operational. Based on the Euromonitor Report, while the year-on-year growth rate of the baby milk powder market in China is expected to slow down from 2011 in terms of retail sales value and is expected to slow down from 2012 in terms of retail sales volume, the retail sales value and the sales volume of the baby milk powder in China between 2010 and 2014 are expected to increase. We anticipate that these additional production lines will increase our milk powder production capacity sufficiently to enable us to meet an increase in demand for our milk formula products and whole milk powder products and without the need to source whole milk powder products externally. The designed annual production capacity of our milk formula products and whole milk powder products was approximately 20,000 metric tons as of December 31, 2010. We anticipate that, when production in the Changqing production facility comes online, our designed annual milk powder production capacity of our milk formula products and whole milk powder products will be approximately 31,000 metric tons.

We repair and maintain our equipment and facilities on a regular basis.

Production Capacity

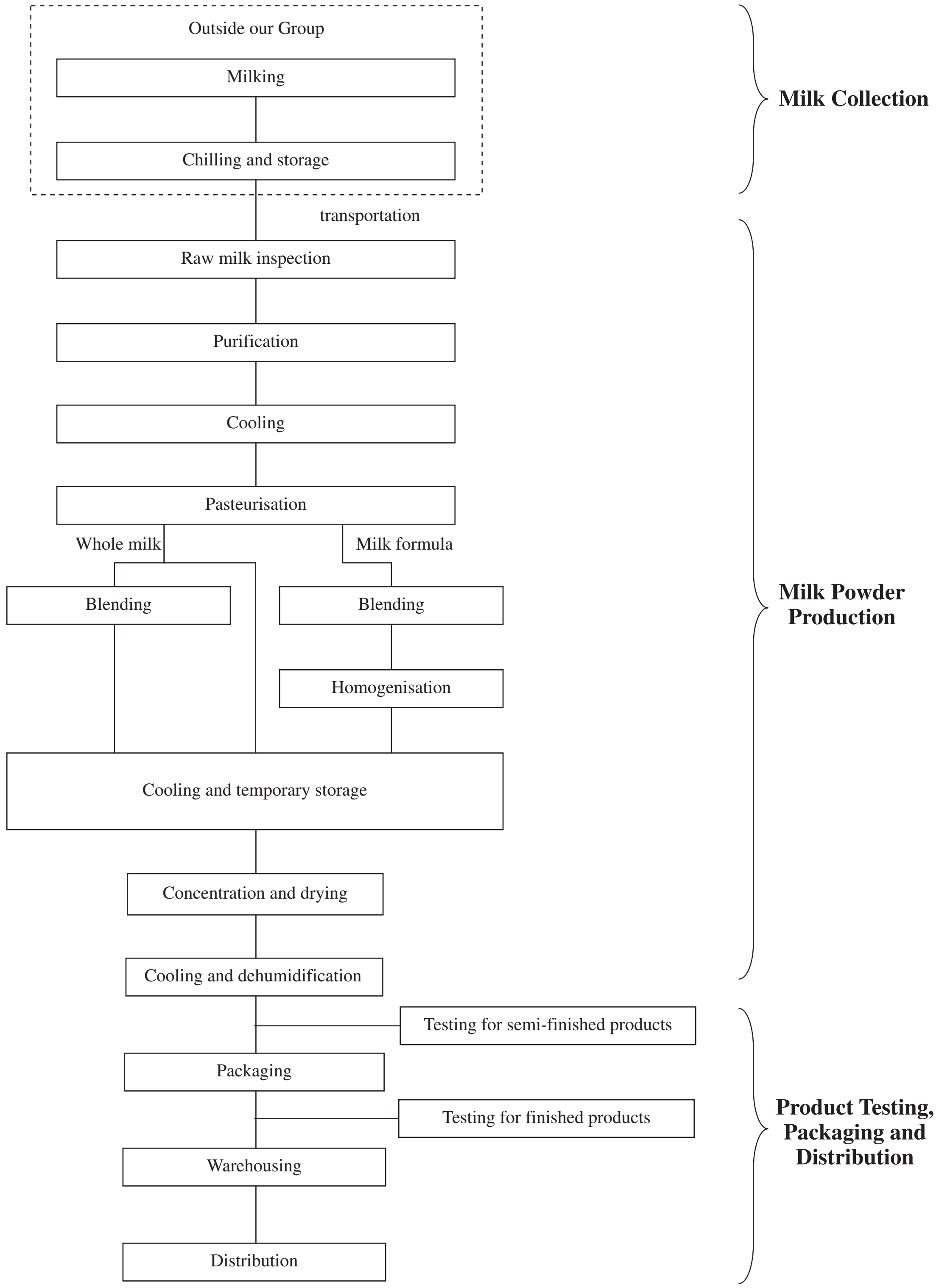
The table below sets forth our design and actual production capacities, and their utilization rates for the years ended December 31, 2008, 2009 and 2010:

	Designed capacity			**Actual outputs**			**Utilization**		
	Year ended December 31,								
	2008	**2009**	**2010**	**2008**	**2009**	**2010**	**2008**	**2009**	**2010**
	(metric tons)	**(metric tons)**	**(metric tons)**	**(metric tons)**	**(metric tons)**	**(metric tons)**	**%**	**%**	**%**
Daqing production facilities									
Phase I									
Milk powder production line.....	10,337	10,337	10,337	8,843	8,831	9,544	85.5	85.4	92.3
Ice cream.................................	3,880	11,680	11,680	440	3,667	5,361	11.3	31.4	45.9
Phase II									
Milk powder production line(1) .	—	—	6,030	—	—	5,779	—	—	95.8

(1) The utilisation rates of our production lines represent our average utilisation rates for a one-year period save for the utilisation rate for Phase II in 2010, which reflects only the utilisation rates of our production lines during the operation period since May 2010 and were calculated based on the actual production volume divided by the designed production volume.

Production Process

The diagram below illustrates, in a simplified manner, the production process for our milk formula products and whole milk powder products.



Milk collection

At the milk collection centers, dairy cows are generally milked daily using milking equipment. To maintain freshness, milk collected from the cows is stored and chilled at a temperature between 3°C and 6°C. Shortly thereafter, the milk collection centers arrange for trucks to deliver the stored and chilled raw milk to our production facilities.

Milk processing

- Raw milk inspection: At our production facilities, all raw milk delivered to us is tested for content and quality before we process and transport it for storage.
- Purification: Physical impurities are separated from the raw milk by centrifugal force.
- Cooling: After centrifugation, which increases the temperature of the milk, the milk is cooled to a temperature between 4°C and 6°C to ensure that any milk quality variations are kept to a minimum.
- Pasteurization: The milk is pasteurized by heating to a critical temperature for a specified amount of time to reduce the presence of micro-organisms.
- Blending: For the production of milk formula, the pasteurized milk is blended with various ingredients in different compositions. For the production of Daqing sweetened whole milk powder, sucrose is added during the blending process.
- Homogenization: For the production of milk formula, milk fat particles are broken down to form a smooth, uniform texture.
- Cooling and temporary storage: The milk (including the blended milk for the production of Daqing sweetened whole milk and the blended and homogenized milk for the production of milk formula) is cooled to a temperature between 4°C and 6°C before it is temporarily stored for further processing.
- Concentration and drying: After the cooling and temporary storage process, the milk is heated to evaporate the water in the milk so as to form condensed milk and is kept in a condensed milk bunker. The condensed milk is dried in a heat chamber and sprayed as a fine mist. The mist dries into milk powder. The resulting milk powder in granular form is a semi-finished product, and its physical and chemical properties are subject to testing.
- Cooling and dehumidification: After the drying process above, the resulting milk powder is channelled into a vibrating fluid bed dryer where it is cooled and dehumidified by fans so as to reduce its temperature from 65°C to a temperature between 20°C and 35°C before it is channelled into a milk powder bunker for packaging.
- Packaging: The milk powder is packaged in a bacteria-free environment using aseptic packaging materials. Packaging bags and cans for some of our products are filled with nitrogen gas to extend the shelf life of the products. After packaging, product samples are tested for compliance with the required quality standards.
- Warehousing and distribution: The finished dairy products are stored at our warehouses and subsequently distributed to our customers.

Quality Control

As at December 31, 2010, we had 39 employees engaged in quality control, of whom 38 were holders of degrees related to food science and technology or biotechnology.

We have appointed Wang Li Ying (王麗穎) as the manager of our quality control and product development department with responsibility for our overall quality control. Ms. Wang is a graduate of 東北農業大學 (Northeast Agricultural University) with a Bachelor of Science degree in Food Science and Engineering. Before joining us in 2008, she had over six years of experience in the food industry. In 2003, Ms. Wang was appointed as a Food Sensory Evaluation Expert (食品感官品評專家) by 黑龍江省完達山乳業股份有限公司 (Heilongjiang Wondersun Dairy Co., Ltd.*). In 2006, Ms. Wang received her Qualification Certificate for Professional Post Holding in Heilongjiang (黑龍江省專業技術職務任職資格證書) as a food engineer issued by the Heilongjiang Human Resources Department (黑龍江省人事廳).

In addition, we have adopted a strict quality control system over our production processes, from sourcing of raw milk to production. This is evidenced by the various awards and certifications we have received, including the GMP certification we obtained for the phase one and phase two production lines at our Daqing production facilities in 2007 and 2010, respectively, and the HACCP Management System Certification (危害分析與關鍵控制點體系認證) for Daqing Dairy in December 2010. For further details, see "Business — Sales and Marketing — Branding and Product Positioning." In 2010, we obtained ISO9001:2008 certification for the design, production and sale of infant milk formula, dairy products (milk powder and liquid milk) and cold beverages. This certification demonstrates that we have an effective quality management system that shows our commitment to quality and our ability to consistently provide products that meet customers' requirements.

Our quality control team monitors closely the implementation of our quality control system, which involves the following quality control measures:

- Raw milk: We test the content and quality of all raw milk delivered to us, which include the level of protein, fat, antibiotics and impurities, and acidity to ensure compliance with the National Quality Standard for Raw Milk (中華人民共和國國家標準生鮮牛乳收購標準) and also test the level of melamine in the raw milk to ensure compliance with the applicable quality standards in the PRC.
- Other raw materials: We carry out sampling tests on the quality of the other raw materials delivered to us, including testing for bacterial content and both physical and chemical properties before we accept and store them for use at a later stage.
- Product control: We test our semi-finished products for the water content and the level of fat and impurities in accordance with our internal quality standards. We also test on the content and quality of our finished products, which include the level of protein, fat, sucrose, impurities, bacteria, antibiotics and melamine to ensure compliance with the applicable quality standards.
- Sanitation control: Our production employees are required to wear disposable caps, masks and protective shoe covers, and change into production clothes.
- Training of personnel: We provide our quality control staff members with compliance training to ensure proper implementation of our quality control procedures.
- Equipment cleaning and maintenance: Almost all of the equipment and piping used in our milk processing plant are made from stainless steel, and we clean the inner surfaces of our milk processing equipment and piping system once a day using a CIP (cleaning in place) system to manage the circulation of cleaning materials automatically through our equipment and piping system without dismantling our equipment and piping system. We also have a team of employees dedicated to monitoring and maintaining our equipment to ensure proper functioning.
- Waste management and disposal: We maintain a water treatment plant at each of our production facilities to manage and dispose of our waste water in accordance with national requirements.

