蒙牛

China Mengniu Dairy Company Limited

中國蒙牛乳業有限公司*

(incorporated in the Cayman Islands with limited liability)

(於開曼群島註冊成立之有限公司)

Stock Code 股份代號 : 2319

誠心打造

誠信

2008

Annual Report 年報

* For identification purpose only
僅供識別

Corporate Profile

China Mengniu Dairy Company Limited (Stock Code: 2319) and its subsidiaries (the “Group”) manufacture and distribute dairy products in China, including Hong Kong and Macau. It is one of the leading dairy product manufacturers in China, with ***MENGNIU*** as its core brand. The Group’s diverse products include liquid milk products, such as UHT milk, milk beverages and yogurt, ice cream and other dairy products such as milk powder. In December 2008, the Group’s annual production capacity reached 5.57 million tons.

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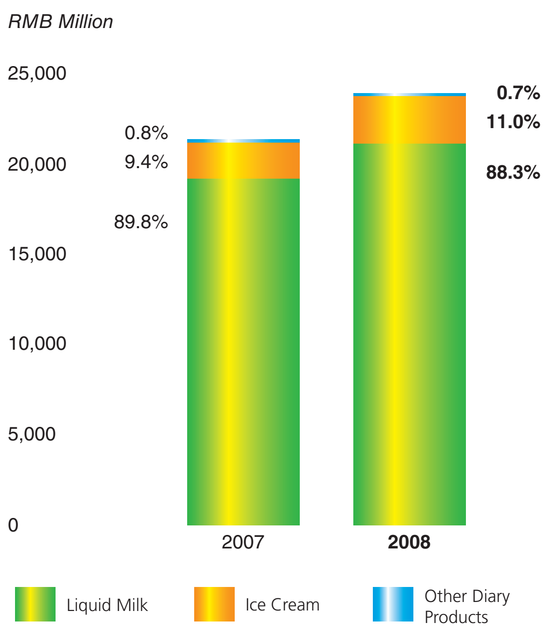
Financial Highlights

For the year ended 31 December	**2008** *RMB'000*	2007 *RMB'000*
Revenue	**23,864,975**	21,318,062
Net profit/(loss) attributable to equity holders of the Company	**(948,600)**	935,786
Net cash inflow from operating activities	**586,880**	2,058,121
Net cash balances	**1,313,305**	1,947,662
Basic earnings/(loss) per share *(RMB)*	**(0.639)**	0.664

- Leveraging on its market leading position and diversified product portfolio, the Group managed to achieve an 11.9% growth in revenue to RMB23,865 million during the year. However, affected by the Milk Incident in the second half of the year, the Group reported net loss attributable to equity holders of RMB948.6 million.
- The Group further expanded its production capacity and its aggregate annual production capacity reached 5.57 million tons in December 2008.
- According to China Industrial Information Issuing Center, National Bureau of Statistics of China and China General Chamber of Commerce, the Group ranked first in China in terms of overall sales volume. It also ranked first, in terms of sales volume, in the sectors of liquid milk and ice cream in China dairy industry in 2008.

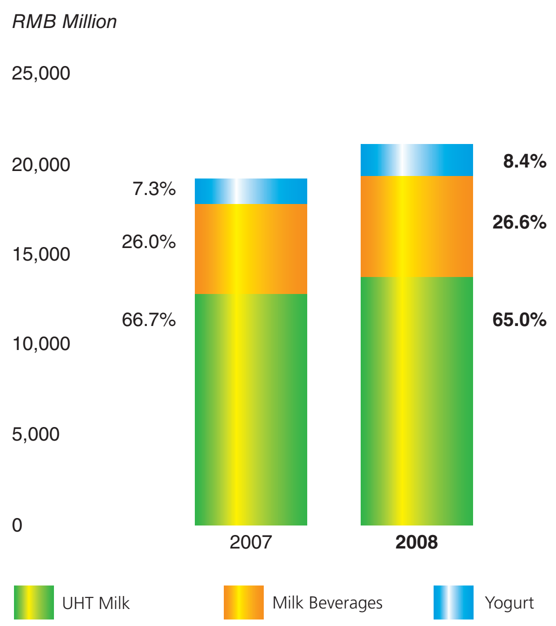
Revenue by Product Mix

For the year ended 31 December



Product Mix in Liquid Milk Segment

For the year ended 31 December



Plant Map

UHT milk and milk beverages

Yogurt

Ice cream

Other dairy products

The Journey of a Milk Droplet

Hi everybody! I am a drop of milk. Please come and join my journey to become the delicious milk from Mengniu.

Internationalized Ranch

Milk cattle

I am a pedigree Herstan cattle native from New Zealand and Australia, and my milk is rich with protein.

Feed

Feed for the milk cattle is carefully prepared by husbandry experts with high-quality grasses from 12 countries to help increase protein level in the milk. Nutritional balance and great taste.

Stables

The milk cattle live in deluxe residences, which are not only cozy and spacious, but can also keep them warm in winter and cool in summer.

Exercise field

A leisure stroll after having a meal can certainly benefit the health of the cattle.

Raw Milk Collection

After a great meal and a good sleep, the cattle are ready to work!

Automatic fishbone-style milking machine

The cattle are milked all by machine and the automatic process helps to prevent bacterial contamination.

Queuing up to "work"

Led by the head of the herd, the cattle fall into line to go "milking work".

Rolling milking machine

As the cattle enjoy soothing light music, my company and I slide smoothly into the milking machine.

Fresh and still warm, I am immediately conveyed into the specialized milk transportation vehicle.

Vehicle for transporting milk

GPS tracks every step of my journey round the clock.

Physicochemical laboratory for raw milk

Here is where I have my first check up for about two dozens items such as ethanol, dextrin, protein hydrolysate and melamine testing.

The Journey of a Milk Droplet

Production Procedures

Confirmed "healthy" after the check up, I move on into the automated production plant.

Milk storage bottle

Don't you feel strange as I am totally disappeared in the production plant? It is because the production process is completely closed and I am moving along in the ducts and into storage tanks, protecting me from contamination.

Flash evaporation machine

This machine helps getting rid of 5% of the water in my body to give me a richer taste.

Automated driverless cart

Antomated driverless cart transports straws and packing materials to ensure them away from contamination in all steps in the production process.

Robotic arm

I am in my temporary new home – the packing box. The robot helps to stack the boxes up in order.

Automated warehouse

With the help of the intelligent warehousing system, I am transported to the warehouse for storage and, like all the dairy products, will leave the warehouse for the market according to our production dates.

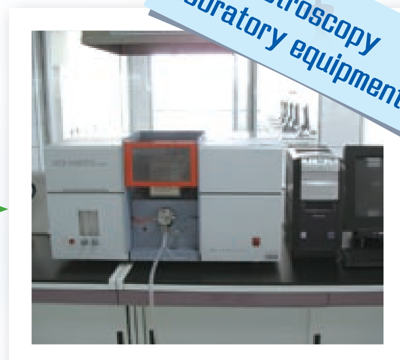
Quality Control Center

General laboratories

Apart from checking the items required by the national standards for dairy product safety, Mengniu also performs additional tests on ten plus hazardous materials including pesticide residues, additives and heavy metals, etc.

Biological engineering laboratory equipment

Spectroscopy laboratory equipment



Chromatography laboratory equipment

Microbiology laboratory equipment

Quality control does not stop here. After I am certified safe to consume, I am subjected to independent third party review conducted by the Chinese Academy of Inspection and Quarantine on regular basis.

CEO's Statement

REBUILD **CUSTOMER CONFIDENCE**
WITH **SINCERITY**

STRENGTHEN OUR **BRAND**
BY ENHANCED **PRODUCT QUALITY**

NIU Gensheng
Chief Executive Officer

I present the annual results of China Mengniu Dairy Company Limited (the "Company") and its subsidiaries ("Mengniu" or the "Group") for the year ended 31 December 2008 to our shareholders.

The China dairy industry had a tough and difficult time in 2008. In the past few years, the industry boomed and achieved rapid growth until September 2008. The milk contamination incident ("the Milk Incident") revealed that the development of operation practice such as raw materials procurement and transportation lagged behind the industry development. The incident also aroused the China dairy industry concerns over product safety. Having involved in the dairy business over decades, I witnessed the progressive growth and development of the industry, and I am deeply sorry for the hard hit suffered by the industry, and damage to public health and consumer confidence caused by the incident.

Under the initiatives of the State to rejuvenate the dairy industry, industry players swiftly responded and implemented a series of measures to strengthen product quality control to protect consumers' health and safety and to restore public confidence in the industry. It is the principle of the Company to "accept more responsibility as a big brand". The Group promptly responded to the government and promised to recall the relevant products. It also installed additional inspection equipment and included additional new testing items for products without delay. "Undertaking for Quality Raw Milk" (「原奶品質承諾書」) were obtained from raw milk collection centres to ensure the provision of safe milk.

The Group had learnt lessons from the incident and accordingly adopted approach from two perspectives to remove any potential safety hazard in the sourcing process. It continued to cooperate with business partners to increase the scale and number of large-scaled dairy farms, so as to quickly increase the proportion of milk products made from high quality raw milk collected from hi-tech dairy farms. At the same time, the Group implemented stringent inspection on raw milk sourcing including further improvement in the "Standards for Raw Milk Inspection and Collection" (「原奶檢驗計劃和收購標準」) according to the relevant State standards. Global Positioning System (the "GPS") and monitoring devices were installed in raw milk tankers. Management tactics of "three-dimension monitoring and a closed operation" were in place to ensure milk safety and quality where dedicated persons were assigned to monitor the cattle, to monitor the milk collection centers and to monitor the milk tankers. A closed germ-free system was also in place for raw milk production and transportation.

Apart from ensuring the raw milk safety, the Group took technological initiatives to ensure each and every of its dairy products is safe for consumption. Milk products were produced in a fully-enclosed environment installed with intelligent system controlling the allocation and sterilization of raw milk and mixing of ingredients. Data storage and alarm system were also in place. With respect to product inspection and testing, the Group introduced new testing equipment to conduct tests for more than 30 items, including more than 10 extra items suggested by the Group in addition to those required by the national standards for dairy product safety. The Group also engaged third parties to conduct random or double inspection on finished products to ensure its products are of absolute reliable quality.

To enhance consumers' understanding of our products and restore their confidence in ***Mengniu*** brand, the Group, following government instruction, arranged consumers and media to visit its production plants. It also launched the "Mengniu Milk Safety Project" (「蒙牛牛奶安全工程」) inviting 10,000 consumers to be our safety inspectors of ***Mengniu*** products. The Group also launched an innovative 24-hour live webcast, the first of its kind in the industry, allowing the public a real time inspection of its production facilities, showing to the public its transparent and modernised management.

Our revenue for the year ended 31 December 2008 increased by 11.9% to RMB23,865 million, whereas net loss attributable to equity holders of the Company was RMB948.6 million. Basic loss per share was RMB0.639. The Board of Directors of the Company (the "Board of Directors") did not recommend payment of a final dividend for the year ended 31 December 2008.

CEO's Statement

Although the China dairy industry and the Group experienced setbacks during the year under review, business development and innovation continued to be the focus of the Group. Leveraging on its research and development capabilities and thorough understanding of niche markets, the Group was able to introduce a variety of functional products that broadened its product portfolio and became the icon of consumption trends. Revenue from the liquid milk segment was RMB21,068.1 million, accounting for 88.3% of the revenue of the Group, and remained the main source of income of the Group. During the year, the Group added *Milk Deluxe Organic Milk (特侖蘇有機奶)*, a new product to the Milk Deluxe series, offering more premium choices to consumers. To tap the tremendous potential in the children dairy products market, the Group enhanced the *Future Star(未來星)* series and developed the pure milk product for growing children. It also organized various promotional activities to enhance consumer awareness of importance of dairy nutrition to children's health. Revenue from the ice cream segment was RMB2,626.5 million, accounting for 11% of the revenue of the Group. The Group restructured this segment during the year and built up a new brand with "Trendy, Carefree, Pleasant and Youthful" image. Revenue from other dairy products segment was RMB170.4 million, accounting for 0.7% of the revenue of the Group. On the back of its new technologies, the Group offered more choices to the market by launching a number of cheese products, including its latest *smoke-dried cheese (熏製奶酪)*, *breakfast cheese series (早餐系列)* and *growth cheese series (成長系列)* which were well-received by the market.

The Group is always committed to healthy development of the China dairy industry. During the year under review, the Group continued to make use of its huge resources and extensive network to provide technical support to milk collection centers and raw milk suppliers. The Group also introduced free health services to milk cattle for the first time. During the year, the Group also invited numerous experts and professionals from different fields such as food, dairy products, nutrition and medicine to visit the Group and seminars were held on sustainable and healthy development of the China dairy industry.

Rewarding the society is always our corporate social responsibility. During the year, the Group organized various charitable activities, including the "Milk Loving Care" campaign, setting up of the "Milk Caring Fund of China" and donations to snowstorm and earthquake victims in China. Environmental protection is another issue the Group never turns a blind eye to. It took an active part in a carbon dioxide emission reduction campaign and organized events such as "Volunteer Cycling Journey" to promote green transport and living. The Group also actively promoted voluntary blood donation and set up the "Mengniu Emergency Blood Donation Team" (「蒙牛集團青年志願者應急獻血隊」), which is now one of the largest emergency blood donation teams among the Chinese enterprises.

Looking forward, the Group will strive to rebuild customer confidence and strengthen its brand by improving product quality. The Group will dedicate itself to building of internationalized advanced dairy farms and their infrastructure and provide support to the business of raw milk suppliers, promoting healthy development of the industry, from upstream to downstream. Furthermore, the Group will continue to strengthen the research and development of its proprietary products and improve their taste, functions and packaging, as well as introduce high-end value-added products to fill the market gap and lead the market trend. As a responsible enterprise, the Group will enhance its quality control and inspection to assure consumer confidence. I strongly believe that the lesson learnt last year prepares the China dairy industry for a brighter future and a better tomorrow.

I wish to express my sincere gratitude to different sectors of the society for their unfailing support and encouragement. My team and I will do our very best to establish ***Mengniu*** as an excellent brand of China.

Lastly, Mr. Li Jianxin, our Independent Non-executive Director and member of the audit committee and the remuneration committee of the Company, passed away on 20 February 2009 from a heart attack. I express my deepest sorrow and regret on behalf of the Board for losing a valuable member. I also wish to show our gratitude for the contributions made by Mr. Li to the Company during his tenure and convey our consolation to his family.