The Melamine Incident

In July 2008, several infants in Gansu in the PRC were diagnosed with kidney stones after consuming milk powder products produced by a milk formula producer in the PRC that were contaminated with melamine. This led to a nationwide investigation into dairy products, particularly milk formula, for traces of melamine. According to the investigation carried out by the AQSIQ in 2008 on the products of 109 milk formula product producers in the PRC, the products of 22 milk formula product producers in the PRC (which did not include us) were found to have been contaminated with melamine. The AQSIQ has subsequently also carried out random sampling tests on the content of melamine in the products of various dairy product producers in the PRC, including us, which revealed that: (i) our Daqing Hi-Calcium and Hi-Iron Milk Formula for women (400 grams per box) and Daqing Multi-Vitamin Hi-Calcium Milk Formula (for the elderly and the middle-aged) (400 grams per box) under our Daqing Milk Formula Series; and (ii) our Follow-up Milk Formula (Stage 2) under our Emilon brand (400 grams per box), which were subject to the tests, passed the melamine tests. The

PRC government has subsequently taken stringent measures to ensure the safety of dairy products such as the recall, removal from retail shelves and destruction of the milk formula products that were contaminated with melamine. The AQSIQ has also sent officers to quality control departments of the milk formula product producers in the PRC to monitor their production processes and inspect the quality and safety of the finished products.

We believe that the common ways in which our products may be contaminated with melamine are: (i) the use of melamine-contaminated cattle feed to feed the dairy cows which form the source of the raw milk supplied to us; and (ii) the addition of melamine by third parties into raw milk at the milk collection centers or prior to the delivery of raw milk to us, or the addition of melamine during the production process of our products. During the years ended December 31, 2008, 2009 and 2010, (i) we did not add any melamine into our products; (ii) none of our products contains any melamine; and (iii) we did not experience any product dispute, product recall or return of products which may have had a material adverse effect on our financial condition or operating results. During the years ended December 31, 2008, 2009 and 2010, none of our products were subjected to any government sanctions relating to quality.

Our Emilon brand of milk formula products, which are targeted at consumers of the middle-to-high income group in the second- and third-tier cities in China, has been negatively affected by the melamine incident. This led some consumers within this target customer group, which generally have stronger purchasing power, to switch to imported brands of milk formula. While this slowed the rate of our revenue growth of the Emilon brand, sales of our Emilon brand still increased despite the difficult market conditions. On the other hand, our Daqing Milk Formula Series recorded faster revenue growth as a result of the melamine incident. The melamine incident led certain players in China that were affected by the melamine incident to exit the market. As consumers in the counties and villages in rural areas in China generally have lower purchasing power, they were in many cases unable to switch to imported brands, which are generally higher-priced products. As a result, significant numbers of consumers in these areas switched to other domestic brand products such as our Daqing Milk Formula Series, which are targeted at consumers in villages and counties near second- and third-tier cities in the PRC.

The gross profit margin of the Daqing Dairy Group decreased from 49.9% for the year ended December 31, 2008 to 46.9% for the year ended December 31, 2009, primarily due to a decrease in the gross profit margin of the Daqing Dairy Group for our milk formula products, which was partially offset by an increase in the gross profit margin of the Daqing Dairy Group for our whole milk powder products. The gross profit margin of the Daqing Dairy Group for our milk formula products declined from 57.3% for the year ended December 31, 2008 to 53.5% for the year ended December 31, 2009. The decline in the gross profit margin of the Daqing Dairy Group for our milk formula products was primarily due to the decline in the gross profit margin of the Emilon brand milk formula by 3.7%, as a result of changes in the sales mix of the Emilon brand product offerings with more of the lower margin Emilon Bei Cong Series being sold compared to the higher margin Emilon Shuang Neng Series as target consumers in the higher priced market segment were more affected by the melamine incident.

The gross profit margin of the Group increased to 51.9% for the year ended December 31, 2010, primarily due to the introduction of our Shi Jia brand with relatively higher gross profit margin of 71.8% and the shift in product mix in favor of the higher gross profit margin milk formula products from 84.6% of revenue in the year ended December 31, 2009 to 92.4% of revenue for the year ended December 31, 2010.

The tests conducted by an external testing center on some of our milk formula products and whole milk powder products in 2008 and 2009 on a sampling basis, and the tests conducted by two external testing centers on all of our milk formula products and whole milk powder products in 2010, confirmed that these products did not contain melamine. These external testing centers are independent parties with respect to the Group. Furthermore, the various internal melamine tests carried out by us on the raw milk supplied to us and some of our finished products in 2008 and 2009 confirmed that these raw milk and finished products did not contain any melamine.

The Hormone-Tainted Milk Formula Incident

In August 2010, three infants in Hubei in the PRC were reported to have experienced pubescent development, which was allegedly caused by the content of estrogen hormones found in a particular domestic brand milk formula products they consumed. This resulted in the Ministry of Health of the PRC launching an investigation into the above alleged claims. The clinical investigation conducted by the Ministry of Health of the PRC on the residue of milk powder consumed by these infants revealed that the milk formula products involved did not contain estrogen hormones such as diethylstilbesterol (乙烯雌酚), medroxy progesterone acetate (醋酸甲孕酮), estradiol (雌二醇) and progesterone (孕酮) that caused these infants' pubescent development.

Our enquiries with the National Dairy Product Testing Center of the PRC (國家乳品檢測中心), the Ministry of Agriculture of the PRC, various external testing centers in Heilongjiang and a testing center in Guangzhou, a PRC government agency operated by the PRC municipal government confirm that presently, there are no requirements and applicable standards on testing of the content of estrogen hormones in dairy products in the PRC. An external testing center outside the PRC, which is an independent party with respect to the Group, was appointed to carry out a sampling test on the content of various hormones, including the above estrogen hormones, in some of our products. The external testing center confirmed that based on the minimum detectable limits of the testing equipment used to carry out the tests, the tests did not detect any of the above estrogen hormones in the sample products that were tested.

We carry out tests on the content and quality of raw milk delivered to us and our finished products in accordance with the applicable quality standards in the PRC. As there are no requirements and applicable standards in the PRC on the testing of the content of estrogen hormones in dairy products, including raw milk, we do not put in place a quality control measure to test the content of estrogen hormones in raw milk delivered to us and our products. We do not add any estrogen hormones into our products.

While we believe that the above alleged hormone-tainted milk formula incident did not have a material adverse effect on our sales of milk formula products since the incident, the incident may undermine consumers' confidence in domestic milk formula products, in particular, pediatric milk formula products and consumers may avoid their purchase of domestic brand milk formula products in the PRC. This may, in turn, have an impact of the sales of domestic brand milk formula products in the PRC. See "Risk Factors — Adverse publicity concerning milk formula and other dairy products may affect our business performance or damage our reputation, and their societal impact may lead to additional government regulations."

The Leather-Milk Incident

In February 2011, some manufacturers added leather protein powder to dairy products, which were produced from hydrolyzed leather scraps in tanneries, raising milk safety concerns similar to those raised by the melamine incident in 2008. The Ministry of Agriculture of the PRC said in an undated notice posted to the website of the State Council, China's Cabinet, that authorities will carry out 6,450 random checks on fresh milk this year — underscoring official concerns that dairy producers may still be trying to use illegal and dangerous methods to boost the protein content of their milk.

Inventory Control And Logistics

Our sales department formulates our annual, quarterly and monthly sales plans. Our production department uses that information to develop its monthly and quarterly production plans taking into account (a) the latest information on the volume of raw milk supplied, (b) the inventory levels of raw materials and finished products and (c) the volume of sales orders. Our production department then provides its monthly and quarterly production plans for its raw milk needs to our purchase department. Our inventory comprises mainly raw materials, packaging materials and finished products. As raw milk is perishable, our normal holding period for raw milk is 24 to 48 hours. However, we normally use the raw milk in our production on the same day of its delivery and do not maintain stocks of raw milk. On the other hand, our normal holding period for other raw materials is normally less than six months from the date of receipt of these raw materials to buffer any contingencies in supply and those of our finished products is normally one month after production of these finished products. We review our inventories based on inventory ageing analysis as well as the expected usage of raw materials and the expected sales of finished products in order to determine if an impairment of inventory should be made. Our other raw materials and finished products generally have a shelf life of between 12 and 24 months. In managing our inventory, we identify and use earlier batches of these raw materials using a first in, first out method. Furthermore, we perform an inventory count on a monthly basis and will treat an inventory which exceeds its shelf life (if any) as obsolete and destroy such inventory immediately. For each of the years ended December 31, 2008, 2009 and 2010, the Group did not make any provision for impairment of inventory. We engage logistics companies, which are independent parties to the Group, to deliver our milk formula products and whole milk powder products to our customers' designated places. We use our own vehicles and transportation team to deliver our ice cream products to our customers and to deliver our milk formula products to our customers to whom we sell our products directly in Daqing. We bear the cost of delivering our products to our customers.

Seasonality

Sales of our products are subject to seasonality. We typically experience higher sales of milk formula products and whole milk powder products in the second half of the year compared to the first half. We believe that this seasonality factor mainly reflects an increase in purchase orders made by our distributors in the second half of the year to increase their inventories in advance of the Chinese New Year in anticipation of higher demand around the holiday period.

Product Development

As of December 31, 2010, we had approximately six employees engaged in product development who were holders of degrees related to food science and technology. We appointed Xia Yuan Jun as our executive director and deputy chief executive officer on October 10, 2010. He is primarily responsible for overseeing product development as well as assisting our chief executive officer in executing the overall business strategies, facilitating business development and managing the operations of our Group. For further details on Mr. Xia's work experience and educational qualifications, see "Management."

Our product development team is dedicated to the following objectives and functions:

- formulating and implementing product development proposals;
- conducting tests on products and be responsible for product developments;
- collating, analyzing, processing and storing technical information of the dairy industry;
- conducting research on product developments and upgrading our existing products;
- organizing and promoting technical collaboration;
- assessing technology programmes; and
- organizing research and development on relevant technological skills.

To further our objectives, we have entered into a co-operation agreement with the College for Food Science at 黑龍江八一農墾大學食品學院 (the College of Food Science at Heilongjiang Bayi Agricultural University). Through this co-operation agreement, we have a three-year collaborative arrangement with the university to train professionals, resolve production and technical issues, and develop new products, technology, equipment and processes to achieve economic efficiency.

We have recently developed and launched new milk formula products which target consumers of premium priced milk formula products, namely three new milk formula products for infants at different growth stages under our Shi Jia Jia You Bao Bao 仕加嘉友寶寶系列 and two new milk formula products for post-natal women under our Shi Jia S'Plan Series 仕加斯普恩系列. In addition, we introduced our You Zhi Series under our Emilon brand in May 2010. The You Zhi Series is currently the most competitively priced product in the Emilon brand which allows us to compete with smaller regional competitors more effectively, especially in third-tier and below cities.