NIU Gensheng
Chief Executive Officer

Hong Kong, 16 April 2009

MENGNIU products...

are quality and tasty

Active in R&D, the Group aims to bring more high-end functional products to customers and set industry trends

好牛奶“源”始优质

优质源头，产出AAA优质好奶，当您品鉴每一滴蒙牛牧场奶时，也正在品鉴我们从源头开始不懈努力的用心。好牛奶，“源”始优质。

3A牛奶　“源”有保证

牧奶源自24个优质奶源区，符合美国FDA A级牛奶标准(Grade A标准)，欧盟动物性食品卫生规定(EC)No 853/2004标准，新西兰食品安全局乳制品标准II (NZFSA DPC2标准)，品质可靠有保证

典范牧场　“源”于国际

以蒙牛澳亚国际牧场为模板，以国际先进集约化管理模式打造科技牧场

均衡饲养　“源”自科学

进口荷斯坦乳牛，采用均衡营养的全混合日粮（TMR）饲养工艺，优化奶牛膳食结构，确保每头奶牛健康成长，其产出的牛奶更富含维生素B群及优质蛋白质

严格认证　“源”控品质

国际先进的原料奶采集系统，全程封闭的GPS原奶储运监测体系，ISO9001质量管理体系，ISO14001环境管理体系，HACCP食品安全管理体系认证，全程化生产模式，严控牛奶高品质

Management Discussion and Analysis

FINANCIAL REVIEW

Leveraging on its market leading position and diversified product portfolio, the Group managed to achieve an 11.9% growth in revenue to RMB23,865 million (2007: RMB21,318.1 million) during the year. However, affected by the Milk Incident in the second half of the year, the Group reported a net loss attributable to equity holders of the Company of RMB948.6 million (2007: profit of RMB935.8 million), and basic loss per share was RMB0.639 (Basic earnings per share for 2007: RMB0.664).

Gross Profit

During the year under review, the Group recorded a gross profit of RMB4,669.4 million (2007: RMB4,803.5 million), representing a decrease of 2.8% as compared with that of 2007. With the impact of rising average price of raw milk in 2008 as compared with prior year, and increasing expenses on product promotion and introduction of various measures on raw milk safety in the second half of the year after the Milk Incident, the overall gross profit margin of the Group for the year was 19.6% (2007: 22.5%). To minimize the cost pressure, the Group actively developed various high-end functional products and improved its product mix during the year.

Operating Expenses

In 2008, the Group recorded operating expenses totalling RMB5,926.2 million (2007: RMB3,785.8 million), representing approximately 24.8% (2007: 17.8%) of the Group's revenue or an increase of 7 percentage points as compared with 2007. During the year, owing to the increase in advertising and promotion expenses and the impact of the Milk Incident, the Group incurred additional operating and non-recurrent expenditures. However, the Group aims to keep such increase to a minimum under the Group's continuous stringent control over its operating expenses.

The selling and distribution costs of the Group amounted to RMB4,428 million (2007: RMB3,302 million), representing approximately 18.6% (2007: 15.5%) of the Group's revenue, of which expenses on advertising and promotion accounted for 9.3%, up by 2.1 percentage points as compared to 7.2% in 2007. Such increase was mainly attributable to the launch of various thematic promotion campaigns in relation to the Beijing Olympics by the Group as a leading player in China dairy industry. The Group also made greater marketing efforts in the second half of the year to enhance consumers' understanding of its production process as well as its improved safety measures.

Administrative and other operating expenses amounted to RMB1,498.2 million (2007: RMB483.8 million), representing 6.3% of the Group's revenue (2007: 2.3%). As a result of inventories written off and certain non-recurrent expenditures incurred after the Milk Incident, administrative and other operating expenses of the Group increased by 4 percentage points as compared with that of last year.

Loss from Operating Activities and Net Loss

As a result of the negative impact of the Milk Incident on the Group, in particular the drop in sales, the write-off of certain products pulled off from the shelves, and additional costs incurred for raw milk disposal and sales promotional campaigns, the Group's LBITDA for 2008 was RMB461.7 million (2007 EBITDA: RMB1,667.3 million) and net loss attributable to equity holders of the Company amounted to RMB948.6 million (net profit attributable to equity holders of the Company for 2007: RMB935.8 million).

Capital Structure, Liquidity and Financial Resources

For the year ended 31 December 2008, the Group's net cash inflow from operating activities amounted to RMB586.9 million (2007: RMB2,058.1 million). Net cash balances (cash and bank balances net of total bank loans) amounted to RMB1,313.3 million (2007: RMB1,947.7 million) as at 31 December 2008, showing that the financial position of the Group remained at a reasonable level.

As at 31 December 2008, the outstanding bank loans of the Group amounted to RMB1,728.7 million (2007: RMB263.2 million), of which RMB1,208.7 million (2007: RMB183.2 million) was repayable within one year and RMB520 million (2007: RMB80 million) was repayable beyond one year. Bank loans in the amount of RMB720.3 million (2007: RMB149.6 million) was fixed interest-bearing.

The total equity of the Group was RMB4,738 million as at 31 December 2008 (2007: RMB5,834.7 million). The debt-to-equity ratio (total bank loans over total equity) of the Group was 36.5% (2007: 4.5%) as at 31 December 2008, 32 percentage points higher than that of 2007.

Management Discussion and Analysis

MARKET REVIEW

The China dairy industry became the public focus and attention in 2008, in particular, the Milk Incident in September 2008 which forced the industry players to review and evaluate, and implement stringent control over the production process, especially the quality of raw materials, rather than solely focus on business growth.

Both the state and local governments quickly introduced a series of measures including the “Regulation on the Supervision and Administration of the Quality and Safety of Dairy Products” (「乳製品質量安全監督管理條例」) and the “Outlines of the Rectification and Revival of the Dairy Industry” (「奶業整頓和振興規劃綱要」) soon after the Milk Incident to strengthen the quality and safety control of dairy products, to protect public health and to promote healthy development of the dairy industry.

The Group responded positively after the Milk Incident with thorough review and evaluation of its operations. The Group implemented a number of effective measures to promote healthy development of the industry, including taking initiatives to construct high quality and standardised raw milk supply bases, exercising stringent control over quality of raw materials and products, implementing inspection on production process from raw milk collection to final product inspection, and improving communication with customers.

BUSINESS REVIEW

During the year under review, customers’ health and safety topped the priority of the Group. It implemented stringent product testing and inspection to ensure product quality and safety. The Group enhanced its production transparency allowing customers’ better understanding of ***Mengniu*** products. The enhanced transparency showed the confidence of the Group in its product quality. The Group also continued to develop and promote high-end products, offering customers with delicious, nutritious and safe dairy products.

Product Safety

Adhering to its principle of "accepting more responsibility as a big brand", to ensure product safety and to rejuvenate the China dairy industry, the Group promptly responded to the government's call soon after the Milk Incident. Other than recalling the relevant products without delay, the Group pledged to tighten its control over raw milk source. It quickly introduced advanced inspection equipment and increased product testing items. Furthermore, the Group called for and obtained "Undertaking for Quality of Raw Milk" (「原奶質量承諾書」) from more than 3,400 raw milk collection centres across the country to ensure product safety.

To enhance its production transparency, public and media were invited to visit its ranch and production plants from September 2008 onwards. The Group also commenced the "Mengniu Milk Safety Project" (「蒙牛牛奶安全工程」) in November and December 2008 to enhance the production transparency and foster consumer confidence. 10,000 consumers were invited across the country to visit the headquarters of the Group in Inner Mongolia and acted as the safety inspectors of the Group. They were invited to observe the production process of ***Mengniu*** products which was of international quality control standards. 100 of them were subsequently elected as committee members of the "Mengniu Milk Safety Project" to exercise long-term supervision over the Group's production process.

At the same time, the Group also achieved "transparent production" by launching a 24-hour live webcast, the first of its kind in the China industry, allowing consumers a real time inspection of certain of its related milk cattle farms, and its testing and production process. The Group strived to improve public confidence in its products through its transparent and modernised management system.

Branding and Marketing

To encourage public participation in sports in the Olympic year, the Group, as a leading dairy brand in China, held campaigns and activities under the theme of "Running to Beijing", including "Running to Beijing – Sui Bian Dance Contest" (「奔向北京 • 隨變炫舞大賽」), "Mengniu's Inter-city All People Sports Game" (「蒙牛城市之間全民健身活動」), "Mengniu Green Cyclists Running to Beijing" (「蒙牛綠色騎手奔向北京」). These activities were promoted under the concept of "Exercise, Health and Nutrition for all of China" which aimed to promote public awareness of sports, food nutrition and healthy lifestyle.

Management Discussion and Analysis

With respect to promotion and marketing, during the year, the Group launched an array of marketing campaigns that matched both the Group's product image and consumer preference. These included a series of diversified musical events, such as "Running to Beijing – Make Your Music Dream Comes True" (「奔向北京 • 成就音樂夢想」) and "Mengniu Suan Suan Ru Music Award Presentation Ceremony" (「蒙牛酸酸乳音樂風雲榜頒獎盛典」), both of which echoed the young and fashionable image of *Suan Suan Ru (酸酸乳)*. To tap the tremendous potential in the children dairy product market and to enhance parents' knowledge on nutrition value of dairy products, the Group established the "Future Star Children Milk Nutrition Research Centre" (「未來星中國兒童牛奶營養研究中心」) and jointly organised a programme called "Winning from the Start – Growth Program" (「贏在起點 • 成長工程」) with the Women's Federation. The Group also set up its first online interactive parenting platform in China to provide information on relationship between milk nutrition and children growth.

Products

During the year under review, leveraging on its innovative technology and knowledge of niche markets, the Group introduced various high-end functional products that broadened its product portfolio.

Liquid milk

Revenue from the liquid milk segment amounted to RMB21,068.1 million, accounting for 88.3% of the revenue of the Group, remained the major source of income of the Group.

UHT milk

Revenue from UHT milk products reached RMB13,697.1 million, accounting for 65% of the revenue of the liquid milk segment. During the year, the Group further expanded the *Milk Deluxe* series by introducing *Milk Deluxe Organic Milk (特侖蘇有機奶)*. Moreover, to cater for the awareness of city dwellers to improve digestion, the Group developed and launched a new product, *Xin Yang Dao Low-Lactose Milk (新養道低乳糖牛奶)* for easy absorption of nutrients, delivering more quality product choices to customers. To develop secondary brand of children milk, the Group enhanced the *Future Star (未來星)* series and developed the pure milk products for growing children, establishing a new children milk product line. To cater for the strong emerging demand in the children's market, the Group will continue to develop more nutritious and delicious milk products for children.

Milk beverages

Revenue from the milk beverages segment was RMB5,593.6 million, accounting for 26.6% of the revenue of the liquid milk segment. *Fruit Milk Drink (真果粒)* received the "Country Award" (「金獎國別獎」) at the 2008 SIAL International Food Products Exhibition organized by Exposium, the largest exhibition group in France and the 10th largest in the world. Supported by different promotion activities, *Suan Suan Ru (酸酸乳)* remained the leading product in the market. *Miao Miao Milk (妙妙奶)*, targeted the children's market, were sold with an innovative and fun packaging to attract children and stimulate their purchase desire. Activities such as "Miao Miao Family Fun Club" (「妙妙家族趣樂會」) helped promoting consumer understanding and acceptance of the children milk products. In future, the Group plans to introduce more milk beverage of different flavours to widen its product range and create new growth drivers.

Yogurt

Revenue from the yogurt segment totalled RMB1,777.4 million, accounting for 8.4% of the revenue of the liquid milk segment. The Group further improved the product *Champion (冠益乳)* which contains coronatine for digestion improvement. It was in a feminine packaging design and was portrayed as a healthy and energetic icon. The product was promoted along with the campaigns such as "Running to Beijing – Everyone Is a Champion" (「奔向北京 • 人人是冠軍」). The Group also established a product line, *Fiber Fruit Grain Yogurt (纖維新意果粒)* series, by adding edible fibre into its *Large Fruit Grain Yogurt (大粒果實酸奶)*. Yoga was used in the marketing to highlight the healthy image of the product. The Group plans to expand the high-end functional product market and strengthen the position of yogurt products to capture the increasing demand in the segment.

Ice-cream

Revenue from the ice-cream segment amounted to RMB2,626.5 million, accounting for 11% of the revenue of the Group. With an aim to branding the ice-cream products as "Trendy, Carefree, Pleasant and Youthful", the Group restructured the segment by regrouping the products under five secondary brands, namely *"Sui Bian, Mood for Green, Deluxe, Qu Zai and Ice+" (隨便、綠色心情、蒂蘭聖雪、趣仔及冰+)*. In 2008, *Sui Bian Euro Roll (隨變歐羅旋)* remained the highlight of this segment, featuring with an exotic European taste with a trendy and ready-to-change style. In future, the Group will strive to improve the products under these five secondary brands by developing more flavours and upgrading product packaging. The Group will increase the proportion of high-end and high value-added products to improve the product mix and present a more distinctive image of ***Mengniu*** brand.

Other dairy products

Revenue from the other dairy products amounted to RMB170.4 million, accounting for 0.7% of the Group revenue. For milk powder products, the Group launched *Jinzhuang Jiazhi (金装佳智)* series, targeting the mid- and high-end markets. Furthermore, as cheese products became more popular in China, the Group successfully developed series of cheese products including *Smoke-dried Cheese (熏制奶酪)*, *Breakfast Cheese (早餐系列)* and *Growth Cheese (成長系列)* that suit Chinese taste. To capture the market potential, the Group will actively improve the flavours of different cheese products and focus on the development of cheese for children, introducing nutritious products to more customers.

Quality Control

The Group is always alert to product quality. It exercised stringent control over various production stages, from raw materials, production, finished products to sales outlets. To ensure the quality of raw milk, the Group continued to strengthen the control of cattle breeding in ranches, including control over the selection, origins and quality of hay and its transportation. New measures were implemented regarding the sanitary standard of cattle farms and cattle vaccination so as to ensure the raw milk quality.

With respect to raw milk collection, the Group established the "Standards for Raw Milk Inspection and Collection" (「原奶檢驗計劃和收購標準」) with reference to the State standards so as to ensure the safety and quality of raw milk. In addition, to enhance the efficiency and standard of raw milk collection and transportation, the Group installed Global Positioning System ("GPS") in raw milk tankers. Management tactics of "three-dimension monitoring and a closed operation" were in place to ensure milk safety and quality where dedicated persons were assigned to monitor the cattle, to monitor the milk collection centres

and to monitor the milk tankers. A closed germ-free system was also in place for raw milk production and transportation.

The Group took technological initiatives to ensure that the production was controlled by a centralized system. Milk products were produced in a fully-enclosed environment installed with an intelligent system controlling the allocation and sterilization of raw milk and mixing of ingredients. Data storage and an alarm system were in place. The Group also introduced latest testing equipment to conduct tests for more than 30 items, in addition to the requisite items required by the national standards for dairy product safety, more than 10 extra items suggested by the Group such as fertilizer residue, additives and heavy metal were tested. The Group also conducted batch-by-batch inspection for raw milk, supplementary ingredients and finished products, and engaged third parties to conduct random or double inspection on finished products. The 4-tier safety check ensured the Group's products are reliable so that customers can enjoy safe and fresh dairy products.

Production and Operation

For the year ended 31 December 2008, the Group further expanded the production capacity and had an aggregate annual production capacity of 5.57 million tons (2007: 4.78 million tons).

With the goal of developing proprietary healthy products for the high-end dairy products market and fine niche markets, The Group's Research and Development ("R&D") Centre continued to develop new products and applied technology. It strived to develop more new high-end products aiming to fill the market gap and lead the dairy product trend in China.

The Group made on-going improvement in its management system. Efforts were made in standardizing quality control and optimizing operation and management and enhancing the cost competitiveness of the Group. The Group will review its management system regularly and make timely adjustments to respond to the market requirements.

Industry Exchange

As a leader in the China dairy industry, the Group commits itself to the healthy development of the dairy industry. With the Group's resources, strong operating network, technical services and management support to ranches, smaller farms, collection centres and dairy farmers, it is hoped that the relationship amongst the industry players for mutual development can be fostered.

During the year under review, the Group continued to provide raw milk suppliers with training and guidance conducted by either external experts or internal staff. The Group introduced free health care services for milk cattle and provided free raw milk inspection and testing service to raw milk suppliers and on-site guidance on breeding management. The Group also consolidated its resources of different equipment suppliers and built a "Mengniu Service Centre for Designated Collection Centres". The service network covers regions of milk source and investigation and follow up action can be carried out once problem arises. Currently, the Group plans to standardize the management of the service centres to assist raw milk suppliers and collection centres to allocate resources more effectively for a better development of the industry.

On 7 November 2008, professionals specialized in food, dairy products, nutrition and medicine from Beijing Children's Hospital, Dairy Association of China and Chinese Nutrition Society visited the Group's production base and exchanged views with the Group. A seminar called "Dairy Products Safety and National Health" was held at which the importance of dairy products to public health and their future development were discussed.

Management Discussion and Analysis

Social Responsibilities

It is the Group's philosophy to reward the society. In the first half of the year, the Group and Bank of China jointly issued the world's first milk caring credit card, "BOC-Mengniu Milk Loving Care Credit Card" (「中銀蒙牛愛心信用卡」). In July 2008, the Group jointly established the "Milk Loving Care Fund of China" with China Children and Teenagers' Fund, demonstrating the joint efforts of social organisation and enterprises. In 2008, the "Milk Loving Care" campaign initiated by the Group covered more than 1,000 primary schools across China where more students were benefited from the scheme. During the year under review, China experienced severe snowstorm and earthquakes happened in Sichuan. As a leading dairy enterprise, the Group responded and donated both resources and cash to the affected regions without delay. "Milk Delivery Express" was also available to tent schools to give children nutrients and hope.

The Group has strong commitment to environmental protection and actively participated in different environmental activities. The Group and the China Association for Non-government Organizations Cooperation and the US Environmental Defense Fund jointly organised a charitable event, "Green Journey • Less Discharge of Carbon Dioxide" (「綠色出行 • 碳路行動」). During the year under review, the Group significantly reduced carbon dioxide emission. The Group also, jointly with the Beijing People's Radio, launched a large cycling event, "Mengniu Green Cyclists Running to Beijing" (「蒙牛綠色騎手奔向北京」) to promote green transport and arouse public awareness of environmental protection and quality living.

In 2007, the Group set up "Mengniu's Emergency Blood Donation Team" (「蒙牛集團青年志願者應急獻血隊」), which is now one of the largest emergency blood donation teams among the Chinese enterprises. The Group will continue this chartable activity to encourage blood donation.

OUTLOOK

In December 2008, 13 government ministries and commissions jointly formulated the "Outlines of the Rectification and Revival of the Dairy Industry" (「奶業整頓和振興規劃綱要」) specifying the targets to rejuvenate the dairy industry in China. It aimed to achieve the following targets by October 2011: increase in the scale of milk cattle breeding operations; integration of production and sales; improvement in the processing flow; standardization of the industry; regulatory control over market competition and enhancement of the quality standard system. The outline set out revolutionary requirements on matters

such as the ratio of first-class milk cattle, the average output per cattle and the scale of breeding farm operations. To date, milk consumption in China remains far below the international average consumption level, representing huge growth potential. On the back of strong support from the State and efforts of dairy enterprises, it is believed that China dairy products will continue to have promising growth prospects.

2008 marked the turning point for the China dairy industry. Accelerated industry consolidation and elimination of inefficient small-scale enterprises are expected in future. With the challenges and opportunities arising from the industry consolidation and restoration of customer confidence, the Group, as a market leader for years, is confident that it is capable to take the lead in the healthy and ordered development of the China dairy industry leveraging on its strong R&D capabilities, sizeable production and stringent quality control.

Promote internationalized advanced ranches and create better future for the China dairy industry with raw milk suppliers

Quality control at milk sources is fundamental to safety of dairy products. The Group, as the industry leader, has commenced to invest since years ago, in the construction of the international ranch in China. During the recent years, with the Group's experience in its investment in various internationalized advanced dairy farms, the Group has supported to speed up the development of small and medium ranches by assisting the building of sizeable ranches and collection centres across the country, pushing for reform to achieve the objectives of integrated breeding and milking, large-scale breeding of milk cattle and regionalization and standardization of ranches.

In future, the Group will continue to enhance the investment in the building of ranches and cooperate with raw milk suppliers and strengthen the management and control over raw milk production. It is hoped that with the increase in operational efficiency of milk station operators and milk farms by introducing to them species improvement, vaccination, and modern breeding technologies, in turn enhancing their confidence in and motivation to safe production and development of the entire dairy industry chain.

Continue to strengthen research and development of proprietary products, to fill the market gap by high-end value-added products

With the increasing consumption power and health concerns in China, the Group believes that nutrition value of food and beverages will become an important factor in consumers' consumption. In a fragmented market where customers prefer higher-end products, products of natural and functional formulae are the products with increasing value. The Group believes that products which can help the digestive and immunity system, to relieve stress, to improve sleeping quality and for beauty will become the market future focus.

The Group will continue to develop healthy products and improve the taste, functions and packaging of dairy products. It will focus on the high-end dairy market and niche markets and aims to become the icon of market trends by launching new high-tech and value-added products. The Group will increase the communication with customers, enhance its transparency and improve product quality under the monitor of its customers and the society.

Management Discussion and Analysis

Strengthen quality inspection and enhance production process transparency to build up customers' confidence in the Group's products

The Group will remain responsible to its customers. The Group will continue to enhance product quality control and inspection at its production to ensure product safety. Apart from monitoring milk source, the Group will refine the operation practice of collection centres and speed up the construction of modern ranches to ensure the raw milk quality and protect the raw milk suppliers' interests. It will continue to apply advanced technologies to ensure that raw milk is transported and processed in a fully-enclosed and germ-free environment. The adding of supplementary ingredients will also be under stringent control. The Group will also exercise strict inspection of the finished products. It has implemented multi-level inspection and supervision with reference to the highest local and international standards so as to offer high quality products to customers.

To promote consumer understanding of its products, the Group will remain transparent and continue to accept public supervision. It will improve its communication with customers and the media for mutual understanding and trust. Through its transparent production, it is believed that the Group will receive consumer recognition.

HUMAN RESOURCES AND REMUNERATION OF EMPLOYEES

As at 31 December 2008, the Group had approximately 23,500 employees in China and Hong Kong. Total staff costs for the year, excluding directors' remuneration, were approximately RMB1,063.2 million (2007: RMB885.9 million). To enhance the quality and competence of the employees, the Group provided intensive training programs to staff members to enrich their knowledge and awareness of the importance of safe production. The Group also implemented a series of measures to increase revenue and reduce costs. With respect to reducing staff costs, the senior management took the lead to accept reduction in salaries, business travel expenses, communication expenses and other office expenses. Internal fringe benefits were also adjusted. The Group has performance-linked incentive plans and share option schemes to increase incentive and efficiency of the employees.

EXECUTIVE DIRECTORS

Mr. Niu Gensheng, aged 51, is the Chief Executive Officer of the Company. Mr. Niu is the Chairman and one of the founders of Inner Mongolia Mengniu Dairy (Group) Company Limited ("Inner Mongolia Mengniu"). Mr. Niu graduated from Inner Mongolia University with a degree in Administration and Management and obtained a Master's degree in Enterprise Management at the Chinese Academy of Social Sciences Graduate School. With his extensive experience and insights in China's dairy industry, Mr. Niu receives high reputation in the industry. In 2007, Mr. Niu was elected as one of "China's Most Influential Business Leaders" for the fifth consecutive year, honored as "2007 Hong Kong Bauhinia Awards". Mr. Niu is devoted to charity and was ranked third in the 2007 Hurun Top 10 for Charity. Mr. Niu currently serves as the Deputy Chairman of Dairy Association of China, China Dairy Industry Association, and the Second China National Committee of International Dairy Federation. Mr. Niu is also an independent non-executive director of two listed companies (including a company listed in China).

Mr. Yang Wenjun, aged 42, is a Vice President of the Company, the Chief Executive Officer and one of the founders of Inner Mongolia Mengniu. Prior to the appointment as Inner Mongolia Mengniu's CEO, Mr. Yang was Inner Mongolia Mengniu's Vice President and the general manager of the liquid milk division, and has solid dairy industry experience. Mr. Yang graduated from Inner Mongolia Light Industry Institute in dairy products and he also holds a Master's degree in Business Administration from Barrington University. Mr. Yang was jointly elected as "2007 Person of the Year in China" by Global Sources and World Entrepreneur. Mr. Yang also received "Special Award of Corporate Culture Building" in 2007 Annual Conference of National Corporate Culture Building.

Mr. Sun Yubin, aged 42, is a Vice President of the Company, secretary of the Party committee and one of the founders of Inner Mongolia Mengniu. Mr. Sun graduated from Inner Mongolia University with a degree in Economic Management. Prior to the appointment as Inner Mongolia Mengniu's secretary of the Party committee, he was a Vice President and the General Manger of ice cream department of Inner Mongolia Mengniu. Mr. Sun has solid dairy industry experience.

Mr. Yao Tongshan, aged 52, is the Chief Financial Officer of the Company. Mr. Yao joined Inner Mongolia Mengniu in October 2001. Mr. Yao graduated from Tianjin University with a Master's degree in Engineering. Mr. Yao previously served as a director of the international credit department at China Construction Bank (Inner Mongolia branch), a manager of investment banking division at a state-owned energy resources investment company and the chief financial officer of Inner Mongolia Mengxi High-tech Group (內蒙古蒙西高新技術集團). Mr. Yao has extensive experience in finance and investment management.

Mr. Bai Ying, aged 38, is a Vice President and the general manager of UHT milk division of the Inner Mongolia Mengniu. He joined Inner Mongolia Mengniu upon its establishment in 1999 and has extensive experiences in dairy industry. Mr. Bai graduated with a Master degree from Inner Mongolia Agriculture University. In 2004, Mr. Bai was granted the "Outstanding Contribution Award for Development of Western Region of Inner Mongolia Autonomous Region" and was elected as one of the "Ten Outstanding Young Persons in Inner Mongolia".

Directors and Senior Management

NON-EXECUTIVE DIRECTORS

Mr. Jiao Shuge (alias Jiao Zhen), aged 43, is the Chairman of the Board of Directors. Mr. Jiao joined the Group in September 2002. Mr. Jiao is currently the general manager at CDH China Fund, L.P. Mr. Jiao received a Bachelor's degree in Mathematics from Shandong University and a Master's degree in Engineering from the Ministry of Space Industry Institute. Mr. Jiao serves as a director of various listed companies.

Mr. Julian Juul Wolhardt, aged 35, joined the Group in January 2006. Mr. Wolhardt is currently a director of KKR Asia Limited focusing on private equity transactions in the Greater China region. Mr. Wolhardt is a CPA and CMA and received a B.S. with honors in Accounting from the University of Illinois (Urbana-Champaign).

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Wang Huaibao, aged 71. Mr. Wang graduated from People's University of China. Mr. Wang served as a Deputy Chairman of the Dairy Association of China and the Chairman and the general manager of Beijing Milk Company (now Beijing Sanyuan Food Company Limited). Mr. Wang also served as the Chairman of the China Dairy Industry Association. Mr. Wang was appointed as an independent director of Inner Mongolia Mengniu on 18 October 2002 and became an independent director of the Company on 23 February 2004.

Mr. Zhang Julin, aged 65, is a professor of accounting. Mr. Zhang graduated from the Economics Department of Lanzhou University. Mr. Zhang served as an assistant dean to the Inner Mongolia Finance and Economics University. Mr. Zhang is currently a Vice Chairman of the Inner Mongolia Audit Society and an independent director for Inner Mongolia Lantai Industrial Co., Ltd. Mr. Zhang is also a member of the Chinese Institute of Certified Public Accountants. Mr. Zhang was appointed as an independent director for Inner Mongolia Mengniu on 18 October 2002 and became an independent director of the Company on 23 February 2004.

Mr. Li Jianxin, aged 45, was a senior economist. Mr. Li studied finance as a graduate student at the School of Economics, Peking University. Mr. Li previously served as a secretary of commission, director of general manager office and deputy director of the policy research office for China Lucky Film Corporation. Mr. Li was appointed as an independent director for Inner Mongolia Mengniu on 18 October 2002 and became an independent director of the Company on 23 February 2004. Mr. Li passed away unexpectedly on 20 February 2009 due to a heart attack. Before his death, Mr. Li served as a director and the secretary to the board of directors at Lucky Film Co. Ltd., a listed company on the Shanghai Stock Exchange.

SENIOR MANAGEMENT

Mr. Bai Jun, aged 45, a senior engineer, is the Chairman of Inner Mongolia Mengniu labor union. Mr. Bai joined Inner Mongolia Mengniu upon its establishment in 1999. Mr. Bai received a Master's degree in Business Administration from People's University of China. Mr. Bai has solid dairy industry experience.

Mr. Lei Yongsheng, aged 47, is the Chief Administrative Officer of the Company and is the Secretary of the Board of Directors of Inner Mongolia Mengniu. Mr. Lei joined the Group in February 2002. Mr. Lei graduated from Inner Mongolia Finance and Economics University with a degree in Economics. Mr. Lei served as a deputy director of Inner Mongolia State-owned Assets Administration Bureau Asset Valuation Center and a deputy director of Inner Mongolia Finance Bureau General Office. Mr. Lei has extensive experience in administrative management.

Mr. Yao Haitao, aged 47, is a Vice President in Administration of Inner Mongolia Mengniu. Mr. Yao joined Inner Mongolia Mengniu in 2003. He graduated from Inner Mongolia Finance and Economics College with a Bachelor's degree in Economics. Mr. Yao has solid experience in administrative management.

Ms. Zhao Yuanhua, aged 46, is a Vice President in Sales and Marketing of Inner Mongolia Mengniu. Ms. Zhao joined Inner Mongolia Mengniu in 2000. She graduated from Baotou University of Iron and Steel Technology with a Bachelor's degree in Technology. Ms. Zhao has solid experience in sales and marketing.