For each of the years ended December 31, 2008, 2009 and 2010, our annual research and development expenses, which mainly comprised the salary of our product development staff, were approximately RMB40,000, RMB104,000 and RMB163,000, respectively.

Intellectual Property Rights

We have registered certain names and logos of our product series with the State Administration for Industry and Commerce in China and the relevant PRC intellectual property administrative authorities as our trademarks. In addition, we have registered our name and logo in Hong Kong as our trademarks.

Competition

We face competition in many aspects of our business. We consider that we compete against domestic and international producers of milk formula products and milk powder products based on product range, brand recognition and reputation, product quality and price, as well as the coverage and effectiveness of the sales and distribution network.

According to the Euromonitor Report, leading global dairy companies, such as Mead Johnson (Guangzhou) Ltd., International Nutrition Co Ltd, Nestle (China) Ltd, Shanghai Wyeth Nutritional Co Ltd and Abbott Nutrition International (China), are market leaders and collectively account for almost 40% of the total market share by sales value in the market in China in 2009. Domestic brands, such as Yili (伊利), Wondersun (完達山), Beingmate (貝因美) and Synutra (聖元) are attempting to gain greater market share in the milk powder market in China.

We believe that, as consumers have become more conscious of the quality of milk formula products and milk powder products following various contamination incidents in recent years, competition in the milk formula and milk powder market has been shifting away from price, making quality and brand reputation increasingly important.

We further consider that, as the PRC government has tightened regulation of the dairy industry in the wake of several food safety incidents, the barriers to entry have grown and the market has become less fragmented. We consider that new market entrants face substantial barriers to entry, including acquiring significant start-up capital, meeting demanding production requirements and standards, and securing reliable and affordable sources of quality raw milk, as well as securing an effective distribution network. We believe that with the greater consumer focus on quality, the tightening regulation and the higher barriers to entry, as well as the PRC government's policies encouraging consolidation in the dairy industry, the milk formula product and milk powder industry will experience consolidation, especially among small-scale enterprises with low productivity, poor quality and poor brand recognition. This consolidation may increase on average the production capacity of larger, more technologically advanced enterprises, which could benefit us but could also create more formidable competitors.

We believe that this consolidation will result in an industry in which the production and distribution of milk formula and milk powder will be dominated by a few market leaders with large production capacity, strong brand recognition and reputation and extensive sales and distribution networks. In addition, we believe that those producers that control their own sources of raw milk will be better positioned for fast growth because of the reliability of supply, the relative stable prices and the ability to better control the quality of raw milk used to make their products. We consider that we are well-positioned to compete effectively in the PRC market and that our strengths will distinguish us from our competitors. We also believe that our position and competitive advantage over some players, such as our longstanding history in the milk formula and whole milk powder market in the PRC, and our access and proximity to the strategic and unique geographic conditions in Daqing, will enable us to capture an increasing portion of the market shares in the PRC, which will reinforce our market position and increase our returns. Furthermore, we believe our intention to evaluate integration opportunities for upstream expansion will further enhance our position in relation to our competitors.

While the market has yet to see a local milk powder manufacturer capable of overriding the leading global brand producers, we believe this will provide us with opportunities to grow, to increase our market share and to further enhance our position in the PRC market. See "Business — Competitive strengths" and "Industry Overview."

Employees

As of December 31, 2010, we had over 500 full-time employees. The following table sets forth a breakdown of our personnel by function as of December 31, 2010:

Management, finance and administration	64
Production	223
Sales, marketing and logistics	208
Procurement	11
Quality control	33
Product development	6
Total	545

We offer to our new employees training relating to our Group and its structure. In addition, we provide in-house training to our employees to enhance their knowledge of our products, production methods, production safety and corporate culture.

Insurance and Welfare Contributions

We maintain insurance on our motor vehicles. However, we do not maintain property, machinery, equipment, inventory, third party liability, product liability or business interruption insurance. We believe that the cost of obtaining product liability insurance in the PRC is high. We have strict quality control system over our production. See "Business — Quality Control" for further details on our quality control system. In addition, during the years ended December 31, 2008, 2009 and 2010, we did not experience any product dispute, product recall or return of products which may have had a material adverse effect on our financial condition or operating results and none of our products had been subject to any government sanctions relating to quality. Therefore, we currently do not consider it necessary to maintain product liability insurance.

In accordance with relevant PRC laws and regulations, we contribute to social welfare insurance for our full-time employees in the PRC, including basic pension insurance, basic medical insurance, unemployment insurance, work-related injury insurance and maternity insurance. See "Regulatory Overview — Laws and regulations relating to labor matters." Prior to April 2010, Daqing Dairy did not register with the relevant authority in respect of the housing provident fund or make any contributions to the housing provident fund. Since its incorporation, Changqing Dairy has not registered with the relevant authority in respect of the housing provident fund or made any contributions to the housing provident fund. See "Risk Factors — We did not comply with PRC regulations relating to the housing provident fund."

Land and Buildings

As at December 31, 2010, we owned three parcels of land (with a total site area of approximately 248,447 sq.m.) and 31 buildings (with a gross floor area of approximately 62,749 sq.m.) mainly for use as our production facilities and offices. In addition, as at December 31, 2010, we owned a unit, with a gross floor area of approximately 98 sq.m., in a building for commercial use.

As at December 31, 2010, we did not lease any properties.

With the consummation of the IPO and for the purpose of the first stage of our vertical integration plan, Wuchang Benniu entered into a lease agreement on March 22, 2011 with Wuchang Pingfangdian, pursuant to which Wuchang Benniu has agreed to lease 500 mu (approximately 83 acres) of land in Wuchang for a term of 30 years for RMB30,000 per year. The lease will expire on March 21, 2041 and is subject to customary termination provisions. We have the right to renew the lease after expiration for such further duration and upon such conditions as may be agreed with Wuchang Pingfangdian provided those terms are no less favorable than terms proposed by any other third party who offers to lease the land.

Legal Proceedings and Compliance

Legal Proceedings

We may be involved in legal proceedings in the ordinary course of our operations. As at December 31, 2010, we were not engaged in any litigation, arbitration or claim of material importance. In addition, we are not aware of any litigation, arbitration or claim pending or threatened by or against us which may have a material adverse effect on our business, financial condition or operating results.

Compliance

We have obtained all licenses, permits or certificates required for the operation of our business and that we complied with all relevant PRC laws, rules and regulations that are applicable to our business during the years ended December 31, 2008, 2009 and 2010.

Environmental matters

We are subject to applicable PRC environmental laws and regulations relating to air, water, noise and solid waste pollution. For further information on the laws and regulations to environmental protection applicable to us, see "Regulatory Overview — Laws and regulations relating to environmental protection."

Our operations do not generate material levels of pollution to the environment other than some air and water pollutants, noise and solid waste such as cardboards, packaging materials for our products and boiler slag (which is a by-product generated from the use of coal as a fuel in our production).

Our quality control team formulates and monitors and the implementation of our quality control systems, including our waste water treatment plant at each of our production facilities, which manages and disposes our waste water in accordance with national standards. We also sell solid waste from our production such as boiler slags to a concrete mixing plant. As our operations do not generate material levels of pollution to the environment, we regularly inspect and maintain our production facilities as well as our waste water treatment plant at each of our production facilities to prevent and minimize noise and other pollutions to the environment in the course of our operations as opposed to engaging new technology or carrying out research and development to reduce the impact of our operations to the environment.

Workplace safety

We are subject to various PRC laws and regulations relating to workplace safety. For further information on the laws and regulations to production safety applicable to us, see "Regulatory Overview - Laws and regulations relating to production safety." Our production team is mainly responsible for monitoring our compliance with workplace safety related laws and regulations. We have also adopted a handbook on workplace safety which sets forth our workplace safety rules that all employees are required to follow. In addition, we provide in-house training to our employees to strengthen their knowledge on workplace safety.

Welfare contributions

In the PRC, we are required to comply with various national and local labor and social welfare laws and regulations. See "Regulatory Overview — Laws and regulations relating to labor matters" in this offering memorandum for further information. Prior to April 2010, Daqing Dairy did not register with the relevant authority or maintain accounts with a designated bank in respect of the housing provident fund, or make any contributions to the housing provident fund. Since its incorporation, Changqing Dairy has not registered with the relevant authority or maintained an account with a designated bank in respect of the housing provident fund, or made any contributions to the housing provident fund.

On April 14, 2010, we obtained a written confirmation from the housing provident fund management center (住房公積金管理中心) of Daqing regarding unpaid contributions during the period from April 3, 1999 (being the effective date of the implementation of the Regulation on Management of the Housing Provident Fund《住房公積金管理條例》) to April 14, 2010. According to such written confirmation, the housing provident fund management center (住房公積金管理中心) will not require Daqing Dairy to make any contribution payment in respect of the above unpaid contributions nor will any penalty or other form of administrative penalties be imposed on Daqing Dairy for the unpaid contributions to the housing provident fund. The letter of confirmation issued by the housing provident fund management centers of Daqing (大慶市住房公積金管理中心) dated June 11, 2010 confirms that since the effective date of the Regulations on Management of the Housing Provident Fund 《住房公積金管理條例》, the housing provident fund management center of Daqing (大慶市住房公積金管理中心) has been progressively implementing the regulations on private enterprises, foreign-invested enterprises and other non State-owned enterprises in Daqing and notes that a substantial number of these enterprises have not set up and contributed towards the housing provident funds and are currently taking steps to set up and contribute towards the housing provident funds. Given the progressive implementation approach of the housing provident fund management center of Daqing (大慶市住房公積金管理中心), while our legal department oversees and ensures our continued compliance with the regulations, Daqing Dairy did not register with the relevant housing provident fund management center (住房公積金管理中心) in respect of the housing provident fund immediately upon the effective date of these regulations. Since April 2010, Daqing Dairy and Changqing Dairy have registered with the relevant housing provident fund management centers (住房公積金管理中心) and maintained accounts with designated banks in respect of the housing provident funds, and made contributions to the relevant housing provident funds. See "Risk Factors — We did not comply with PRC regulations relating to the housing provident fund."

In addition, Wuchang Benniu, our recently established indirect wholly owned subsidiary in the PRC, has registered with the relevant provident fund management centers in March 2011. Wuchang Benniu will make the relevant contributions to such centers upon commencement of operation.

According to our PRC legal advisers, should the relevant local administrative authorities require us to settle the unpaid contributions in the future and we fail to do so within the stipulated time limit, the relevant local administrative authorities have the right to apply for court orders to demand payment. We may be subject to a fine in the amount of between RMB10,000 and RMB50,000 for failure to register with the housing provident fund management centers (住房公積金管理中心) or maintain accounts with a designated bank. Based on the above letters of confirmation issued by the relevant housing provident fund management centers (住房公積金管理中心), our PRC legal advisers have advised us that there is a low likelihood the relevant housing provident fund management centres will either order Daqing Dairy and Changqing Dairy to compensate for the outstanding housing provident fund contributions which they have failed to pay or impose penalties on Daqing Dairy and Changqing Dairy for the above non-compliance.

The Laws And Regulations Relating To The Industry

The primary production and operations entities of the Group are Daqing Dairy and Changqing Dairy, which are located in the PRC. Both companies' business operations, including the production, marketing and sale of milk formula products, whole milk powder and other dairy products, are subject to industrial policies, relevant laws, regulations and rules and government policies. We have also established Wuchang Benniu, proposing to develop and operate our dairy farm. With respect to its current business operations, our Group is mainly subject to the following laws, regulations and rules:

Laws and Regulations Relating to the Operation of Dairy Farms

According to the Stock-breeding Law of the PRC (《中華人民共和國畜牧法》) effective on July 1, 2006, a stockbreeding and veterinary administrative department of the People's Government at the county level or above shall, according to the stockbreeding development plan and market demands, direct and support the structural adjustment of stockbreeding, develop strong livestock and poultry production and enhance the market competitiveness of livestock and poultry products. The state shall support the grassland pasturing areas to carry out basic construction of pasture fencing, water conservancy, pasture improvement, and forage and feed bases, improve the structure of livestock flocks, improve the species of livestock, change the production form, develop penned animal feeding and rotational grazing, gradually realize the balance between the livestock and forage and improve the ecological environment of the pastures.

A dairy farm shall satisfy the following conditions: (1) production site and equipment necessary for feeding scale; (2) technicians; (3) anti-epidemic conditions required by law, administrative regulations and relevant authority of the State Council; (4) marsh gas tank or other equipment used for comprehensive utilization of livestock and poultry manure, waste water and other solid waste. Furthermore, the sponsor of the dairy farm shall register with the local relevant authority at county level in respect of the dairy farm's name, address, species of livestock and poultry and scale.

According to the Law of the PRC on Animal Epidemic Prevention (《中華人民共和國動物防疫法》) effective on January 1, 2008, the administrative departments for veterinary medicine under the local people's governments at or above the county level shall organize the implementation of the plans for mandatory immunization against animal epidemics. The People's Governments at the township level and the neighborhood offices in cities shall make arrangements for the units and individuals that raise animals in the areas under their respective jurisdiction to make a success of mandatory immunization. The units and individuals that raise animals shall perform their duties in accordance with law in mandatory immunization against animal epidemics and do a good job in this respect, as required by the administrative departments for veterinary medicine.

An animal farm shall meet the following requirements in respect of anti-epidemic: (1) the distance between the farm and residents living areas, the source of drinking water, schools, hospitals and other public places shall comply with the standard provided by the relevant authority of the State Council; (2) production areas shall be closed and separated, and project design and process flow conform to requirements of anti-epidemic; (3) there shall be free-pollution disposal equipment and disinfecting equipment for waste water, solid waste, diseasedly dead animals and infected animal product; and (4) there shall be animal anti-epidemic technicians; (5) there shall be a set of well-served system of animal anti-epidemic. Moreover, any unit or individual who intends to establish an animal farm shall apply for a Qualification Certificate for Animal Anti-epidemic.

The breeding and dairy animals and the pet animals shall be kept in conformity with the health standards set by the administrative department for veterinary medicine under the State Council. The breeding and dairy animals shall be subject to regular check-up by institutions for prevention and control of animal epidemics; the ones that fail to pass the check-up shall be dealt with according to the regulations of the administrative department for veterinary medicine under the State Council.

According to the Rule of the Record Procedure Management on the Livestock and Poultry Farms (Raising Communities) of Heilongjiang (《黑龍江省畜禽養殖場(小區)備案程序管理辦法》) effective on March 27, 2010, the stockbreeding and veterinary administrative departments of the people's governments at county level shall take charge of the local work of record. The livestock and poultry farms (raising communities) shall file a record with the stockbreeding and veterinary administrative departments at county level and obtain the Stock-breeding Code. Where the application is not filed with the relevant administrative departments, or the application is disqualified by the relevant administrative departments, the relevant unit will not be granted the Stock-breeding Code. Any unit in violation of such rule may be punished according to the Stock-breeding Law of the PRC and the Law of the PRC on Animal Epidemic Prevention.

On June 26, 2006 the Ministry of Agriculture promulgated Rules on Management of Identification and Files of Livestock and Poultry《畜禽標識和養殖檔案管理辦法》, pursuant to which, among other things, livestock and poultry farms shall: (1) obtain identification cards from the local relevant authority at county level and place cards onto the animals breed by them; (2) prepare breeding files which record livestock and poultry's species, amount, reproduction, identification, origin and in-and- out of farm dates, etc.; and (3) register with the relevant local authority and obtain breeding code.

On January 9, 2008 the general office of the Ministry of Agriculture promulgated the Production Technical Specifications of Standardized Breeding of Dairy Cows in Large Scale (Trial) 《奶牛標準化規模養殖生產技術規範(試行)》which provides technical requirements for site selection and design, preparation of feed, management of breeding, breeding selection and reproduction, hygiene and anti-epidemic, construction and management of milking spaces, disposal of animal waste and other waste, recording and management of files.

On November 7, 2008 the State Council promulgated the Notice on Forwarding Planning Outline of Dairy Industry's Rectification and Revival by NDRC and other departments《國務院辦公廳關於轉發發展改革委等部門奶業整頓和振興規劃綱要的通知》, which provides several measures to strengthen quality supervision over dairy food in all respects, rebuilt consumers' confidence, improve the quality of dairy food production enterprises, strengthen administration of purchase of raw milk and improve breeding level. Pursuant to the Notice, among other things, (i) all the dairy product enterprises are required to fulfil the standard which is listed in the Good Manufacturing Practice ("GMP") for the Dairy Product Enterprise (乳製品企業良好生產規範) which was renamed as Good Manufacturing Practice for Milk Products (乳製品良好生產規範) in 2010 within three years. Any dairy product enterprise failing to fulfil the above standard will be suspended from producing the dairy product; (ii) the infant milk power product enterprises are also required to implement HACCP Management System; and (iii) all dairy cow farms shall implement Hygiene Standards of Dairy Cow Farm (GB16568)《奶牛場衛生規範(GB16568)》within required period. Any farm failing to reach the standards within 3 years will be subject to suspending production for rectification.

On March 26, 2010 the Ministry of Health issued Good Manufacturing Practice (GMP) for Milk Products (GB12693-2010) (乳製品良好生產規範) which provides a set of standards applying to production enterprises which use cow milk (or goat milk) and its processed products as main raw materials to produce dairy products. Standards therein mainly cover production facility, hygiene management, packaging materials, food safety in process of production, inspection, storage and transportation of products, recall of defective products, training, management units and staff, and recording and file management.

On February 17, 2009 the AQSIQ and Standardization Administration jointly issued Hazard Analysis and Critical Control Point (HACCP) System-Requirements for Dairy Processing Plant (GB/T 27342-2009) (危害分析與關鍵點體系乳製品生產企業要求), which provides requirement for establishment, implementation and improvement of HACCP system in respect of dairy product production, mainly including disinfection to materials, safety and cold chain control over additives and ingredients and package materials, especially, with emphasis on transportation, storage and inspection of raw and fresh milk and other raw materials, receipt and storage of supplemental materials and package materials.

Policies relating to the Foreign-invested Pediatric Nutrition Products Industry

Guidance on the foreign investment industry in the PRC can be found in the Foreign Investment Industrial Guidance Catalogue (2007 version)《外商投資產業指導目錄》(2007年修訂), which has been promulgated and implemented from time to time. In the Foreign Investment Industrial Guidance Catalogue, which was jointly issued by the NDRC and MOFCOM on October 31, 2007, the business of development and production of infant food and food for the elderly has been listed as a business for which foreign investment is encouraged.

In addition, under the Dairy Product Industrial Policies (2009 Version)《乳製品工業產業政策(2009年修訂)》 released by the Ministry of Industry and Information Technology of the PRC (中華人民共和國工業和信息化部) and the NDRC on June 26, 2009, investment in dairy products must comply with certain admission conditions, such as the establishment and composition of enterprises, the scale and capability of processing, technology and equipment, product quality, environmental health and protection, energy consumption and production safety.

Laws and Regulations Relating to the Food and Dairy Industry

Food Safety

The Food Safety Law of the PRC《中華人民共和國食品安全法》("Food Safety Law"), which was adopted by the Standing Committee of the NPC on February 28, 2009 and became effective on June 1, 2009, stipulates that food safety standards are compulsory and must include the following:

- maximum limits relating to the level of pathogenic micro-organisms, pesticide residue, veterinary medicine residue, heavy metals, contaminants, and other substances which may be harmful to human health;
- types, scope of application and dosage of food additives;
- nutritional requirements of staple and supplementary food exclusively for infants and toddlers and other special groups of people;
- requirements for labels, identification and instructions relevant to food safety and nutrition;
- hygiene requirements for food production operations;
- quality requirements relating to food safety;
- methods and procedures for food inspection and testing; and
- other particulars proposed to be developed as food safety standards.

If there is any contravention of the Food Safety Law, which includes the use of non-edible substances or the use of chemical substances other than food additives in food production, the relevant authority will (i) forfeit all the income generated from the affected products by any person who contravenes the Food Safety Law and all equipment and raw materials used in the production of the affected products, and (ii) impose on such person a fine, which is equivalent to a sum not exceeding RMB50,000 if the prices of the affected products and food additives are less than RMB10,000 or a sum which is equivalent to five to 10 times of the prices of the affected products and food additives if the prices of the affected products and food additives are RMB10,000 or more.

The Regulations for the Implementation of the Food Safety Law of the PRC《中華人民共和國食品安全法實施條例》, effective on July 20, 2009, require food production operators to operate in accordance with relevant PRC laws, regulations and food safety standards, establish sound food safety management systems and adopt effective measures to ensure that food is safe, to be responsible for the safety of the food which they produce and trade, be responsible to the public, and assume social responsibility.

The Notice on the Issuance of the Recent Special Rectification Emphasis, Requirement and Focus on Nationwide Crackdown on Illegal Addition of Non-edible Substances and Misuse of Food Additives《關於印發〈全國打擊違法添加非食用物質和濫用食品添加劑專項整治近期工作重點及要求〉的通知》was promulgated by the Ministry of Health of the PRC and became effective on March 6, 2009. The notice prohibits the addition of non-edible substances in food additives, melamine and other non-edible substances in the production of food products such as dairy products.

Under the Regulations on the Supervision and Administration of the Quality and Safety of Dairy Products《乳品質量安全監督管理條例》, which were promulgated by the PRC State Council (國務院) on October 9, 2008 and became effective on October 9, 2008, dairy animal breeders, raw milk purchasers, dairy products production enterprises and sellers are considered the first responsible persons who should assume responsibility for the quality and safety of the dairy products which they produce, purchase, transport and sell. Fresh milk and dairy products must comply with the national safety standards governing the quality of dairy products, which are developed by the competent health department of the State Council and amended from time to time in accordance with the results of risk monitoring and risk assessments. The addition of non-edible chemical substances or other substances which may be harmful to human health during the production process of dairy products is prohibited. If any violation of these regulations results in violation of Criminal Law, any violator will be prosecuted and the issuing authority may revoke the food production license of such person. If any violation of these regulations does not constitute a crime, the relevant authority will forfeit the affected products, illegal gains and relevant tools and and impose a fine equal to a sum between 15 and 30 times of the prices of the affected products, on any violator and the issuing authority may revoke the food production license of such person.