Mr. Ding Sheng, aged 41, is a Vice President and the general manager of yogurt division of Inner Mongolia Mengniu. Mr. Ding joined Inner Mongolia Mengniu in 2003 and has solid dairy industry experience. Mr. Ding graduated from Nankai University with a Master's degree in Business Administration. Mr. Ding was awarded as an "Outstanding Staff of Dairy Industry in Inner Mongolia" in 2006.

Mr. Wu Jingshui, aged 43, is a Vice President in Finance of Inner Mongolia Mengniu. Mr. Wu graduated from Inner Mongolia Light Industry Institute majoring in financial accounting and holds a senior accountant qualification. Before being appointed as the Vice President in Finance of Inner Mongolia Mengniu, Mr. Wu served as Chief Financial Officer of liquid milk division and Chief Financial Officer of Inner Mongolia Mengniu. Mr. Wu has extensive experience in financial management.

COMPANY SECRETARY AND QUALIFIED ACCOUNTANT

Mr. Kwok Wai Cheong, Chris, aged 36, the Financial Controller and Company Secretary of the Company, joined the Group in May 2007. Prior to joining the Group, Mr. Kwok was the Financial Controller of a Hong Kong Main Board listed company and he also had served in an international accounting firm. Mr. Kwok graduated from The Hong Kong Polytechnic University with a Bachelor's degree in Accountancy. Mr. Kwok is a member of the Hong Kong Institute of Certified Public Accountants and a fellow member of Association of Chartered Certified Accountants.

MENGNIU products...

are safe and reliable

MENGNIU **practices stringent supervision and control throughout the entire production process from raw milk sourcing, to production and finished products, encompassing 4-tier safety test by the most advanced equipment and independent third parties to guarantee its products are safe and reliable**

层层监管

生产监管— 全封闭系统实时监控

安全监管— 全方位质量检测

运输监管— GPS定位跟踪

生活监管— 精心营造优越环境

健康监管— 精挑国际优良奶牛

营养监管— 精选全球优质牧草

只为这一管

每一盒牛奶的生产，蒙牛都尽心尽力。从奶源开始所有环节都严格把关，保证每一盒牛奶的健康营养。有我们层层认真监管，您只管安心饮用。

Corporate Governance Report

The Company is dedicated to ensure high standards of corporate governance with an emphasis on a diligent Board of Directors (the "Board"), sound internal control, and increasing transparency and accountability to shareholders. The Board acknowledges that good corporate governance practices and procedures are beneficial to the Group and its shareholders. The Company is committed to improve those practices and maintain its ethical corporate culture.

The Company has adopted the code provisions set out in the Code of Corporate Governance Practices (the "CG Code") contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") as its own code of corporate governance practices.

Throughout the year, the Group has fully complied with all the compulsory code provisions set out in the CG Code.

THE BOARD

As at 31 December 2008, the Board comprised ten Directors, including five Executive Directors, namely, Mr. Niu Gensheng, Mr. Yang Wenjun, Mr. Sun Yubin, Mr. Yao Tongshan and Mr. Bai Ying, two Non-executive Directors, namely, Mr. Jiao Shuge (alias Jiao Zhen) and Mr. Julian Juul Wolhardt, and three Independent Non-executive Directors, namely, Mr. Wang Huaibao, Mr. Zhang Julin and Mr. Li Jianxin. The Chairman of the Board is Mr. Jiao Shuge and the Chief Executive Officer of the Company is Mr. Niu Gensheng.

The Board is responsible for the leadership and management of the Company. Key responsibilities of the Board comprise formulation of the Group's overall strategies and policies, setting of performance and management targets, evaluation of business performance and supervision of management's performance. The management was delegated the authority and responsibility by the Board for the management and operations of the Group. In addition, the Board has also delegated various responsibilities to the Board Committees as detailed in this report.

Subsequent to the balance sheet date, Mr. Li Jianxin, an independent non-executive director, an audit committee and a remuneration committee member of the Company passed away on 20 February 2009 due to a heart attack. Following the passing away of Mr. Li, the Company has only two Independent Non-executive Directors and two audit committee members which fall below the minimum number of three Independent Non-executive Directors and three audit committee members as required under Rule 3.10(1) and Rule 3.21 of the Listing Rules respectively. In this regard, the Company is in the process of and will as soon as possible appoint a suitable candidate to fill the vacancy and will announce the appointment of a new independent non-executive director and audit committee member as soon as possible and in any event within the time period set forth in Rule 3.11 and Rule 3.23 of the Listing Rules.

Biographies of the Directors are set out on pages 25 to 27 of the annual report, which demonstrates a diversity of skills, expertise, experience and qualifications. There is no other material financial, business or relevant relationships among the Directors.

INDEPENDENCE OF INDEPENDENT NON-EXECUTIVE DIRECTORS

The Independent Non-executive Directors possess appropriate professional qualifications, or accounting or related financial management expertise. Their role is to provide independent and objective opinions to the Board for its consideration and decisions. The Company has received annual confirmation of independence from the existing Independent Non-executive Directors in accordance with Rule 3.13 of the Listing Rules. The Board has assessed their independence and concluded that all existing Independent Non-executive Directors are independent within the definition of the Listing Rules. The Company also considers Mr. Li Jianxin to be independent under the Listing Rules during his term of office.

BOARD PROCEEDINGS

The Board meets at least four times a year and additional operational meetings are also held, when required. The Company Secretary is responsible for preparing agenda and notices for the meetings. Senior management of the Group also provides the directors with relevant information on a timely basis regarding key business developments of the Group and issues affecting the Group. Agenda and other information packages are normally delivered to the directors before the meetings. The directors also have independent access to the senior management in respect of operating issues. The directors may take independent professional advice where appropriate to discharge their duties, at the Company's expenses.

During the year ended 31 December 2008, the Board held nine meetings. The attendance of each of the directors at the Board meetings is as follows:

Directors	**Attendance of Board meetings in 2008**(2)
Niu Gensheng	9/9
Yang Wenjun	9/9
Sun Yubin	9/9
Yao Tongshan(1)	4/4
Bai Ying(1)	3/4
Jiao Shuge (alias Jiao Zhen)	9/9
Julian Juul Wolhardt	9/9
Wang Huaibao	8/9
Zhang Julin	9/9
Li Jianxin	8/9

Notes:

(1) Mr. Yao Tongshan and Mr. Bai Ying were both appointed as Executive Directors with effect from 15 July 2008.

(2) During the year, the Company held four quarterly meetings and five other meetings to handle operational-level matters. According to the Company's articles of association, the quorum for convening a Board meeting is two members.

Minutes of meetings of the Board and Board Committees are kept by the Company Secretary of the Company and are not only open for inspection by the directors but also sent to the directors for their records. All directors have access to the Company Secretary of the Company, who is responsible for ensuring that the Board procedures are complied with and advising the Board on compliance matters.

Corporate Governance Report

CHAIRMAN AND CHIEF EXECUTIVE OFFICER

The role of the Chairman is separate from that of the Chief Executive Officer to ensure a balance of power and authority. The Chairman is responsible for overseeing the functioning of the Board while the Chief Executive Officer is responsible for managing the Group's business.

The Chairman shall ensure that Board meetings are planned and conducted effectively and all directors are properly briefed on issues arising at Board meetings. He is also responsible for ensuring that the directors receive in a timely manner adequate information, which must be complete and reliable.

APPOINTMENT, RE-ELECTION AND REMOVAL OF DIRECTORS

Each director has entered into a service contract with the Company for a term of three years. The directors are subject to retirement by rotation and re-election at each annual general meeting of the Company in accordance with article 112 of the Company's articles of association. The directors appointed as an addition to the Board or to fill a casual vacancy on the Board shall be subject to re-election by the shareholders at the first general meeting after the appointment.

BOARD COMMITTEES

To oversee particular aspects of the Company's affairs and to assist in the execution of its responsibilities, the Company has established three Board Committees under the Board, namely the Audit Committee, the Remuneration Committee and the Nomination Committee, each of which is governed by specific terms of reference approved by the Board, covering its functions, duties and powers. The terms of reference of the respective Board Committees have complied with the CG Code provisions and are available for public inspection at the Company's principal place of business in Hong Kong. The Committees have been structured to include a majority of Independent Non-executive Directors as members in order to reinforce independence.

REMUNERATION COMMITTEE

As at 31 December 2008, the Remuneration Committee comprised four members, three of whom are Independent Non-executive Directors and one Non-executive Director. The Remuneration Committee is chaired by Mr. Wang Huaibao, Independent Non-executive Director.

The duties of the Remuneration Committee are to review annually and recommend to the Board the overall remuneration policy for the directors and senior management to ensure that the level of remuneration is linked to their level of responsibilities undertaken. The Remuneration Committee shall also evaluate annually the performance of the directors and the senior management and recommend to the Board specific adjustments in their remuneration and/or reward payments.

The Company's policy on remuneration is to maintain fair and competitive packages based on business needs and industry practice. For determining the level of fees paid to members of the Board, market rates and factors such as each director's workload and required commitment will be taken into account. In addition, factors comprising economic and market situations, individual contributions to the Group's results and development as well as individual potential are considered when determining the remuneration packages of executive directors.

During the year, the Remuneration Committee had performed the following:

– assessed the performance of the directors and senior management;

– reviewed and approved the remuneration for the directors and senior management;

– reviewed the remuneration policy and recommended to the Board; and

– reviewed the proposal of granting of share options according to the Company's share option scheme, and made recommendations to the Board.

The Remuneration Committee held one meeting during the year ended 31 December 2008 and one meeting to date in 2009. The attendance record of each member of the Remuneration Committee for the year is set out below:

Directors	**Attendance of Remuneration Committee Meeting in 2008**
Wang Huaibao *(chairman)*	1/1
Julian Juul Wolhardt	1/1
Zhang Julin	1/1
Li Jianxin	1/1

NOMINATION COMMITTEE

As at 31 December 2008, the Nomination Committee comprised three Non-executive Directors, two of whom are independent (Mr. Wang Huaibao and Mr. Zhang Julin). The Nomination Committee is chaired by Mr. Jiao Shuge, Non-executive Director and the Chairman of the Board.

The responsibilities of the Nomination Committee is to review the structure, size and composition, including the skills, knowledge and experiences of the Board and make recommendations to the Board regarding any proposed changes. The Nomination Committee is also responsible to identify and nominate suitable candidates qualified to become Board members and makes recommendations to the Board on relevant matters relating to the appointment or re-appointment of directors if necessary, in particular, candidates who can add value to the management through their contributions in the relevant strategic business areas and which appointments will result in the constitution of a stronger and more diverse Board. In the selection process, the Nomination Committee makes reference to criteria including, inter alia, reputation for integrity, accomplishment and experience in the dairy industry, professional and educational background, and commitment in respect of available time.

The Nomination Committee held one meeting in the year ended 31 December 2008 to discuss the nomination of two additional Executive Directors namely, Mr. Yao Tongshan and Mr. Bai Ying. The attendance record of each member of the Nomination Committee for the year is set out below:

Directors	**Attendance of Nomination Committee Meeting in 2008**
Jiao Shuge *(chairman)*	1/1
Wang Huaibao	1/1
Zhang Julin	1/1

AUDIT COMMITTEE

As at 31 December 2008, the Audit Committee comprised three Non-executive Directors, two of whom are independent and possess the relevant professional qualifications required under the Listing Rules. The Committee is chaired by Mr. Zhang Julin, Independent Non-executive Director.

The Audit Committee serves as a focal point for communication between other directors, the external auditors, and the management as their duties relate to financial and other reporting, internal controls and the auditing. The Audit Committee assists the Board in fulfilling its responsibilities by providing an independent review of financial reporting and by satisfying themselves as to the effectiveness of the Company's internal controls and as to the efficiency of the audits.

During the year, the Audit Committee has performed the following:

– met with the external auditors to discuss the general scope and findings of their audit and interim review works;

– reviewed external auditors' management letter and management's response;

– reviewed and recommended to the Board for approval of the external auditors' remuneration;

– made recommendations to the Board on the re-appointment of the external auditors;

– reviewed the external auditors' independence, objectivity and the effectiveness of the audit process;

– reviewed and monitored the integrity of financial statements, annual and interim reports, and annual and interim announcements of the Company;

– discussed auditing, internal control, risk management and financial reporting matters before recommending them to the Board for approval; and

– reviewed the connected transactions entered into by the Group.

All issues raised by the external auditors and the Audit Committee have been addressed by the senior management. The work and findings of the Audit Committee have been reported to the Board. During the year, no issues brought to the attention of the senior management and the Board were of sufficient significance for disclosure in the annual report.

The Audit Committee held three meetings in the year ended 31 December 2008 and one meeting to date in 2009. The attendance record of each member of the Audit Committee in 2008 is set out below:

Directors	**Attendance of Audit Committee Meetings in 2008**
Zhang Julin *(chairman)*	3/3
Jiao Shuge	3/3
Li Jianxin	3/3

Other than the reporting responsibilities of the Company's auditors (please refer to the auditors' report set out on pages 49-50), the directors acknowledge their responsibility for preparing the financial statements of the Group and the Company which give a true and fair view of the state of affairs of the Group and the Company as at 31 December 2008 and the profit and cash flows of the Group for the year then ended.

INTERNAL CONTROL

The Board is responsible for maintaining an established and effective internal control system, to safeguard the assets of the Group and the interest of shareholders, and for reviewing its effectiveness regularly. Aiming at strengthening the risk management culture of the Group and minimizing the impacts of the major risks on the business and earnings of the Group, the senior management of the Group meets to actively evaluate and review the significant risks to which the Group is exposed and reports to the Board on a regular basis. The Group also appoints external consultants, when considered appropriate, to review the Group's internal control, working systems and workflows, as well as the management systems, and to make suggestions on system enhancement.

Besides strict implementation of a performance assessment system and training programs for its staff, the Group has in place a series of written working systems in respect of business, production, finance, legal compliance and administration aspects, to ensure the significant risks, to which the Group is exposed, are contained:

– Control environment – The Group has established defined organizational structures. Authority to operate various business functions is delegated to respective management within limits set by senior management of the headquarters or the Executive Directors. The senior management meets on a regular basis to discuss and approve business strategies, plans and budgets prepared by individual business units. The performance of the Group is reported to the Board on a regular basis.

– Risk assessment – The Group identifies, assesses and ranks the risks that are most relevant to the Group's business according to their likelihood, financial consequence and reputational impact on the Group.

– Control activities – Policies and procedures are set for each business function, in which approvals, authorization, verification, recommendations, performance reviews, asset security and segregation of duties are included.

– Information and communication – The Group's working systems document operational procedures of all business units, as well as authorization and approval procedures for significant decision making.

– Monitoring – The Group adopts a control and risk self-assessment methodology, continuously assessing and managing its business risks by way of assessment by the headquarters of the Group and each business unit on a regular basis, and communication of key control procedures to employees.