The Notice of the General Administration of Quality Supervision, Inspection and Quarantine of the PRC ("AQSIQ") on the Enhancement of the Licensing of Dairy Product Production《國家質量監督檢驗檢疫總局關於加強乳製品生產許可工作的通知》was promulgated by the AQSIQ and became effective on November 12, 2008. Under the notice, the relevant Provincial Department of Administration of Quality Supervision, Inspection and Quarantine (省級質量技術監督局) ("Provincial AQSIQ") must ensure that dairy product enterprises have the relevant testing facilities and, where they are involved in the production of infant milk formula products, have the relevant personnel, to test the content of melamine in the raw materials they use and their products. Dairy product enterprises unable to meet the above requirements, they must appoint testing centers that are equipped with melamine testing facilities and certified by the relevant Provincial.

According to the Notice on the Further Enhancement of Quality and Safety Works on Dairy Products《關於進一步加強乳品質量安全工作的通知》promulgated by the General Office of the State Council (國務院辦公廳) on September 16, 2010, each province, city directly under the central government and autonomous region in the PRC, among others, must:

- strictly manage the dairy industry by enforcing the policies of the dairy product industry, including the completion of the inspection of the existing dairy product enterprises by the end of 2010. The relevant quality control departments must revoke the production permits of the relevant dairy product enterprises that fail to meet the industry standards;
- through the AQSIQ, complete the amendments of the regulations on the inspection of dairy product production permits before the end of October 2010. The provincial AQSIQ must carry out strict inspection on newly set up dairy product enterprises and must not issue production permits to such enterprises that fail to fulfil the relevant conditions;
- through the AQSIQ, carry out new inspections before the end of February 2011 on existing dairy product enterprises that have obtained production permits in accordance with the regulations, and order these enterprises that fail to meet the relevant requirements are obliged to rectify the non-compliance and stop production or sales activities;
- prohibit the issuance of permits for purchase of raw milk to parties other than dairy product enterprises, dairy farms, dairy farmer societies that have registered with the relevant departments of industrial commerce;
- through the local AQSIQ, enhance the inspection and carry out sample testings of not less than 15% of all batches of raw milk and milk powder products purchased by the food processing enterprises. Food processing enterprises must test the content of melamine in raw milk and milk powder products they purchase, and strictly enforce the system of presentation of licence and certificate;
- through the local AQSIQ, carry out a sampling test on the products of dairy product enterprises once every week. Dairy product enterprises must test the content of melamine in each batch of their outgoing products;
- expedite the implementation of a national information database on dairy production enterprises;

- refine further the overall inspection on the operations, management and purchase records of dairy product enterprises and enhance the retrieval of record. Food processing enterprises must, prior to their purchases, verify the relevant dairy product enterprises and business units, inspection reports, invoices and other information;
- order dairy product enterprises that fail to record or trace the products or identify the authenticity of products they purchase in accordance with the relevant regulations to cease business operations and revoke the permits;
- implement electronic information tracking system covering, among other things, sources of raw milk, procurement and production;
- complete the development of electronic information tracking system and put in place by the end of 2011 the standards and regulations relating to such tracking system as may be implemented in the dairy industry in respect infant milk formula and milk powder products;
- carry out a comprehensive inspection of infant milk formula product enterprises' hazard analysis and critical control point terminal system, and immediately order the closure of the enterprises that fail to meet the relevant requirements, the rectification of the non-compliance and if the enterprises fail to meet the relevant requirements after the rectification, revocation of the production permits, and publish such closure, rectification and revocation of permits in the main local media; and
- through the quality inspection department, publish and update the names and products of infant formula milk powder product enterprises online.

In accordance with the requirement by the Notice on the Further Enhancement of Quality and Safety Work on Dairy Product, on November 1, 2010 AQSIQ issued the Announcement on Promulgating the Rule of Inspection on Enterprises' Condition of Producing Infant Formula Power (2010 version) and the Rule of Inspection on Enterprises' Condition of Producing Dairy Product (2010 version), which provided the revised rules for inspecting conditions of producing infants formula power and dairy products. Furthermore, the Announcement stipulated that as of March 1, 2011 the existing dairy product enterprises which fail to obtain new production permit shall suspend producing dairy products and infant formula powder.

On a regular press conference as of February 24, 2011, AQSIQ announced that, according to the Notice on the Further Enhancement of Quality and Safety Work on Dairy Product, the re-inspection of production permit for dairy products shall be completed before the end of February; however, in order to endure the quality of re-inspection work the deadline has been rescheduled to the end of March, 2011.

Food Hygiene

According to the Food Safety Law of the PRC, food production operations must comply with the following hygiene requirements:

- appropriate space must be available for treating raw materials for food and for processing, packaging and storing food, based on the variety and quantity of food produced; such space must be kept tidy and clean; and appropriate distance must be maintained between such space and toxic or hazardous elements or other sources of contamination;
- appropriate equipment and facilities must be available for food production, disinfection, workplace dress changes, cleaning, lighting, illumination, ventilation, anti-corrosion, dust-proofing, fly-proofing, rat-proofing, insect-proofing, cleansing and treating waste water, rubbish and other waste storage;
- technical professionals and management personnel in the field of food safety and a regulated system to ensure food safety must be available;
- equipment and production lines must be arranged in a practical way to prevent cross-contamination between food that is pending processing and food that is ready-to-eat and between raw materials and finished products, and to avoid contact between food and toxic or unclean substances;
- tableware, drinking utensils and containers for ready-to-eat food must be cleaned and disinfected prior to use, and cooking utensils and other utensils must be washed after use and kept clean;

- containers, utensils and equipment used for storage, transportation, loading and unloading of food must be safe, harmless and kept clean to prevent food contamination and must conform to specifications such as maintaining temperature at the level required to ensure food safety; food must be transported separately from toxic and hazardous substances;
- ready-to-eat food must be kept in small packaging or use packaging materials and tableware which are non-toxic and clean;
- food production and operating staff must maintain good personal hygiene, wash their hands thoroughly and wear clean working clothes and headwear while producing and operating food; non-toxic and clean tools must be used while selling ready-to-eat food without packaging;
- water used must comply with the national hygiene standards for drinking water;
- detergents and disinfectants used must be safe and harmless for the human body; and
- other relevant PRC laws and regulations must be complied with.

Food Production License

In accordance with the Food Safety Law, China has implemented a licensing system on food production and operation. Food producers must obtain food production licenses. Furthermore, food producers who have obtained food production licenses and are selling the food they produce at their production premises are not required to obtain food circulation licenses.

The Regulations of the PRC on the Administration of Production Licenses for Industrial Products《中華人民共和國工業產品生產許可證管理條例》, which were promulgated by the State Council on July 9, 2005 and became effective on September 1, 2005, put in place a production licensing system for enterprises which produce processed food, such as dairy products, meat products, beverages, rice, noodles, cooking oil, wine, and other processed products which may directly affect human health. Under the Provisional Detailed Rules for Supervision and Administration of Quality and Safety in Food Production and Processing Enterprises 《食品生產加工企業質量安全監督管理實施細則(試行)》, which were issued by the AQSIQ and became effective on September 1, 2005, food production and processing enterprises must meet the required production conditions for food quality and safety and must obtain food production licenses. Produced or processed food is only allowed to be sold after passing inspections and obtaining market access labels on food quality and safety. The effective period for a food production license is three years. If enterprises wish to continue their operation after the expiry of the effective period, they must submit applications to the original quality and technical supervision departments six months before the effective period expires. Pursuant to the Regulations on Supervision and Inspection of Food Production and Processing Enterprises Bearing Primary Responsibility For Quality and Safety《食品生產加工企業落實質量安全主體責任監督檢查規定》, which were promulgated by the AQSIQ on December 23, 2009 and became effective on March 1, 2010, food production and processing enterprises must maintain the name on its food production license so that it is in line with its business license, and the actual food production site and food production scope must be consistent with the contents of the food production license. Furthermore, food production and processing enterprises must establish the following systems, including purchase inspection record system, manufacturing process control system, delivery inspection record system, sub-standard product management system, recall system for unsafe products, and consumer complaint accept system. Employee health, professional training and implementation of enterprise standards for food production and processing enterprises must comply with relevant PRC laws and regulations.

Food Standardization

Under the Standardisation Law of the PRC《中華人民共和國標準化法》, which became effective on April 1, 1989, and its implementing regulations《中華人民共和國標準化法實施條例》and the relevant interpretation provisions《中華人民共和國標準化法條文解釋》, which became effective on April 6, 1990 and July 23, 1990, respectively, standards relating to the protection of personal health and the safety of persons and property, as well as standards imposed by other laws and regulations, are classified as "mandatory standards." Food hygiene standards are part of the mandatory standards. According to the Notice of Issues Relating to the Implementation of the Three Compulsory National Standards, Including General Technical Requirements of Infant Formula Powder and Infant Supplementary Cereals Powder《關於實施<嬰幼兒配方粉及嬰幼兒補充穀粉通用技術條件>等三項強制性國家標準有關問題的通知》(國標委農輕聯[2004]63號), which was issued by the Standardisation Administration Commission of the PRC and the AQSIQ on June 29, 2004, production enterprises should strictly comply with the three compulsory national standards, namely GB10767-1997 General Technical Requirements of Pediatric Formula Powder and Pediatric Supplementary Cereals Powder《嬰幼兒配方粉及嬰幼兒補充穀粉通用技術條件》), GB 10765-1997 Infant Formula Milk Powder Ⅰ《嬰兒配方乳粉Ⅰ》and GB 10766-1997 Infant Formula Milk Powder II, Ⅲ《嬰兒配方乳粉II, Ⅲ》.

The National Food Safety Standards for "Raw Milk" (GB19301-2010) and 66 Other Items of Food (Wei Tong [2010] No. 7) (《生乳》(GB19301-2010) 等66項食品安全國家標準 (衛通[2010]7號)), promulgated by the Ministry of Health of the PRC on March 26, 2010, established national food safety standards for 66 food items. These include national standards with serial numbers GB19644-2010 milk powder (乳粉), which will become effective on December 1, 2010; GB10765-2010 infant formula (嬰兒配方食品), which will become effective on April 1, 2011, GB10767-2010 older infants and young children formula (較大嬰兒和幼兒配方食品), which will become effective on April 1, 2011, GB12693-2010 good manufacturing practice for milk products (乳製品良好生產規範), which will become effective on December 1, 2010 and GB23790-2010 good manufacturing practice for powdered formulae for infants and young children (粉狀嬰幼兒配方食品良好生產規範), which became effective on December 1, 2010.

In addition to adhering to these compulsory national standards, enterprises producing pediatric formula products may also adopt enterprise standards that are not below the corresponding technical requirements of the national standards. Enterprises are required to file such standards with the local standardization administrative department.

Food Inspection

In accordance with the Food Safety Law, China implemented an inspection system relating to food production and operations. Under this law, the State and local food safety supervision and administrative departments (食品安全監督管理部門) are required to carry out food inspection and may not exempt any food from inspection. The quality and technical supervision departments, industry and commerce administrative departments and food and drug supervision and administration departments at and above the county level are responsible for carrying out food inspections by conducting sample tests on a regular or irregular basis. An enterprise that engages in the production of food, or in business operations relating to the production of food, may itself inspect the food it produces, or the food may be inspected by the authorized food inspection agent, in order to ensure compliance with the requirements of the Food Safety Law.

Food Identification Administration System

Pursuant to the Provisions on the Administration of Food Identification《食品標識管理規定》, which were promulgated by the AQSIQ on August 27, 2007 and became effective on September 1, 2008, and subsequently amended by the AQSIQ on October 22, 2009, food identification labels must state the name of the food, the place and date of production, the expiry date of the food, the net content of the package, food size as required by relevant specific regulations (in the case of quantitative packaging food), the list of ingredients, the names, addresses and contact information of the producers and product standard codes implemented by the producers. Food identification labels on the primary and subsidiary food for infants or other specific groups must state the main nutritional components and their respective contents.

Food labels with wordings such as "nutrition" and "strengthen" in their names or descriptions are required to disclose the nutrition and calories of such food in accordance with the relevant national standards and comply with the content and composition standards required by under national standards. Food produced under the production licensing management arrangement is required to display its food production license number and quality safety (QS) mark on the food label.

Food Recall

The PRC has established a food recall system as required by the Food Safety Law. Pursuant to the Provisions on the Administration of Food Recall《食品召回管理規定》, which were issued by the AQSIQ and became effective on August 27, 2007, food recall is categorised into three grades based on the degree of severity of the food safety hazard. Food may be recalled either voluntarily or by order of the government.

1. Voluntary recall

In the case of a voluntary recall under the Provisions on the Administration of Food Recall:

- the food producer must immediately cease production and sale of the food identified as unsafe for human consumption;
- from the date on which the food has been identified as unsafe and must be recalled, the relevant sellers must be notified not to sell, and consumers must be notified not to consume, within one day for a grade one recall, within two days for a grade two recall, and within three days for a grade three recall;
- information distributed by food producers to the public relating to a food recall must be reported to the quality and technical supervision departments of the provincial-level government or above in accordance with relevant requirements;
- from the date on which the food has been identified as unsafe and must be recalled, the producer should submit its food recall plan to the quality and technical supervision departments of provincial-level through the quality and technical supervision departments of municipal-level governments where such producers are located and must do so within three days for a grade one recall, within five days for a grade two recall, and within seven days for a grade three recall; and
- from the date on which recall has been conducted, progress reports must be submitted to the quality and technical supervision departments of provincial-level governments through the quality and technical supervision departments of municipal-level governments where such producers are located and must do so once every three days for a grade one recall, once every seven days for a grade two recall and once every 15 days for a grade three recall.

2. Recall by order

If any of the following cases, the AQSIQ will order food producers to recall the relevant unsafe food and may publish relevant food safety information and consumption warnings or adopt other measures to avoid any further harm being caused to the public:

- food producers deliberately concealing the hazards of food safety, or food producers not taking recall action where a voluntary recall is appropriate;
- the harm has expanded or recurred due to the fault of food producers; and
- hidden problems relating to food safety which may be harmful to human health and life are discovered during a selective inspection conducted by the nation's supervisors.

Food producers are required to cease production and sale of the unsafe food immediately after receiving notice of a recall order.

Supervision on the use of food additives

Under the Food Safety Law, no food additive may be used in food unless it is deemed technically necessary and has been proven safe and reliable after undergoing risk assessments. The competent health department of the State Council (國務院衛生主管部門), on the basis of the technical necessity and the results of the food safety risk assessments, is responsible for revising the permitted varieties, scope of use and dosage standards of food additives in a timely manner. A food producer may only use food additives in accordance with the food safety standards, and may not, during the process of food production, use any chemical substances other than approved food additives or any other substances which may potentially cause harm to human health.

When purchasing raw materials for producing food, food additives and food-related products, a producer shall inspect the license and relevant product compliance certification document of the supplier. If a supplier is unable to provide a compliance certification document, the producers are required to carry out an inspection of the raw materials in accordance with the relevant food safety standards. No raw material for food, food additive or food-related products may be purchased or used unless it complies with the relevant food safety standards. A food production enterprise must establish an inspection record system for the purchase of raw materials for producing food, food additives and food-related products which records information such as their names, specifications and quantities, the names and contact information of the suppliers and the date of purchase. Such inspection record must be true and must be retained for at least two years.

The Measures for the Administration of New Varieties of Food Additives《食品添加劑新品種管理辦法》, which were promulgated and became effective on March 30, 2010 by the Ministry of Health of the PRC, stipulate that:

- food additives must not be used to conceal the decomposition or deterioration in food;
- food additives must not be used to conceal the quality deficiencies in food or those arising during the food production process;
- food additives must not be used for the purposes of creating counterfeit or fake products;
- food additives must not be used to reduce the nutritional value of food;
- the use of food additives must be kept to a minimal that can achieve the intended result; and
- food enterprises must remove processing substances or aids used in food production before the completion of the finished products save for the permitted residue quantities.

Marketing of breast milk substitute products

Pursuant to the Measures for the Administration of the Marketing of Breast Milk Substitute Products《母乳代用品銷售管理辦法》, which were jointly promulgated by the Ministry of Health, the Ministry of Internal Trade, the Ministry of Radio, Film & Television, the State Press and Publication Administration and the China National Council of Light Industry of the PRC as well as the State Administration for Industry and Commerce of the PRC (中華人民共和國國家工商行政管理總局) ("SAIC") on June 13, 1995 and became effective on October 1, 1995, packaging labels of breast milk substitute products shall prominently be marked with a statement about the advantages of breastfeeding. Furthermore, no pictures of infants or terms such as "breast milk" shall be printed on the packaging labels of these products. Producers and distributors of breast milk substitute products are also prohibited from, among other things, giving breast milk substitute products or samples of these products as gifts to medical and healthcare bodies, pregnant women, families with infants as part of the promotion of these products. For the purposes of the Measures for the Administration of the Marketing of Breast Milk Substitute Products, breast milk substitute products refer to, among other things, infant formula products which are manufactured in accordance with applicable PRC laws on food standards that meet normal nutritional requirements and suit the physiological characteristics of infants between four and six months of age and other dairy products for infants which are designed as substitutes for breast milk.

Provincial Regulations

The Regulations Applicable to the Dairy Industry in Heilongjiang《黑龍江省奶業條例》, which were promulgated by the Standing Committee of the People's Congress of Heilongjiang on October 15, 2004, set out the detailed standards for the sale and purchase of raw milk, and for the processing and safety of raw milk and dairy products, in Heilongjiang.

Laws on Products Quality

Products that we manufacture are subject to the laws, rules and regulations in relation to the product quality in the PRC. The Product Quality Law of the PRC《中華人民共和國產品質量法》("Product Quality Law"), promulgated on February 22, 1993, which became effective on September 1, 1993 and subsequently amended on July 8, 2000, is the principal law governing the supervision and administration of product quality, and is applicable to the production and sale of any products in the PRC.

According to the Product Quality Law, manufacturers are liable for the quality of products they produce and sellers must take reasonable actions to ensure the quality of the products they sell. The seller is responsible for the repair, exchange or refund of the products if the product displays any of the following defects; in the event consumers suffered losses as a result of the defective products, the seller shall also make compensation:

- the product sold does not have the attribute or function that it should have, and there was no advance explanation or statement made to that effect;
- the product sold does not comply with the adopted standards indicated on the product or its package; or
- the product sold does not comply with similar product quality as indicated by means of product instruction or sample.

The manufacturer will be liable for any bodily harm or damage to property (other than the defective product itself) caused by the defective products of the manufacturer unless the manufacturer is able to prove that:

- it has not circulated the product;
- the defect did not exist at the time when the product was circulated; or
- the state of scientific or technological knowledge at the time when the product was circulated was not such that it allowed the defect to be discovered.

The seller will be liable for any bodily harm or damage to property (other than the defective product itself) caused by the defective products sold if such defect is caused by the seller.

A person who is harmed or whose property is damaged by the defective product may claim such loss against the manufacturer or the seller.

Laws on Product Liabilities

Pursuant to the General Principles of the Civil Law of the PRC《中華人民共和國民法通則》 promulgated by the National People's Congress on April 12, 1986 and the Law of the PRC on the Protection of Consumers' Rights and Interests《中華人民共和國消費者權益保護法》promulgated by the Standing Committee of the National People's Congress on October 31, 1993, which became effective on January 1, 1987 and January 1, 1994, respectively, both manufacturers and distributors will be held jointly liable for losses and damage suffered by consumers caused by the defective products they manufacture and distribute.

Laws and Regulations Relating to Health Care Food

Pursuant to Administrative Rules on Registration of Health Care Food《保健食品註冊管理辦法》 Promulgated by State Food and Drug Administration (國家食品藥品監督管理局) on April 30, 2005，any individual or entity who intends to produce health care food within the PRC shall register relevant health care food with food and drug administration authority and obtain the Approval Certificate for Heath Care Food (保健食品批准證書) ; when applying for registration, the applicant shall provide to relevant authority the sample of health care food which shall be produced in accordance with Good Manufacturing Practice for Heath Care Food (GB17405-1998) 《保健食品良好生產規範 (GB17405-1998)》;

In 1998 the Ministry of Health issued Good Manufacturing Practice for Heath Care Food which provided a set of basic technical standards applying to health care food production enterprises' staff, design, equipment, raw material, production, storage and transportation of finished products and management of quality and hygiene

Laws and Regulations Relating to Labor Matters

The PRC Labor Contract Law《中華人民共和國勞動合同法》, which became effective on January 1, 2008, imposes certain requirements in respect of human resources management, including, among other things, signing labor contracts with employees, terminating labor contracts, paying remuneration and compensation and making social insurance contributions. In addition, the PRC Labor Contract Law requires employers to provide remuneration packages which are not lower than the relevant local minimum standards.

The PRC Employment Promotion Law《中華人民共和國就業促進法》, which became effective on January 1, 2008, requires that individuals have equal employment opportunities, both in hiring and in employment terms, without discrimination on the basis of ethnicity, race, gender, religious belief, communicable disease or rural residence. Under this law, enterprises are also required to provide employees with vocational training. Administrative authorities at the county level or above are responsible for implementing policies to promote employment.

The Regulation on Work-Related Injury Insurance《工傷保險條例》, which became effective on January 1, 2004, requires employers to pay work-related injury insurance fees for their employees. Under the Interim Measures Concerning the Maternity Insurance of Enterprises Employees《企業職工生育保險試行辦法》, which became effective on January 1, 1995, employers must pay maternity insurance fees for their employees.