To reinforce the internal control on the quality of the raw milk collected from the milk suppliers, stringent monitoring measures on milk collection process and the delivery of raw milk to our plants are in place. These included placing more staff and installing monitoring system at each milk collection centre to carry out on-site monitoring, installing global positioning system in the tankers to check the delivery process, as well as installing additional testing equipment to examine the quality of the raw milk collected. Details of which are set out in our Management Discussion and Analysis section of this annual report.

During the year ended 31 December 2008, the Board had examined the internal control system and reviewed the evaluation performed by the Audit Committee, the management and internal and external auditors, on the effectiveness of internal control. No significant areas of concern were identified.

EXTERNAL AUDITORS

The Group's independent external auditors are Ernst & Young. The Audit Committee is responsible for the appointment of the external auditors and reviewing the non-audit functions performed by the external auditors for the Group. In particular, the Committee will, prior to the execution of contract with external auditors and the commencement of their duties, consider whether the non-audit functions will result in any potential material conflict of interest.

Details of fees paid or payable to Ernst & Young for the year ended 31 December 2008 are as follows:

Services rendered	**2008** ***RMB'000***	2007 *RMB'000*
Annual audit	**3,250**	3,040
Interim review	**535**	486
	3,785	3,526

The Board is satisfied with the audit fees, process and effectiveness of Ernst & Young and has recommended their reappointment as the Company's external auditors at the forthcoming annual general meeting.

Corporate Governance Report

DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted, in terms no less exacting than, the standard required by the Model Code for Securities Transactions by Directors of Listed Issuers set out in Appendix 10 of the Listing Rules as the Company's code of conduct and rules governing dealings by all the directors in the securities of the Company ("Model Code"). Having made specific enquiry of all the directors, the Company confirms that, during the year ended 31 December 2008, all the directors have strictly complied with the Model Code.

INVESTOR RELATIONS AND COMMUNICATIONS

The Company adopts a proactive policy in promoting investor relations and communications. Regular meetings are held with institutional investors and financial analysts to ensure two-way communications on the Company's performance and development. When the Company announces its interim and annual results, briefings are conducted to apprise investors, analysts and the press of the Group's operating results as well as business strategies and outlook. Investor relations website is updated on a timely basis to ensure that investors are able to have access to the Company's information, latest news and reports. Eight out of the nine directors, including the Chairman, have attended the annual general meeting in May 2008 to be available to answer questions at the meeting.

Separate resolutions are proposed at general meetings for each substantially separate issue, including election of directors.

Details of voting procedures by way of a poll and rights of shareholders to demand a poll were included in the circular dispatched to the shareholders of the Company. The circular also included relevant details of proposed resolutions and biography of directors standing for re-election.

Report of the Directors

The board of directors (the "Directors") presents its report together with the audited financial statements of the Company and the Group for the year ended 31 December 2008.

PRINCIPAL ACTIVITIES AND ANALYSIS OF OPERATIONS

The principal activity of the Company is investment holding. The principal activities of the main Group's operating subsidiary, Inner Mongolia Mengniu Dairy (Group) Company Limited ("Inner Mongolia Mengniu"), and its subsidiaries are manufacturing and distribution of dairy products including liquid milk (comprising UHT milk, milk beverages and yogurt), ice cream and other dairy products (such as milk powder) in China, including Hong Kong and Macau.

Particulars of the Company's subsidiaries are set out in note 17 to the financial statements.

The Group's revenue is derived principally from business activities in China. An analysis of the Group's performance for the year ended 31 December 2008 by business segments is set out in note 3 to the financial statements.

RESULTS AND APPROPRIATIONS

The results of the Group for the year ended 31 December 2008 are set out in the consolidated income statement on page 51.

The Directors do not recommend the payment of any dividend for the year.

PROPERTY, PLANT AND EQUIPMENT

Details of the movements in the property, plant and equipment of the Group and the Company during the year are set out in note 13 to the financial statements.

RESERVES

Details of the movements in the reserves of the Group and of the Company during the year are set out in the consolidated statement of changes in equity on page 54 and note 38 to the financial statements. The Company's distributable reserves, calculated in accordance with statutory provisions applicable in the Company's place of incorporation, amounted to approximately RMB5,333,876,000 as at 31 December 2008 (2007: RMB2,966,963,000).

DONATIONS

Charitable and other donations made by the Group during the year amounted to approximately RMB20,050,000 (2007: RMB6,922,000).

SHARE CAPITAL AND SHARE OPTIONS

Details of movement in the Company's share capital and share options during the year are set out in notes 37 and 40 to the financial statements.

Report of the Directors

DIRECTORS

The Directors during the year and up to the date of this report were:

Executive Directors

Mr. NIU Gensheng
Mr. YANG Wenjun
Mr. SUN Yubin
Mr. YAO Tongshan (appointed on 15 July 2008)
Mr. BAI Ying (appointed on 15 July 2008)

Non-Executive Directors

Mr. JIAO Shuge (alias JIAO Zhen)
Mr. Julian Juul WOLHARDT

Independent Non-Executive Directors

Mr. WANG Huaibao
Mr. ZHANG Julin
Mr. LI Jianxin (passed away on 20 February 2009)

In accordance with Article 112 of the Company's articles of association, Mr. Yang Wenjun, Mr. Julian Juul Wolhardt and Mr. Zhang Julin, will retire by rotation and Mr. Yao Tongshan and Mr. Bai Ying will retire in accordance with the articles of association of the Company and, being eligible, offer themselves for re-election at the forthcoming annual general meeting.

The Company considers that Mr. Wang Huaibao and Mr. Zhang Julin are independent pursuant to the criteria set out in the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited ("Listing Rules") and that a confirmation of independence has been received from existing Independent Non-Executive Directors. The Company also considers Mr. Li Jianxin to be independent under the Listing Rules during his term of office.

Following the passing away of Mr. Li, the Company has only two independent non-executive directors and two audit committee members and accordingly does not have the requisite minimum number of independent non-executive directors and audit committee members (i.e. three) under the Listing Rules. The Company is in the process of and will as soon as possible within the time period under the Listing Rules appoint a suitable candidate to fill the vacancy.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

Brief biographical details of the Directors and the senior management are set out on pages 25 to 27.

DIRECTORS' SERVICE CONTRACTS

No director proposed for re-election at the forthcoming annual general meeting has service contract with the Company which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

DIRECTORS' INTERESTS IN CONTRACTS

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

DIRECTORS' INTERESTS, LONG AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES

As at 31 December 2008, the interests and short positions of the Directors and chief executives of the Company in the shares, underlying shares and debentures of the Company and any associated corporation (within the meaning of Part XV of the Securities and Futures Ordinance) ("SFO") as recorded in the register required to be kept under Section 352 of SFO or as otherwise notified to the Company and the Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to the Model Code for Securities Transactions by Directors of Listed Companies (the "Model Code") were as follows:

Long/short positions in shares of the Company/Associated Corporation:

Name of Director	Company/Name of Associated Corporation	Nature of Interest	Total Number of Ordinary Shares	Percentage of the Company's Issued Share Capital
Niu Gensheng	Company	Personal Interest	68,781,022 (L)	4.40%
	Company	Corporate Interest *(Note 1)*	256,499,966 (L)	16.43%
	Company	Interests under Concert Party Agreement *(Note 2)*	383,049,601 (L)	24.53%
	Inner Mongolia Mengniu	Personal Interest	37,156,995 (L)	4.63%
	Inner Mongolia Mengniu	Personal Interest	21,977,010 (S)	2.74%
Yang Wenjun	Company	Personal Interest	1,506,196 (L)	0.10%
	Company	Interests under Concert Party Agreement *(Note 2)*	383,049,601 (L)	24.53%
	Inner Mongolia Mengniu	Personal Interest	2,404,453 (L)	0.30%

Name of Director	Company/Name of Associated Corporation	Nature of Interest	Total Number of Ordinary Shares	Percentage of the Company's Issued Share Capital
Sun Yubin	Company	Personal Interest	2,498,444 (L)	0.16%
	Company	Interests under Concert Party Agreement *(Note 2)*	383,049,601 (L)	24.53%
	Inner Mongolia Mengniu	Personal Interest	3,988,453 (L)	0.50%
Bai Ying	Company	Personal Interest	148,837 (L)	0.01%
	Company	Interests under Concert Party Agreement *(Note 2)*	383,049,601 (L)	24.53%
	Inner Mongolia Mengniu	Personal Interest	237,600 (L)	0.03%

Notes:

1. 132,607,821 shares are held by Yinniu Milk Industry Limited ("Yinniu"), a substantial shareholder of the Company, which is controlled as to 81.3% by Xin Niu International Limited ("Xin Niu"). 123,892,145 shares are held by Jinniu Milk Industry Limited ("Jinniu"), a substantial shareholder of the Company, which is controlled as to 43.6% by Xin Niu. Niu Gensheng, by virtue of a proxy, has been delegated voting rights of the shares in Yinniu and Jinniu held by Xin Niu.

2. On 24 July 2008, Xin Niu, Yinniu, Jinniu, Niu Gensheng and a group of 21 individuals comprising Directors and management staff of the Group (the "Management Shareholders") (together, the "Concert Parties") entered into a concert party agreement (the "Concert Party Agreement") regarding their interest in the Company. The Concert Party Agreement constitutes an agreement under section 317 of the SFO. Details of the shareholding of the Concert Parties (who are not Directors of the Company) are set out in the section headed "Substantial Shareholders' Interests" below.

(L) Indicates a long position.
(S) Indicates a short position.

The Directors of the Company have been granted options under the Company's share option scheme, details of which are set out in the section "Share Option Scheme" below.

Save as disclosed above, as at 31 December 2008, none of the Directors and the Chief Executives of the Company had any interests and short positions in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO).

SUBSTANTIAL SHAREHOLDERS' INTERESTS

As at 31 December 2008, the interests or short positions of substantial shareholders, other than the Directors or the Chief Executives of the Company whose interests, long and short positions in the shares of the Company and of its associated corporations (within the meaning of Part XV of the SFO) are set out above, in the shares and underlying shares of the Company as recorded in the register required to be maintained under section 336 of the SFO were as follows:

Name of Substantial Shareholder	Number of Ordinary Shares	Percentage of Issued Share Capital
Xin Niu	256,499,966 (L) *(Note 1)*	16.43%
	383,049,601 (L) *(Note 2)*	24.53%
Yinniu	132,607,821 (L) *(Note 1)*	8.49%
	383,049,601 (L) *(Note 2)*	24.53%
Jinniu	123,892,145 (L) *(Note 1)*	7.93%
	383,049,601 (L) *(Note 2)*	24.53%
UBS AG	191,039,756 (L)	12.23%
	30,659,597 (S)	1.96%
J P Morgan Chase & Co	95,456,794 (L)	6.11%
	2,070,500 (S)	0.13%
	90,630,694 (P)	5.80%
Altman Jeffrey Alan	83,445,000 (L)	5.34%
OWL Creek GP, L.L.C.	83,445,000 (L)	5.34%
Deng Jiuqiang	383,049,601 (L) *(Note 2)*	24.53%
Lu Jun	383,049,601 (L) *(Note 2)*	24.53%
Sun Xianhong	383,049,601 (L) *(Note 2)*	24.53%
Wang Fuzhu	383,049,601 (L) *(Note 2)*	24.53%
Bai Jun	383,049,601 (L) *(Note 2)*	24.53%
Hou Jiangbin	383,049,601 (L) *(Note 2)*	24.53%
Qiu Lianjun	383,049,601 (L) *(Note 2)*	24.53%
Pang Kaitai	383,049,601 (L) *(Note 2)*	24.53%
Chu Xiuli	383,049,601 (L) *(Note 2)*	24.53%
Li Shurong	383,049,601 (L) *(Note 2)*	24.53%
Liu Xiaoling	383,049,601 (L) *(Note 2)*	24.53%
Wang Guisheng	383,049,601 (L) *(Note 2)*	24.53%
Wang Ai Suo	383,049,601 (L) *(Note 2)*	24.53%
Wang Jishan	383,049,601 (L) *(Note 2)*	24.53%
Wang Jianbang	383,049,601 (L) *(Note 2)*	24.53%
Jiang Hong	383,049,601 (L) *(Note 2)*	24.53%
Zheng Wenping	383,049,601 (L) *(Note 2)*	24.53%
Ren Meicheng	383,049,601 (L) *(Note 2)*	24.53%

Notes:

(1) 132,607,821 shares are held by Yinniu, a substantial shareholder of the Company, which is controlled as to 81.3% by Xin Niu. 123,892,145 shares are held by Jinniu, a substantial shareholder of the Company, which is controlled as to 43.6% by Xin Niu. Niu Gensheng, by virtue of a proxy, has been delegated voting rights of the shares in Yinniu and Jinniu held by Xin Niu.

(2) On 24 July 2008, Xin Niu, Yinniu, Jinniu, Niu Gensheng and the Management Shareholders entered into the Concert Party Agreement regarding their interest in the Company. The Concert Party Agreement constitutes an agreement under section 317 of the SFO and the aggregate number of shares under the Concert Party Agreement is 383,049,601, representing approximately 24.53% of the issued shares of the Company as at 31 December 2008. These shares are beneficially owned by Yinniu, Jinniu, Niu Gensheng, Yang Wenjun, Sun Yubin, Bai Ying (the shareholdings of these parties are set out in the table above or in the section headed "Directors' Interests, long and short position in shares, underlying shares and debentures") and Deng Jiuqiang (as to 2,753,636 shares), Lu Jun (as to 1,134,104 shares), Sun Xianhong (as to 1,118,060 shares), Wang Fuzhu (as to 704,721 shares), Bai Jun (as to 570,542 shares), Hou Jiangbin (as to 9,447,321 shares), Qiu Lianjun (as to 9,001,526 shares), Pang Kaitai (as to 2,232,558 shares), Chu Xiuli (as to 2,181,818 shares), Li Shurong (as to 2,029,598 shares), Liu Xiaoling (as to 2,029,598 shares), Wang Guisheng (as to 1,587,596 shares), Wang Ai Suo (as to 2,282,170 shares), Wang Jishan (as to 2,946,976 shares), Wang Jianbang (as to 676,533 shares), Jiang Hong (as to 507,399 shares), Zheng Wenping (as to 9,894,289 shares) and Ren Meicheng (as to 2,516,691 shares).

(S) Indicates a short position.
(L) Indicates a long position.
(P) Indicates a lending position.

Saved as disclosed above and in the section "Share Option Scheme" below, as at 31 December 2008, no other interests or short position in the shares or underlying shares of the Company were recorded in the register maintained under section 336 of the SFO.

CONNECTED TRANSACTIONS

On 8 April 2008, the Company entered into an Equity Interest Transfer Agreement with certain sellers (the "Sellers"), pursuant to which the Company has conditionally agreed to acquire approximately 8.97% of the equity interest in Inner Mongolia Mengniu, the main operating subsidiary of the Company, by allotting and issuing 135,328,255 ordinary shares of the Company (the "Consideration Shares") to the Sellers. As some of the Sellers are connected persons of the Company, the acquisition was constituted a connected transaction of the Company. Details of the acquisition were disclosed in the Company's announcement dated 8 April 2008. The acquisition was completed during the year and the Consideration Shares were issued on 25 July 2008 to the Sellers accordingly.