Under the Interim Regulations Concerning the Levy of Social Insurance Fees《社會保險費征繳暫行條例》, which became effective on January 22, 1999 and the Interim Measures Concerning the Administration of the Registration of Social Insurance《社會保險登記管理暫行辦法》, which were adopted on March 19, 1999, employers in the PRC must apply for social insurance registration with the local social insurance authorities and make contributions to the basic pension insurance fund, basic medical insurance fund and unemployment insurance fund for their employees. According to the Regulation on Management of the Housing Fund《住房公積金管理條例》, which became effective on April 3, 1999 and amended on March 24, 2002, enterprises in the PRC must register with the housing fund management center and then maintain housing fund accounts with designated banks for their employees and contribute to the fund an amount not less than 5% of the employee's average monthly salary in the previous year.

Laws and Regulations Relating to Production Safety

The PRC Production Safety Law《中華人民共和國安全生產法》("Production Safety Law"), which became effective on November 1, 2002, is the principal law governing the supervision and administration of production safety in the PRC. This law requires production entities to meet the relevant legal requirements, such as providing its staff with training and a handbook on production safety and providing safe working conditions in compliance with relevant laws, rules and regulations. Any production entities unable to provide the required safe working conditions may not engage in production activities.

Violation of the Production Safety Law may result in the imposition of fines and penalties, the suspension of operations, an order to cease operations, or even criminal liability in severe cases.

Laws and Regulations Relating to Environmental Protection

Our Group is subject to environmental protection laws, rules and regulations in the PRC.

The Environmental Protection Law of the PRC《中華人民共和國環境保護法》, which became effective on December 26, 1989, authorized the state environmental protection authority to formulate national environmental quality and discharge standards and monitor the environmental system at the national level.

The Law of the PRC on the Prevention and Control of Environmental Noise Pollution《中華人民共和國環境噪聲污染防治法》, which became effective on March 1, 1997, stipulates the supervision and management measures in respect of the prevention and control of environmental noise pollution including industrial noise pollution, as well as noise pollution from construction, transportation and social activities. The law also specifies the relevant legal liabilities.

Other major environmental regulations applicable to our Group include the Law of the PRC on the Prevention and Control of Water Pollution《中華人民共和國水污染防治法》together with the related implementation rules, the Law of the PRC on the Prevention and Control of Air Pollution《中華人民共和國大氣污染防治法》, the Law of the PRC on the Prevention and Control of Solid Waste Pollution《中華人民共和國固體廢物污染環境防治法》, the Regulation regarding the Administration of Construction Project Environmental Protection《建設項目環境保護管理條例》, and the Law of the PRC on Environmental Impact Assessment《中華人民共和國環境影響評價法》.

On May 8, 2001 the State Environmental Protection Administration promulgated the Administrative Rules on Pollution Prevention in Breeding Livestock and Poultry《畜禽養殖污染防治管理辦法》, pursuant to which, among other things, (1) newly built, rebuilt and extendedly built livestock and poultry farms shall go through environmental impact assessment and relevant approval procedures; (2) when conducting completion acceptance procedures in respect of pollution prevention equipment of the farm, the environmental protection authority shall examine implementing results of comprehensive utilization of waste manure generated from livestock and poultry; (3) livestock and poultry farms shall not be built in the following areas: (i) protection zones of drinking water source, landscape and famous scenery and the core areas and buffering areas of nature reserves; (ii) residential areas, areas for education, culture and scientific research, medical space and other population-concentrated areas; (iii) areas not for breeding animal stipulated by local governments at county level; and (iv) other areas needed to be specially protected by national or local laws and regulations; and (4) in the areas where the gross amount of pollution discharge is restricted by laws, livestock and poultry farms shall obtain Pollution Discharge Permit and its pollution discharge shall be in compliance with such Permit.

Violation of these laws, rules or regulations may result in the imposition of fines and penalties, the suspension of operations, an order to cease operations, or even criminal liability in severe cases.

Laws and Regulations Relating to Dividend Distribution

The principal regulations governing the distribution of dividends by WFOEs:

- the Corporation Law of the PRC of 2005《中華人民共和國公司法》(2005);
- the Wholly Foreign-Owned Enterprise Law of the PRC of 2000《中華人民共和國外資企業法》(2000); and
- the Wholly Foreign-Owned Enterprise Law Implementation Rules of the PRC of 2001,《中華人民共和國外資企業法實施細則》(2001).

Under the current regulatory regime in China, WFOEs in China may pay dividends only out of their accumulated profit, if any, determined in accordance with PRC accounting standards and regulations. After making up for any deficit in prior years pursuant to the PRC laws, a WFOE in China is required to set aside each year as general reserves at least 10% of its after-tax profit, determined in accordance with PRC accounting standards and regulations, until the cumulative amount of such reserves reaches 50% of its registered capital. These reserves are not distributable as dividends. Each year the foreign-invested enterprises shall draw from after-tax profit staff bonus and welfare fund, the portion of which may be at such enterprises' discretion. WFOEs that are in deficit or liquidation may not distribute dividends.

Laws and Regulations Relating to Taxation

Because we are not incorporated in mainland China, your investment in our Notes is expected to be largely exempt from PRC tax laws, except as disclosed in the section entitled "Risk Factors — Risks Relating to Our Business — We may be deemed to be a PRC tax resident under the PRC Enterprise Income Tax Law《中華人民共和國企業所得稅法》issued on March 16, 2007 which took effect on January 1, 2008 ("EIT Law") and this may subject us to PRC taxation on our worldwide income, require us to withhold taxes on interest we pay on the Notes and require holders of the Notes to pay taxes on gains realized from the sale of the Notes." But because virtually all of our business operations are in mainland China and we carry out these business operations through operating subsidiaries organized under the PRC law, our PRC operations and our operating subsidiaries in mainland China are subject to PRC tax laws and regulations, which indirectly affect your investment in the Notes.

Dividends from our PRC operations

Under the PRC taxation laws effective prior to January 1, 2008, dividends paid by our PRC subsidiaries or joint ventures to us were exempt from PRC income tax. However, pursuant to the EIT Law and EIT Rules that became effective on January 1, 2008, dividends payable by foreign invested enterprises, such as subsidiaries and joint ventures in China, to their foreign investors are subject to a withholding tax at a rate of 10% unless any lower treaty rate is applicable. Under these laws and rules, enterprises established under the laws of foreign jurisdictions but whose "de facto management body" is located in China are treated as "resident enterprises" for PRC tax purposes, and will be subject to PRC income tax on their worldwide income.

For such PRC tax purposes, dividends from PRC subsidiaries to their foreign shareholders are excluded from such taxable worldwide income. Under the EIT Rules, "de facto management bodies'' is defined as the bodies that have material and overall management control over the business, personnel, accounts and properties of an enterprise. Substantially all of our management is currently based in China and may remain in China. Therefore, we may be treated as a PRC resident enterprise for EIT purposes.

If we are deemed to be a PRC resident enterprise, we would be subject to the PRC enterprise income tax at the rate of 25% on our worldwide income. Furthermore, we might be obliged to withhold PRC income tax generally at a rate of 10% on payments of interest and other amounts on the Notes to investors that are non-resident enterprises, because the interest and other amounts might be regarded as being derived from sources within China. In addition, any gain realized by such investors that is non-resident enterprise from the transfer of the Notes might be regarded as being derived from sources within China and accordingly might be subject to a 10% PRC tax.

Taxation of our PRC operations

Our subsidiaries through which we conduct our business operations in China are subject to PRC tax laws and regulations.

The key taxes applicable to companies in the PRC are EIT and value added tax. The EIT Law of the PRC which became effective on January 1, 2008, impose a uniform enterprise income tax rate of 25% on both domestic and foreign-invested enterprises. A resident enterprise is subject to enterprise income tax on the income derived both inside and outside the territory of the PRC. If an organization or presence is set up in the PRC by a non-resident enterprise, it will be subject to enterprise income tax on the income derived from such organization or presence in the PRC and the income derived from outside the PRC but with actual connection with such organization or presence in the PRC. For a non-resident enterprise which has not set up an organization or presence in the PRC, or has set up an organization or presence but the income derived has no actual connection with such organization or presence, its income derived in the PRC will be subject to enterprise income tax.

The EIT shall be levied at the rate of 25%. A non-resident enterprise without a permanent establishment in the PRC or such non-resident enterprise which has set up a permanent establishment in PRC but its earning income is not connected with the abovementioned permanent establishment will be subject to tax on their PRC-sourced income. The income shall be taxed at the reduced rate of 10%.

Pursuant to the Provisional Regulations of the PRC on Value-Added Tax 《中華人民共和國增值稅暫行條例》, which was promulgated on December 13, 1993 and amended on November 5, 2008, and its implementation regulations, which were promulgated on December 15, 2008, all of which became effective on January 1, 2009, unless stated otherwise, the tax rate for value-added tax payers who are selling or importing goods, and providing processing, repairs and replacement services in the PRC shall be 17%.

Laws and Regulations Relating to Foreign Exchange Control

Under the PRC Foreign Currency Administration Rules《中華人民共和國外匯管理條例》 promulgated in 1996 and revised in 1997 and as amended in 2008 and various regulations issued by SAFE and other relevant PRC government authorities, Renminbi is convertible into other currencies for the purpose of current account items, such as trade related receipts and payments and the payment interest and dividend. The conversion of Renminbi into other currencies and remittance of the converted foreign currency outside China for the purpose of capital account items, such as direct equity investments, loans and repatriation of investment, requires the prior approval from SAFE or its local office. Payments for transactions that take place within China must be made in Renminbi. Unless otherwise approved, PRC companies may repatriate foreign currency payments received from abroad or retain the same abroad. Foreign-invested enterprises may retain foreign exchange in accounts with designated foreign exchange banks subject to a cap set by SAFE or its local office. Foreign exchange proceeds under the current accounts may be either retained or sold to a financial institution engaging in settlement and sale of foreign exchange pursuant to relevant rules and regulations of the State. For foreign exchange proceeds under the capital accounts, approval from SAFE is required for its retention or sale to a financial institution engaging in settlement and sale of foreign exchange, except where such approval is not required under the rules and regulations of the State.

On October 21, 2005, SAFE issued the Notice on Issues Relating to the Administration of Foreign Exchange in Fund-raising and Reverse Investment Activities of Domestic Residents Conducted via Offshore Special Purpose Companies《國家外匯管理局關於境內居民通過境外特殊目的公司融資及返程投資外匯管理有關問題的通知》, which became effective November 1, 2005. The notice requires PRC residents to register with the local SAFE branch in the following circumstances: (i) before establishing or controlling any company (referred to in the notice as a "special purpose vehicles") outside the PRC for the purpose of capital financing; (ii) after contributing their assets or shares of a domestic enterprise into overseas special purpose vehicles, or raising funds overseas after such contributions; and (iii) after any major change in the share capital of the special purpose vehicles without any round-trip investment being made. Under these rules, failure to comply with the foreign exchange registration procedures may result in restrictions being imposed on the foreign exchange activities of the violator, including restrictions on the payment of dividends and other distributions to its offshore parent company, and may also subject the violators to penalties under the PRC foreign exchange administration regulations.