Saved as disclosed above, there were no other transactions which need to be disclosed as connected transactions in accordance with the requirements of the Listing Rules.

The Company has complied with relevant requirements under Chapter 14A of the Listing Rules.

SHARE OPTION SCHEME

The Company operates a share option scheme (the "Scheme") for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. The following share options were outstanding under the Scheme during the year.

Name or Category of Participant	Number of share options: As at 1 January 2008	Granted during the year	Exercised during the year	Lapsed during the year	As at 31 December 2008	Date of grant of share options	Exercise Period of share options (both dates inclusive)[2]	Exercise price of share options
								HK$
Executive directors								
Yang Wenjun[1]	4,561,000	–	–	–	4,561,000	9.11.2007	9.11.2009 to 8.11.2013	32.24
	–	9,000,000	–	–	9,000,000	18.8.2008	18.8.2010 to 17.8.2014	22.03[3]
Sun Yubin[1]	1,875,000	–	–	–	1,875,000	9.11.2007	9.11.2009 to 8.11.2013	32.24
	–	1,680,000	–	–	1,680,000	18.8.2008	18.8.2010 to 17.8.2014	22.03[3]
Yao Tongshan	1,659,000	–	–	–	1,659,000	9.11.2007	9.11.2009 to 8.11.2013	32.24
	–	1,000,000	–	–	1,000,000	18.8.2008	18.8.2010 to 17.8.2014	22.03[3]
Bai Ying[1]	137,000	–	–	–	137,000	26.10.2006	26.10.2007 to 25.10.2012	13.4
	2,277,000	–	–	–	2,277,000	9.11.2007	9.11.2009 to 8.11.2013	32.24
	–	3,680,000	–	–	3,680,000	18.8.2008	18.8.2010 to 17.8.2014	22.03[3]
Employees in Aggregate[1]	6,117,561	–	(192,065)	(610,095)	5,315,401	26.10.2006	26.10.2007 to 25.10.2012	13.4
	34,233,000	–	–	(1,473,000)	32,760,000	9.11.2007	9.11.2009 to 8.11.2013	32.24
	–	65,180,000	–	(1,422,000)	63,758,000	18.8.2008	18.8.2010 to 17.8.2014	22.03[3]
	50,859,561	80,540,000	(192,065)	(3,505,095)	127,702,401			

(1) Xin Niu, Yinniu, Jinniu and the Management Shareholders entered into the Concert Party Agreement on 24 July 2008 and accordingly, Xin Niu, Yinniu, Jinniu and the Management Shareholders (who include Yang Wenjun, Sun Yubin and Bai Ying) were all deemed to be interested in an aggregate of 27,261,000 share options in the Company under the SFO as at 31 December 2008.

(2) The exercise period of the share options granted commences after a certain vesting period and the fulfilment of certain performance targets, and ends on a date which is not later than six years from the date of grant of such options. Further details of the share option scheme are set out in note 40 to the financial statements.

(3) The closing price of the Company's shares immediately before the date of granted (i.e. 18 August 2008) was HK$22.

Subsequent to the balance sheet date, 2,280,500, 937,500, 829,500, 1,172,750 and 17,878,000 units granted to Yang Wenjun, Sun Yubin, Yao Tongshan, Bai Ying, and other employees, respectively, of share option were lapsed due to the unfullfillment of vesting conditions attached.

The values of share options calculated using the binomial model are subject to certain fundamental limitations, due to the subjective nature of and uncertainty relating to a number of assumptions of the expected future performance input to the model, and certain inherent limitations of the model itself. Details of the valuation are set out in note 40 to the financial statements.

The value of an option varies with different variables of certain subjective assumptions. Any change to the variables used may materially affect the estimation of the fair value of an option.

PRE-EMPTIVE RIGHTS

There is no provision for pre-emptive rights under the Company's articles of association or the laws of the Cayman Islands which would oblige the Company to offer new shares on a pro rata basis to its existing shareholders.

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

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

PUBLIC FLOAT

As at the date of this report, the Company has maintained the prescribed public float under the Listing Rules, based on the information that is publicly available to the Company and within the knowledge of the Directors.

MANAGEMENT CONTRACTS

No contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

MAJOR CUSTOMERS AND SUPPLIERS

The percentage of purchases attributable to the five largest suppliers of the Group combined was less than 30% of the total purchases of the Group.

The percentage of revenue attributable to the five largest customers of the Group combined was less than 30% of the total revenue of the Group.

PLEDGE OF ASSETS

As at 31 December 2008, the Group pledged certain bank deposits, bills receivable and certain property, plant and equipment aggregating to approximately RMB559,782,000 (2007: RMB766,584,000). Details are set out in respective notes to the financial statements.

CONTINGENT LIABILITIES AND COMMITMENTS

Details of contingent liabilities and commitments are set out in notes 42 and 41 to the financial statements.

FINANCIAL SUMMARY

A summary of the results for the year and of the assets and liabilities of the Group as at 31 December 2008 and for the previous four financial periods are set out on page 140.

CORPORATE GOVERNANCE

The Company's corporate governance principles and practices are set out in the Corporate Governance Report on pages 30 to 38.

AUDITORS

The financial statements have been audited by Ernst & Young. A resolution for the re-appointment of Ernst & Young as auditors of the Company will be proposed at the forthcoming annual general meeting.

By order of the Board of Directors
Niu Gensheng
Chief Executive Officer

Hong Kong, 16 April 2009

Corporate Information

BOARD OF DIRECTORS

Executive Directors

Mr NIU Gensheng
Mr YANG Wenjun
Mr SUN Yubin
Mr YAO Tongshan (appointed on 15 July 2008)
Mr BAI Ying (appointed on 15 July 2008)

Non-Executive Directors

Mr JIAO Shuge (alias JIAO Zhen)
Mr Julian Juul WOLHARDT

Independent Non-Executive Directors

Mr WANG Huaibao
Mr ZHANG Julin
Mr LI Jianxin (passed away on 20 February 2009)

SENIOR MANAGEMENT

Mr BAI Jun
Mr LEI Yongsheng
Mr YAO Haitao
Ms ZHAO Yuanhua
Mr DING Sheng
Mr WU Jingshui
Mr KWOK Wai Cheong, Chris
(Qualified Accountant & Company Secretary)

STOCK CODE

Hong Kong Stock Exchange 2319

INVESTOR RELATIONS CONTACT

Mr KWOK Wai Cheong, Chris
Unit 1001, 10th Floor, Jubilee Centre
18 Fenwick Street, Wanchai
Hong Kong
Email: mengniu_ir@mengniu.com.cn
Website: www.mengniuir.com

PLACE OF BUSINESS IN HONG KONG

Unit 1001, 10th Floor, Jubilee Centre
18 Fenwick Street, Wanchai
Hong Kong

REGISTERED OFFICE

M&C Corporate Service, P.O. Box 309 GT
Ugland House, South Church Street
George Town, Grand Cayman
Cayman Islands

PRINCIPAL SHARE REGISTRAR

Butterfield Fund Services (Cayman) Limited
Butterfield House
68 Fort Street
P.O. Box 705, George Town
Grand Cayman, Cayman Islands

HONG KONG BRANCH SHARE REGISTRAR

Computershare Hong Kong Investor Services Limited
46th Floor, Hopewell Centre
183 Queen's Road East, Wanchai
Hong Kong

LEGAL ADVISORS

As to Hong Kong Law
Norton Rose

As to Cayman Islands Law
Maples and Calder Asia

PRINCIPAL BANKERS

Agricultural Bank of China
Bank of China
Industrial Commercial Bank of China
BNP Paribas

AUDITORS

Ernst & Young

INVESTOR RELATIONS CONSULTANT

Strategic Financial Relations (China) Limited

ERNST & YOUNG
安 永

To the shareholders of China Mengniu Dairy Company Limited (the "Company")
(Incorporated in the Cayman Islands with limited liability)

We have audited the financial statements of the Company set out on pages 51 to 139, which comprise the consolidated and company balance sheets as at 31 December 2008, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

DIRECTORS' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

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

AUDITORS' RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit. Our report is made solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

To the shareholders of China Mengniu Dairy Company Limited (the "Company")
(Incorporated in the Cayman Islands with limited liability)

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

OPINION

In our opinion, the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2008 and of the Group's loss and cash flows for the year then ended in accordance with International Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Ernst & Young
Certified Public Accountants

18th Floor
Two International Finance Centre
8 Finance Street, Central
Hong Kong

16 April 2009

Consolidated Income Statement

For the year ended 31 December 2008

	Notes	2008 RMB'000	2007 RMB'000
CONTINUING OPERATIONS			
REVENUE	4	**23,864,975**	21,318,062
Cost of sales		**(19,195,576)**	(16,514,557)
GROSS PROFIT		**4,669,399**	4,803,505
Other income and gains	4	**122,654**	98,096
Selling and distribution costs		**(4,428,027)**	(3,302,020)
Administrative expenses		**(622,162)**	(461,902)
Other operating expenses	5	**(876,033)**	(21,829)
PROFIT/(LOSS) FROM OPERATING ACTIVITIES		**(1,134,169)**	1,115,850
Interest income		**54,841**	43,566
Finance costs	8	**(39,394)**	(50,060)
Share of profits and losses of associates		**29,447**	20,954
PROFIT/(LOSS) BEFORE TAX	6	**(1,089,275)**	1,130,310
Income tax income/(expense)	9	**161,454**	(21,658)
PROFIT/(LOSS) FOR THE YEAR FROM CONTINUING OPERATIONS		**(927,821)**	1,108,652
DISCONTINUED OPERATION			
Profit for the year from a discontinued operation	10	**3,357**	–
PROFIT/(LOSS) FOR THE YEAR		**(924,464)**	1,108,652
Attributable to:			
Equity holders of the Company		**(948,600)**	935,786
Non-controlling/minority interests		**24,136**	172,866
		(924,464)	1,108,652
DIVIDENDS			
Dividends paid	11	**187,667**	156,020
Proposed final dividend	11	**–**	187,535
EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY (EXPRESSED IN RMB PER SHARE)			
Basic			
– For profit/(loss) for the year	12	**(0.639)**	0.664
– For profit/(loss) from continuing operations		**(0.641)**	0.664
– For profit from a discontinued operation		**0.002**	N/A
Diluted			
– For profit for the year		**N/A**	0.664
– For profit from continuing operations		**N/A**	0.664
– For profit from a discontinued operation		**0.002**	N/A

Consolidated Balance Sheet

As at 31 December 2008

	Notes	2008 RMB'000	2007 RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment	13	**5,247,072**	5,042,648
Construction in progress	14	**215,017**	313,439
Other intangible assets	15	**32,667**	31,404
Land use rights	16	**256,524**	228,739
Interests in associates	18	**40,107**	57,573
Available-for-sale investments	20	**18,029**	17,316
Goodwill	21	**199,143**	199,143
Deferred tax assets	22	**186,881**	6,302
Other financial assets	23	**18,333**	21,139
		6,213,773	5,917,703
CURRENT ASSETS			
Inventories	24	**824,453**	877,443
Bills receivable	25	**64,778**	114,882
Trade receivables	26	**284,079**	261,365
Prepayments and deposits	27	**374,904**	214,364
Other receivables	28	**90,679**	40,198
Pledged deposits	29	**41,693**	44,506
Cash and bank balances	29	**3,041,965**	2,210,818
		4,722,551	3,763,576
Assets of a disposal group classified as held for sale	10	**378,951**	–
		5,101,502	3,763,576
CURRENT LIABILITIES			
Trade payables	30	**2,155,265**	1,315,395
Bills payable	31	**239,345**	259,065
Deferred income	36	**12,918**	11,752
Accruals and customers' deposits	32	**745,535**	544,662
Other payables		**1,048,792**	1,013,171
Interest-bearing bank loans	33	**1,208,660**	183,156
Other loans	34	**72,942**	36,004
Income tax payable		**–**	185
		5,483,457	3,363,390
Liabilities directly associated with assets classified as held for sale	10	**282,649**	–
		5,766,106	3,363,390
NET CURRENT ASSETS/(LIABILITIES)		**(664,604)**	400,186
TOTAL ASSETS LESS CURRENT LIABILITIES		**5,549,169**	6,317,889

	Notes	2008 RMB'000	2007 RMB'000
NON-CURRENT LIABILITIES			
Interest-bearing bank loans	33	**520,000**	80,000
Long term payables	35	**107,988**	224,192
Deferred income	36	**183,210**	178,993
		811,198	483,185
NET ASSETS		**4,737,971**	5,834,704
EQUITY			
Equity attributable to equity holders of the Company			
Issued capital	37	**163,137**	151,277
Retained earnings		**363,555**	1,547,733
Other reserves	38(A)	**3,937,924**	3,412,619
		4,464,616	5,111,629
Non-controlling/minority interests		**273,355**	723,075
TOTAL EQUITY		**4,737,971**	5,834,704

Niu Gensheng
Director

Jiao Shuge
Director

Consolidated Statement of Changes in Equity

For the year ended 31 December 2008

		Attributable to equity holders of the Company					
	Notes	Issued capital RMB'000	Other reserves RMB'000 Note 38(A)	Retained earnings RMB'000	Total RMB'000	Non-controlling/ minority interests RMB'000	Total equity RMB'000
At 1 January 2007		145,573	1,859,469	993,822	2,998,864	633,816	3,632,680
Profit for the year		–	–	935,786	935,786	172,866	1,108,652
Currency translation differences		–	(57,529)	–	(57,529)	–	(57,529)
Total income and expense for the year		–	(57,529)	935,786	878,257	172,866	1,051,123
Issue of shares	37	5,682	1,342,547	–	1,348,229	–	1,348,229
Shares issued under equity-settled share option arrangements	40	22	3,044	–	3,066	–	3,066
Equity-settled share option arrangements	40	–	39,233	–	39,233	–	39,233
Transfer to statutory reserves		–	225,855	(225,855)	–	–	–
Dividends paid to minority shareholders		–	–	–	–	(32,801)	(32,801)
Dividends paid to equity holders of the Company	11	–	–	(156,020)	(156,020)	–	(156,020)
Acquisition of minority interests		–	–	–	–	(50,806)	(50,806)
At 1 January 2008		**151,277**	**3,412,619**	**1,547,733**	**5,111,629**	**723,075**	**5,834,704**
Profit/(loss) for the year		**–**	**–**	**(948,600)**	**(948,600)**	**24,136**	**(924,464)**
Currency translation differences		**–**	**(81,614)**	**–**	**(81,614)**	**–**	**(81,614)**
Total income and expense for the year		**–**	**(81,614)**	**(948,600)**	**(1,030,214)**	**24,136**	**(1,006,078)**
Issue of shares for acquisition of additional interest in a subsidiary	37	**11,843**	**422,141**	**–**	**433,984**	**(433,984)**	**–**
Shares issued under equity-settled share option arrangements	40	**17**	**2,245**	**–**	**2,262**	**–**	**2,262**
Equity-settled share option arrangements	40	**–**	**134,622**	**–**	**134,622**	**–**	**134,622**
Transfer to statutory reserves		**–**	**47,911**	**(47,911)**	**–**	**–**	**–**
Dividends paid to non-controlling shareholders		**–**	**–**	**–**	**–**	**(44,672)**	**(44,672)**
Dividends paid to equity holders of the Company	11	**–**	**–**	**(187,667)**	**(187,667)**	**–**	**(187,667)**
Capital injection from non-controlling shareholders		**–**	**–**	**–**	**–**	**4,800**	**4,800**
At 31 December 2008		**163,137**	**3,937,924**	**363,555**	**4,464,616**	**273,355**	**4,737,971**

Consolidated Statement of Cash Flows

For the year ended 31 December 2008

	Notes	2008 RMB'000	2007 RMB'000
Cash flows from operating activities			
Profit/(loss) before tax			
From continuing operations		**(1,089,275)**	1,130,310
From discontinued operation		**3,357**	–
Adjustments for:			
Interest income		**(54,841)**	(43,566)
Finance costs	8	**39,394**	50,060
Depreciation of property, plant and equipment	6	**630,046**	522,706
Amortisation of land use rights	6	**5,604**	4,681
Amortisation of other intangible assets	6	**4,050**	3,088
Loss on disposal of items of property, plant and equipment	5	**6,227**	8,298
Share-based payment expense	40	**134,622**	39,233
Write-back of provision against trade receivables and other receivables	6	**(1,711)**	(7,903)
Share of profits and losses of associates		**(29,447)**	(20,954)
Profit for the year from a discontinued operation		**(3,357)**	–
Write-down of inventories to net realisable value	5	**179,873**	4,413
Amortisation of deferred income	4	**(12,545)**	(10,816)
Foreign exchange differences, net	4	**(65,825)**	(38,822)
		(253,828)	1,640,728
Increase in other financial assets		**(13,135)**	(37,867)
Decrease/(increase) in inventories		**(125,278)**	189,604
Decrease/(increase) in trade and bills receivables		**29,467**	(53,372)
Decrease in pledged deposits		**2,813**	565
Increase in prepayments, deposits and other receivables		**(102,616)**	(39,574)
Increase in trade and bills payables		**817,024**	252,268
Increase in accruals and other payables		**318,297**	174,736
Cash generated from operations		**672,744**	2,127,088
Interest paid		**(22,925)**	(35,088)
Income taxes paid		**(62,939)**	(33,879)
Net cash inflow from operating activities		**586,880**	2,058,121

Consolidated Statement of Cash Flows

For the year ended 31 December 2008

	Notes	2008 RMB'000	2007 RMB'000
Cash flows from investing activities			
Proceeds from disposal of items of property, plant and equipment		**10,234**	2,554
Purchases of items of property, plant and equipment		**(290,484)**	(503,039)
Purchases of construction in progress	14	**(497,862)**	(819,117)
Purchase of other intangible assets	15	**(5,313)**	(21,288)
Purchase of land use rights	16	**(34,582)**	(107,178)
Disposal/(purchase) of available-for-sale investments		**538**	(2,000)
Acquisition of minority interests		**–**	(120,960)
Acquisition of a subsidiary with a view to resale	10	**(89,661)**	–
Capital injection to associates		**(1,350)**	(1,055)
Capital injection to a jointly-controlled entity		**(80,000)**	(15,000)
Receipt of government grants	36	**17,928**	73,173
Dividends received from a discontinued operation		**22,750**	–
Purchase of time deposits with original maturity of more than three months		**(369,000)**	(304,000)
Interest received		**54,841**	43,566
Dividends received from associates		**12,152**	4,807
Net cash outflow from investing activities		**(1,249,809)**	(1,769,537)
Cash flows from financing activities			
Proceeds from interest-bearing bank loans		**1,674,498**	282,632
Repayment of interest-bearing bank loans		**(206,021)**	(889,494)
Dividends paid to equity holders of the Company	11	**(187,667)**	(156,020)
Dividends paid to minority shareholders		**(39,872)**	(32,801)
Proceeds from other loans		**72,942**	9,504
Repayment of other loans		**(36,004)**	(4,500)
Repayment of long term payables		**(202,962)**	(236,096)
Capital contribution by the joint venture partner		**80,000**	15,000
Proceeds from issuance of new shares	37	**–**	1,363,526
Shares issued under the employee share option scheme		**2,262**	3,066
Share issue costs		**(2,130)**	(15,297)
Net cash inflow from financing activities		**1,155,046**	339,520
Net increase in cash and cash equivalents		**492,117**	628,104
Cash and cash equivalents at beginning of year	29	**1,756,818**	1,180,058
Effect of foreign exchange rate changes, net		**(29,970)**	(51,344)
Cash and cash equivalents at end of year	29	**2,218,965**	1,756,818
Analysis of balances of cash and cash equivalents			
Cash and bank balances	29	**2,218,965**	1,756,818

Balance Sheet

As at 31 December 2008

	Notes	2008 RMB'000	2007 RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment	13	**48**	65
Interests in subsidiaries	17	**4,524,581**	1,682,872
		4,524,629	1,682,937
CURRENT ASSETS			
Dividends receivable		**75,915**	193,060
Prepayments, deposits and other receivables	28	**955,284**	281,151
Cash and cash equivalents	29	**54,058**	737,085
Interest in a subsidiary with a view to resale	10, 17	**67,004**	–
		1,152,261	1,211,296
CURRENT LIABILITIES			
Accruals and other payables		**2,914**	1,665
		2,914	1,665
NET CURRENT ASSETS		**1,149,347**	1,209,631
NET ASSETS		**5,673,976**	2,892,568
EQUITY			
Issued capital	37	**163,137**	151,277
Reserves	38(B)	**5,510,839**	2,741,291
TOTAL EQUITY		**5,673,976**	2,892,568

Niu Gensheng
Director

Jiao Shuge
Director

Notes to Financial Statements

1. CORPORATE INFORMATION

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

2.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs") and the disclosure requirements of the Hong Kong Companies Ordinance. They are prepared on a historical cost basis except for share options which have been measured at fair value. They are presented in Renminbi ("RMB") and all values are rounded to the nearest thousand except when otherwise indicated.

Basis of consolidation

The consolidated financial statements comprise the financial statements of the Company and its subsidiaries (collectively referred to as the "Group") for the year ended 31 December 2008. The financial statements of the subsidiaries are prepared for the same reporting year as the Company, using consistent accounting policies. All income and expenses and unrealised gains and losses resulting from intra-group transactions are eliminated in full. Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the day that such control ceases.

The acquisition of subsidiaries during the year has been accounted for using the purchase method of accounting. This method involves allocating the cost of the business combinations by recognising the identifiable assets acquired, and liabilities and contingent liabilities assumed at the date of acquisition at their fair value, except for non-current assets (or disposal groups) that are classified as held for sale at the acquisition date in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*, which should be recognised at fair value less costs to sell. The cost of the acquisition is measured at the aggregate of the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange.

Non-controlling or minority interests are the equity in subsidiaries not attributable, directly or indirectly, to the Company. An acquisition of non-controlling or minority interests is accounted for using the entity concept method whereby the difference between the consideration and the book value of the share of the net assets acquired is recognised as an equity transaction.

Basis of presentation

The Group has reported a net loss for the year ended 31 December 2008 and, as at that date, it had net current liabilities. The deterioration of the Group's financial performance and position during the year has resulted from the milk contamination incident that occurred in September 2008. In preparing the consolidated financial statements, the directors of the Company have given careful consideration to the future liquidity of the Group. After making an assessment of the Group's financial performance, working capital and liquidity position, the directors are of the view that the Group will be able to meet in full its financial obligations as they fall due for the foreseeable future. Accordingly, the consolidated financial statements have been prepared on a going concern basis.

2.2 IMPACT OF NEW AND REVISED IFRSs

The Group has adopted the following new interpretations and amendments to IFRSs for the first time for the current year's financial statements:

IAS 39 and IFRS 7 Amendments	Amendments to IAS 39 *Financial Instruments: Recognition and Measurement* and IFRS 7 *Financial Instruments: Disclosures – Reclassification of Financial Assets*
IFRIC 11	IFRS 2 – *Group and Treasury Share Transactions*
IFRIC 12	*Service Concession Arrangements*
IFRIC 14	IAS 19 – *The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*

The adoption of these new interpretations and amendments has had no significant effect on these financial statements.

The Group has early adopted IFRS 3 (as revised in 2008) *Business Combinations* ("IFRS 3R") and IAS 27 (as revised in 2008) *Consolidated and Separate Financial Statements* (as amended in 2008) ("IAS 27R") as of 1 January 2008.

IFRS 3R introduces a number of changes in the accounting for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009. The Group early adopted IFRS 3R on a prospective basis to business combination for which the acquisition date is on or after 1 January 2008. The Group chooses to account for the non-controlling interests (previously the minority interests) in the acquiree at fair value for the business combination during the year.

IAS 27R requires that a change in the ownership interest of a subsidiary without loss of control is accounted for as an equity transaction. Therefore, such a change will have no impact on goodwill, nor will it give rise to a gain or loss. Furthermore, the revised standard changes the accounting for losses incurred by the subsidiary as well as the loss of control of a subsidiary. The changes introduced by IAS 27R will affect future transactions with minority interests.

2.3 IMPACT OF ISSUED BUT NOT YET EFFECTIVE IFRSs

The Group has not applied the following new and revised IFRSs, that have been issued but are not yet effective, in these financial statements.

IFRS 1 (Revised)	*First-time Adoption of International Financial Reporting Standard*[2]
IFRS 1 and IAS 27 Amendments	Amendments to IFRS 1 *First-time Adoption of IFRSs* and IAS 27 *Consolidated and Separate Financial Statements – Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate*[1]
IFRS 2 Amendments	Amendments to IFRS 2 *Share-based Payment – Vesting Conditions and Cancellations*[1]
IFRS 7 Amendments	Amendments to IFRS 7 *Financial Instruments Disclosures-Improving Disclosures about Financial Instruments*[1]
IFRS 8	*Operating Segments*[1]
IAS 1 (Revised)	*Presentation of Financial Statements*[1]
IAS 23 (Revised)	*Borrowing Costs*[1]
IAS 32 and IAS 1 Amendments	Amendments to IAS 32 *Financial Instruments: Presentation* and IAS 1 *Presentation of Financial Statements – Puttable Financial Instruments and Obligations Arising on Liquidation*[1]
IAS 39 Amendment	Amendment to IAS 39 *Financial Instruments: Recognition and Measurement – Eligible Hedged Items*[2]
IFRIC 9 and IAS 39 Amendments	Amendments to IFRIC 9 – *Reassessment of Embedded Derivatives* and IAS 39 *Financial Instruments Recognition and Measurement – Embedded Derivatives*[3]
IFRIC 13	*Customer Loyalty Programmes*[3]
IFRIC 15	*Agreements for the Construction of Real Estate*[1]
IFRIC 16	*Hedges of a Net Investment in a Foreign Operation*[4]
IFRIC 17	*Distribution of Non-cash Assets to Owners*[2]
IFRIC 18	*Transfers of Assets from Customers*[5]

Apart from the above, the International Accounting Standards Board has issued Improvements to IFRSs* which sets out amendments to a number of IFRSs primarily with a view to removing inconsistencies and clarifying wording. Except for the amendment to IFRS 5 which is effective for annual periods on or after 1 July 2009, other amendments are effective for annual periods beginning on or after 1 January 2009 although there are separate transitional provisions for each standard.

1 Effective for annual periods beginning on or after 1 January 2009
2 Effective for annual periods beginning on or after 1 July 2009
3 Effective for annual periods beginning on or after 1 July 2008
4 Effective for annual periods beginning on or after 1 October 2008
5 Effective for transfers of assets from customers received on or after 1 July 2009

* Improvements to IFRSs contains amendments to IFRS 5, IFRS 7, IAS 1, IAS 8, IAS 10, IAS 16, IAS 18, IAS 19, IAS 20, IAS 23, IAS 27, IAS 28, IAS 29, IAS 31, IAS 34, IAS 36, IAS 38, IAS 39, IAS 40 and IAS 41.

2.3 IMPACT OF ISSUED BUT NOT YET EFFECTIVE IFRSs *(continued)*

IFRS 1 (Revised) has an improved structure that does not contain any changes to the substance of accounting and this standard does not apply to the Group as the Group is not a first-time adopter of IFRSs.

The IAS 27 Amendment requires all dividends from subsidiaries, associates or jointly-controlled entities to be recognised in the income statement in the separate financial statements. The amendment is applied prospectively only. The IFRS 1 Amendment allows a first-time adopter of IFRSs to measure its investment in subsidiaries, associates or jointly-controlled entities using a deemed cost of either fair value or the carrying amount under the previous accounting practice in the separate financial statements. The Group expects to adopt the IAS 27 Amendment from 1 January 2009. The amendments have no impact on the consolidated financial statements. As the Group is not a first-time adopter of IFRSs, the IFRS 1 Amendment is not applicable to the Group.

The IFRS 2 Amendments clarify that vesting conditions are service conditions and performance conditions only. Any other conditions are non-vesting conditions. Where an award does not vest as a result of a failure to meet a non-vesting condition that is within the control of either the entity or the counterparty, this is accounted for as a cancellation. The Group has not entered into any share-based payment schemes with non-vesting conditions attached and, therefore, the amendments are unlikely to have any financial impact on the Group.

The amendments to IFRS 7 are made to enhance disclosures about fair value measurement and liquidity risk, and do not have any financial impact on the Group.

IFRS 8, which will replace IAS 14 *Segment Reporting*, specifies how an entity should report information about its operating segments, based on information about the components of the entity that is available to the chief operating decision maker for the purposes of allocating resources to the segments and assessing their performance. The standard also requires the disclosure of information about the products and services provided by the segments, the geographical areas in which the Group operates, and revenue from the Group's major customers. The Group expects to adopt IFRS 8 from 1 January 2009.

IAS 1 (Revised) introduces changes in the presentation and disclosures of financial statements. The revised standard separates owner and non-owner changes in equity. The statement of changes in equity will include only details of transactions with owners, with all non-owner changes in equity presented as a single line. In addition, this standard introduces the statement of comprehensive income, with all items of income and expense recognised in profit or loss, together with all other items of recognised income and expense recognised directly in equity, either in one single statement, or in two linked statements. The Group expects to adopt IAS 1 (Revised) from 1 January 2009.

IAS 23 has been revised to require capitalisation of borrowing costs when such costs are directly attributable to the acquisition, construction or production of a qualifying asset. As the Group's current policy for borrowing costs aligns with the requirements of the revised standard, the revised standard is unlikely to have any financial impact on the Group.