On August 29, 2008, SAFE promulgated Notice 142 which regulates the conversion by a foreign-funded enterprise of foreign currency into Renminbi by restricting how the converted Renminbi may be used. Notice 142 requires that the Renminbi funds converted from the foreign currency capital of a foreign-funded enterprise may only be used for purposes within the business scope approved by the applicable governmental authority and may not be used for equity investments within the PRC unless specifically provided for otherwise. In addition, SAFE strengthened its supervision over the flow and use of the Renminbi funds converted from the foreign currency capital of a foreign-funded enterprise. The use of such Renminbi capital may not be changed without SAFE's approval, and may not, in any case, be used to repay or prepay Renminbi loans if such loans are outstanding. Violations of Notice 142 will result in severe penalties, such as heavy fines as set out in the relevant foreign exchange control regulations.

Laws and Regulations Relating to Overseas Listing

In August 2006, MOFCOM, the State Assets Supervision and Administration Commission, the State Administration of Taxation, the State Administration of Industry and Commerce, the China Securities Regulatory Commission ("CSRC") and SAFE jointly adopted the M&A Provisions, which was revised in June, 2009. The M&A Provisions requires, among other things, that offshore special purpose vehicles, formed for overseas listing purposes through acquisitions of PRC domestic companies controlled by PRC companies or individuals, obtain the approval of the CSRC prior to publicly listing their securities on an overseas stock exchange. In September 2006, CSRC published a notice on its official website specifying documents and materials required to be submitted to it by special purpose vehicles seeking CSRC approval of their overseas listings.

RELATED PARTY TRANSACTIONS

The following discussion describes certain related party transactions between our consolidated subsidiaries and our directors, executive officers and substantial shareholders and, in each case, the companies with whom they are affiliated. Each of our related party transactions was entered into in the ordinary course of business, on fair and reasonable commercial terms, in our interests and the interests of our shareholders.

As a listed company on the Hong Kong Stock Exchange, we are subject to the requirements of Chapter 14A of the Listing Rules which require certain "connected transactions" with "connected persons" be approved by a company's independent shareholders. Unless otherwise disclosed, each of our related party transactions disclosed hereunder that constitutes a connected transaction within the meaning of the Listing Rules requiring shareholder approval has been discontinued prior to the IPO or is otherwise exempted from compliance under Chapter 14A of the Listing Rules.

The following table sets forth certain transactions between our Group and our related parties for the periods indicated:

	Year ended December 31,		
	2008	**2009**	**2010**
	RMB (in thousands)	**RMB (in thousands)**	**RMB (in thousands)**
Sales of raw materials to:			
— Jintianran Dairy	—	17,001	—
Sales of scrap materials to:			
— Daqing Baixinyuan	—	251	—
Loans granted to:			
— Changqing Dairy [(1)]	150,000	52,489	—
Interest charged to:			
— Changqing Dairy [(1)]	1,531	8,088	—
Purchase property, plant and equipment from:			
— Dazheng Building	66,106	10,358	—
Purchase of trademark from:			
— Dazheng Real Estate	—	200	—
Trademark fees charge by:			
— Dazheng Real Estate	1,858	—	—
Purchase of whole milk powder from:			
— Jintianran Dairy	—	33,380	—
Interest-free advance granted by:			
— Daqing Wanlong	—	—	50,000
License fee paid to:			
— Global Dairy Canada [(2)]	—	—	—

(1) The amounts represent the loans granted to and the related interest charged to Changqing Dairy prior to our acquisition of Changqing Dairy.

(2) During the year ended December 31, 2010, the Group paid license fee of HK$1.00 to Global Dairy Canada in respect of the right to use the name of Global Dairy Canada.

The following table sets forth certain transactions between the Daqing Dairy Group and our related parties for the periods indicated:

	Year ended December 31,		
	2008	**2009**	**2010**
	RMB'000	**RMB'000**	**RMB'000**
Sales of raw materials to:			
— Jintianran Dairy	—	17,001	—
Sales of scrap materials to:			
— Daqing Baixinyuan	—	251	—
Loans granted to:			
— Changqing Dairy [(1)]	150,000	52,489	—
Interest charged to:			
— Changqing Dairy [(1)]	1,531	8,088	—
Purchase property, plant and equipment from:			
— Dazheng Building	66,106	10,358	—
Purchase of trademark from:			
— Dazheng Real Estate	—	200	—
Trademark fees charge by:			
— Dazheng Real Estate	5,926	—	—
Purchase of whole milk powder from:			
— Jintianran Dairy	—	33,380	—
Interest-free advance granted by:			
— Daqing Wanlong	—	—	50,000

(1) The amounts represent the loans granted to and the related interest charged to Changqing Dairy prior to our acquisition of Changqing Dairy.

DESCRIPTION OF MATERIAL INDEBTEDNESS AND OTHER OBLIGATIONS

At the close of business on December 31, 2010, the Group had outstanding indebtedness of approximately RMB100.0 million, consisting of all long-term bank borrowings. Except as aforesaid or as otherwise disclosed herein, and apart from intra-group liabilities, the Group did not have any outstanding loan capital issued and outstanding or agreed to be issued, bank overdrafts, loans or other similar indebtedness, liabilities under acceptances or acceptable credits, debentures, mortgages, charges, hire purchases commitments, guarantees or other material contingent liabilities at the close of business on December 31, 2010.

The Daqing Dairy Group's and our borrowings, including bank borrowings and other loans are set forth below for the periods presented:

	The Daqing Dairy Group		The Group			
	Year ended December 31,					
	2008	2009	2008	2009	2010	2010
	RMB	RMB	RMB	RMB	RMB	US$
	(in thousands)					
Borrowings due within one year						
Bank borrowings						
- Secured	30,000	30,000	30,000	30,000	—	—
- Unsecured	30,000	170,000	30,000	170,000	—	—
Borrowings from Pre-IPO Investors	—	—	—	102,275	—	—
	60,000	200,000	60,000	302,275	—	—
Borrowings due over one year						
Bank borrowings						
- Unsecured	—	—	—	—	100,000	15,152
Total borrowings	60,000	200,000	60,000	302,275	100,000	15,152

The Daqing Dairy Group's borrowings

The Daqing Dairy Group had bank financing of RMB200.0 million as of December 31, 2009, consisting of three separate loans of RMB100.0 million, RMB30.0 million and an aggregate of RMB30.0 million raised by Daqing Dairy and RMB40.0 million raised by Changqing Dairy. The Daqing Dairy Group's RMB100.0 million loan, which has been repaid, charged an interest rate of 5.310% and had a one year term that matured in January 2010 and was secured on certain property of a related party as well as certain land use rights and properties of a third party, which were released upon repayment. Each of the second and third loan generally had a one year term and charged an interest rate of 5.310% per annum. The second loan, which matured in October 2010 and was secured on certain land use rights and properties of Changqing production facility, was repaid in June 2010 and the security was released upon such repayment. The third loan, which matured in April and May 2010, and was secured by the Guarantor listed in the table below as part of its business in return for fees, was repaid in April and May 2010 and the third party guarantee was released upon such repayment. The Daqing Dairy Group has obtained and drawndown a new loan of RMB30.0 million from the bank in June 2010 upon our repayment of the second loan and another new loan of RMB30.0 million from the bank in May 2010 upon repayment of the third loan, which are secured by guarantees provided by the Guarantor. Each of these two new loans charges an interest rate of 0.4425% per month and has a repayment term of 36 months from June 2010 and May 2010, respectively. The loan of

RMB40.0 million raised by Changqing Dairy has term of one year and matures in August 2010 and charges interest at 6.903% per annum. The loan was secured by a guarantee from a related party. This loan was repaid in May 2010 and the guarantee from the related party was released accordingly. Upon repayment of the loan, Changqing Dairy has obtained and drawndown a new loan of RMB40.0 million from the bank in May 2010, which is secured by a guarantee provided by the Guarantor. The new loan charges an interest rate of 0.4425% per month and has a repayment term of 36 months from May 2010. As a result of the above loan repayments and the drawdown of the new loans, we had RMB100.0 million of bank borrowings as of December 31, 2010. We believe that these loans will be repaid through additional loans or through our working capital. See "Related Party Transactions" and "Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources."

The Daqing Dairy Group raised three separate bank loans in 2008 from our principal bank in Daqing, amounting to RMB70.0 million in aggregate. The first loan of RMB 30.0 million had term of one year and was repaid in 2009. This loan was secured by a guarantee provided by the Guarantor and charged an interest rate of 7.470% per annum. The second loan of RMB10.0 million was an unsecured two month term loan, drawn on September 28, 2008 and repaid on November 6, 2008 and charged an interest rate of 6.210% per annum. The third loan of RMB30.0 million had a term of one year and was repaid in 2009. This loan was secured on certain land use rights and properties of our Daqing Plant. The Daqing Dairy Group was also granted an interest free, unsecured advance of RMB30.0 million from a third party in December 2008, which we repaid in 2009.

For further information regarding the above borrowings, see "Related Party Transactions."

The Group's borrowings

As at December 31, 2008, there was an advance from a third party amounting to RMB30.0 million which was repaid in 2009. The Pre-IPO Investors granted the Company a three-month term loan for S$21.0 million (approximately RMB102.3 million) (the "First Pre-IPO Loan") that matured in February 2010. This was repaid in February 2010 by the Group through an assumption of debt agreement with Zhao Yu and Kenmoore. Subsequent to the repayment of the First Pre-IPO Loan, the Pre-IPO Investors extended a 18-month term loan to the Company amounting to S$15.75 million (approximately RMB76.51 million) on March 1, 2010. We have repaid this second loan from the Pre-IPO Investors with part of the proceeds from our IPO on November 1, 2010.

As at December 31, 2010, we had unutilized banking facilities of approximately RMB200.0 million.

As at December 31, 2010, our Group had outstanding indebtedness of approximately RMB100.0 million, comprising long-term bank borrowings of RMB100.0 million. The tables below set forth the details of the RMB100.0 million borrowings:

Daqing Dairy

No.	Date of Contract	Contract Reference No	Lender	Loan Amount (RMB) (in thousands)	Interest Rate (per month)	Loan Period	Guarantor
1.	May 25, 2010	[2010] Long Kai Jie Zhi No. 007	Longjiang Bank (Daqing branch)*	30,000	0.4425%	From May 25, 2010 to May 24, 2013	Daqing Commercial and Industry Co. Ltd (limited by guarantee)*
2.	June 10, 2010	[2010] Long Kai Jie Zhi No. 010	Longjiang Bank (Daqing branch)*	30,000	0.4425%	From June 10, 2010 to June 9, 2013	Daqing Commercial and Industry Co. Ltd (limited by guarantee)*

Changqing Dairy

No.	Date of Contract	Contract Reference No	Lender	Loan Amount (RMB)	Interest Rate	Loan Period	Guarantor
1.	May 25, 2010	[2010] Long Kai Jie Zhi No. 008	Longjiang Bank (Daqing branch)*	40,000	0.4425%	From May 25, 2010 to May 24, 2013	Daqing Commercial and Industry Co. Ltd (limited by guarantee)*