2.3 IMPACT OF ISSUED BUT NOT YET EFFECTIVE IFRSs *(continued)*

The IAS 32 Amendments provide a limited scope exception for puttable financial instruments and instruments that impose specified obligations arising on liquidation to be classified as equity if they fulfil a number of specified features. IAS 1 Amendments require disclosure of certain information relating to these puttable financial instruments and obligations classified as equity. As the Group currently has no such financial instruments or obligations, the amendments are unlikely to have any financial impact on the Group.

The amendment to IAS 39 addresses the designation of a one-sided risk in a hedged item, and the designation of inflation as a hedged risk or portion in particular situations. It clarifies that an entity is permitted to designate a portion of the fair value changes or cash flow variability of a financial instrument as hedged item. As the Group has not entered into any such hedges, the amendment is unlikely to have any financial impact on the Group.

The amendments to IFRIC 9 and IAS 39 are made in response to the earlier amendments to IAS 39 and IFRS 7 regarding reclassification of financial assets. As the Group has not reclassified hybrid financial instruments in accordance with the October 2008 amendments to IAS 39, the amendments are unlikely to have any financial impact on the Group.

IFRIC 13 requires customer loyalty award credits to be accounted for as a separate component of the sales transaction in which they are granted. The consideration received in the sales transaction is allocated between the loyalty award credits and the other components of the sale. The amount allocated to the loyalty award credits is determined by reference to their fair value and is deferred until the awards are redeemed or the liability is otherwise extinguished. As the Group currently has no customer loyalty award scheme, the interpretation is not applicable to the Group and therefore is unlikely to have any financial impact on the Group.

IFRIC 15 clarifies when and how an agreement for the construction of real estate should be accounted for as a construction contract in accordance with IAS 11 *Construction Contracts* or an agreement for the sale of goods or services in accordance with IAS 18 *Revenue*. As the Group currently has no such agreement for the constructions of real estate, the interpretation is unlikely to have any financial impact on the Group.

IFRIC 16 provides guidance on the accounting for a hedge of a net investment in a foreign operation. This includes clarification that (i) hedge accounting may be applied only to the foreign exchange differences arising between the functional currencies of the foreign operation and the parent entity; (ii) a hedging instrument may be held by any entities within a group; and (iii) on disposal of a foreign operation, the cumulative gain or loss relating to both the net investment and the hedging instrument that was determined to be an effective hedge should be reclassified to the income statement as a reclassification adjustment. As the Group currently has no hedge of a net investment in a foreign operation, the interpretation is unlikely to have any financial impact on the Group.

2.3 IMPACT OF ISSUED BUT NOT YET EFFECTIVE IFRSs *(continued)*

IFRIC 17 standardises practice in the accounting for non-reciprocal distributions of non-cash assets to owners. The interpretation clarifies that (i) a dividend payable should be recognised when the dividend is appropriately authorised and is no longer at the discretion of the entity; (ii) an entity should measure the dividend payable at the fair value of the net assets to be distributed; and (iii) an entity should recognise the difference between the dividend paid and the carrying amount of the net assets distributed in profit or loss. Other consequential amendments were made to IAS 10 *Events after the Reporting Period* and IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*. The Group expects to apply the interpretation from 1 January 2010 prospectively. While the adoption of the interpretation may result in changes in certain accounting policies, the interpretation is unlikely to have any significant financial impact on the Group.

IFRIC 18 applies to all entities that receive from customers of an item of property, plants and equipments or cash for the acquisition or construction of such items. These assets must then be used to connect the customer to a network or to provide ongoing access to a supply of goods or services, or both. The Interpretation is applied prospectively. As the Group did not receive from customers such assets, the Interpretation is unlikely to have any financial impact on the Group.

In May 2008, the IASB issued its first *Improvements to IFRSs* which sets out amendments to a number of IFRSs. The Group expects to adopt the amendments from 1 January 2009 except for the amendment to IFRS 5 which is effective for annual periods on or after I July 2009. There are separate transitional provisions for each standard. While the adoption of some of the amendments may result in changes in accounting policies, none of these amendments are expected to have a significant financial impact on the Group.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Subsidiaries

A subsidiary is an entity whose financial and operating policies the Company controls, directly or indirectly, so as to obtain benefits from its activities. The results of subsidiaries are included in the Company's income statement to the extent of dividends received and receivable. The Company's interests in subsidiaries are stated at cost less any impairment losses.

Associates

An associate is an entity in which the Group has significant influence and which is neither a subsidiary nor a jointly controlled entity. The Group's interests in associates are accounted for under the equity method of accounting. Under the equity method, the investments in associates are carried in the balance sheet at cost plus post-acquisition changes in the Group's share of net assets of the associates. After application of the equity method, the Group determines whether it is necessary to recognise any additional impairment loss with respect to the Group's net investment in the associates. The consolidated income statement reflects the Group's share of the results of the operations of the associates. When there has been a change recognised directly in the equity of the associates, the Group recognises its share of any changes and discloses this, when applicable, in the consolidated statement of changes in equity. Unrealised gains and losses resulting from transactions between the Group and its associates are eliminated to the extent of the Group's interests in the associates, except where unrealised losses provide evidence of an impairment of the asset transferred.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Associates *(continued)*

The reporting dates of the associates and the Group are identical and the associates' accounting policies conform to those used by the Group for the transactions and events in similar circumstances.

Joint venture

The Group has an interest in a joint venture which is a jointly controlled entity. A joint venture is a contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control, and a jointly controlled entity is a joint venture that involves the establishment of a separate entity in which each venturer has an interest. The Group recognises its interest in the joint venture using proportionate consolidation. The Group combines its share of each of the assets, liabilities, income and expenses of the joint venture with the similar items, line by line, in its consolidated financial statements. Unrealised gains and losses resulting from transactions between the Group and its jointly controlled entities are eliminated to the extent of the Group's interests in the jointly controlled entities, except where unrealised losses provide evidence of an impairment of the asset transferred. The financial statements of the joint venture are prepared for the same reporting year as the Group, using consistent accounting policies.

When the Group contributes or sells assets to the joint venture, any portion of gain or loss from the transaction is recognised based on the substance of the transaction. When the Group purchases assets from the joint venture, the Group does not recognise its share of the profits of the joint venture from the transaction until it resells the assets to an independent party. The joint venture is proportionately consolidated until the date on which the Group ceases to have joint control over the joint venture.

Goodwill

Goodwill on acquisition is initially measured at cost being the excess of the cost of the business combination over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment, annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

The Group performs its annual impairment test of goodwill as at 31 December. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units) to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised. An impairment loss recognised for goodwill is not reversed in a subsequent period.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Goodwill *(continued)*

Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit retained.

Gain on bargain purchase

Any excess of the Group's interest in the net fair value of the acquirees' identifiable assets, liabilities and contingent liabilities over the cost of acquisition of subsidiaries (previously referred to as negative goodwill), after reassessment, is recognised immediately in the income statement.

The excess for associates and jointly-controlled entities is included in the Group's share of the associates' and jointly-controlled entities' profits or losses in the period in which the investments are acquired.

Property, plant and equipment and depreciation

Property, plant and equipment, other than construction in progress, are stated at cost, excluding the costs of day to day servicing, less accumulated depreciation and accumulated impairment in value. The cost of self-constructed assets includes the cost of materials, direct labour and an appropriate proportion of production overheads. Such cost also includes the cost of replacing part of the plant and equipment when that cost is incurred, if the recognition criteria are met.

Depreciation is calculated on the straight-line basis to write off the cost of each item of property, plant and equipment to its residual value over its estimated useful life.

The estimated useful lives of property, plant and equipment are as follows:

Buildings and structures	20 years
Plant and machinery	5 to 10 years
Office equipment	5 years
Motor vehicles	5 years

When each major inspection is performed, its cost is recognised in the carrying amount of the property, plant and equipment as a replacement if the recognition criteria are satisfied.

An item of property, plant and equipment is derecognised 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 derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the consolidated income statement in the year the item is derecognised.

The assets' residual values, useful lives and the depreciation method are reviewed, and adjusted if appropriate, at least at each financial year end.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Construction in progress

Construction in progress represents plants and properties under construction, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction and capitalised borrowing costs on related borrowed funds during the period of construction. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

Intangible assets (other than goodwill)

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is the fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Internally generated intangible assets, excluding capitalised development costs, are not capitalised and expenditure is reflected in the consolidated income statement in the year in which the expenditure is incurred.

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each balance sheet date.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangible assets are not amortised. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is accounted for on a prospective basis.

Patents and licences

Purchased patents and licences are stated at cost less any impairment losses and are amortised on the straight-line basis over their estimated useful lives of 10 years.

Trademark

Acquired trademark is stated at cost less any impairment losses and is amortised on the straight-line basis over its estimated useful life of 10 years.

Research and development costs

Research costs are expensed as incurred. An intangible asset arising from development expenditure on an individual project is recognised only when the Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the project and the ability to measure reliably the expenditure during the development.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Intangible assets (other than goodwill) *(continued)*

Research and development costs (continued)

During the period of development, the asset is tested for impairment annually. Following the initial recognition of the development expenditure, the cost model is applied requiring the asset to be carried at cost less any accumulated amortisation and accumulated impairment losses. Amortisation of the asset begins when the development is complete and the asset is available for use. It is amortised over the period of expected future sales. During the period of which the asset is not yet in use, it is tested for impairment annually.

Computer software

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised on the straight-line basis over their estimated useful lives of 3 to 10 years.

Non-current assets and disposal groups held for sale

Non-current assets and disposal groups are classified as held for sale if their carrying amounts will be recovered principally through a sales transaction rather than through continuing use. For this to be the case, the asset or disposal group must be available for immediate sale in its present condition subject only to terms that are usual and customary for the sale of such assets or disposal groups and its sale must be highly probable.

Non-current assets and disposal groups classified as held for sale are measured at the lower of their carrying amounts and fair values less costs to sell.

Impairment of non-financial assets other than goodwill

The Group assesses at each reporting date whether there is any indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is charged to the consolidated income statement in the period in which it arises, unless the asset is carried at a revalued amount in which case the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Impairment of non-financial assets other than goodwill *(continued)*

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such an indication exists, the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the consolidated income statement in the period in which it arises.

Inventories

Inventories are valued at the lower of cost and net realisable value.

Costs incurred in bringing each product to its present location and condition are accounted for as follows:

Raw materials	–	cost on a weighted average basis;
Finished goods	–	cost of direct materials and labour and a proportion of manufacturing overheads based on normal operating capacity but excluding borrowing costs on a weighted average basis.

Net realisable value is the estimated selling price in the ordinary course of business, less any estimated costs of completion and the estimated costs necessary to make the sale.

Cash and cash equivalents

Cash and cash equivalents comprise cash at banks and on hand and term deposits with an original maturity of three months or less. For the purpose of the consolidated statement of cash flows, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts, if any.

Investments and other financial assets

Financial assets in the scope of IAS 39 are classified as loans and receivables and available-for-sale investments, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year end.

All regular way purchases and sales of financial assets are recognised on the trade date, that is, the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Investments and other financial assets *(continued)*

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

After initial measurement, loans and receivables are subsequently carried at amortised cost using the effective interest method less any allowance for impairment. Amortised cost is calculated taking into account any discount or premium on acquisition and includes fees that are an integral part of the effective interest rate and transaction costs. Gains and losses are recognised in the consolidated income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Available-for-sale investments

The Group only holds available-for-sale investments which are non-trading investments in unlisted equity securities intended to be held on a long term basis. After initial recognition, available-for-sale investments are measured at fair value, with gains or losses recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in equity is included in the consolidated income statement. Interest and dividends earned are reported as interest income and dividend income, respectively and are recognised in the consolidated income statement as “Other income and gains” in accordance with the policies set out for “Revenue recognition” below. Losses arising from the impairment of such investments are recognised in the consolidated income statement as “Impairment losses on available-for-sale financial assets” and are transferred from the available-for-sale investment revaluation reserve.

When the fair value of unlisted equity securities cannot be reliably measured because (a) the variability in the range of reasonable fair value estimates is significant for that investment or (b) the probabilities of the various estimates within the range cannot be reasonably assessed and used in estimating fair value, such securities are stated at cost less any impairment losses.

Fair value

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business at the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm’s length market transactions; reference to the current market value of another instrument which is substantially the same; and a discounted cash flow analysis.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Impairment of financial assets

The Group assesses at each balance sheet date whether there is any objective evidence that a financial asset or a group of financial assets is impaired.

Assets carried at amortised cost

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced through the use of an allowance account. The amount of the impairment loss is recognised in the consolidated income statement. Loans and receivables together with any associated allowance are written off when there is no realistic prospect of future recovery.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. Any subsequent reversal of an impairment loss is recognised in the consolidated income statement, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date.

In relation to trade and other receivables, a provision for impairment is made when there is objective evidence (such as the probability of insolvency or significant financial difficulties of the debtor and significant changes in the technological, market, economic or legal environment that have an adverse effect on the debtor) that the Group will not be able to collect all of the amounts due under the original terms of an invoice. The carrying amount of the receivables is reduced through the use of an allowance account. Impaired debts are derecognised when they are assessed as uncollectible.

Assets carried at cost

If there is objective evidence that an impairment loss has been incurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Impairment losses on these assets are not reversed.

Available-for-sale financial assets

If an available-for-sale financial asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in the consolidated income statement, is transferred from equity to the consolidated income statement. A provision for impairment is made for an available-for-sale equity investment when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires judgement. Impairment losses on equity instruments classified as available for sale are not reversed through the consolidated income statement.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Derecognition of financial assets

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired;
- the Group retains the rights to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or
- the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Group's continuing involvement is the amount of the transferred asset that the Group may repurchase, except in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, where the extent of the Group's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Financial liabilities

Financial liabilities at amortised cost (including interest-bearing bank loans)

Financial liabilities, including trade and bills payables, other payables, other loans, long term payables and interest-bearing bank loans, are initially stated at fair value of the consideration received less directly attributable transaction costs and are subsequently measured at amortised cost, using the effective interest method unless the effect of discounting would be immaterial, in which case they are stated at cost. The related interest expense is recognised within "finance costs" in the consolidated income statement.

Gains and losses are recognised in the consolidated income statement when the liabilities are derecognised as well as through the amortisation process.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Financial liabilities *(continued)*

Financial guarantee contracts

Financial guarantee contracts in the scope of IAS 39 are accounted for as financial liabilities. A financial guarantee contract is recognised initially at its fair value less transaction costs that are directly attributable to the acquisition or issue of the financial guarantee contract, except when such contract is recognised at fair value through profit or loss. Subsequent to initial recognition, the Group measures the financial guarantee contract at the higher of: (i) the amount of the best estimate of the expenditure required to settle the present obligation at the balance sheet date; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with IAS 18 Revenue.

Derecognition of financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled, or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference between the respective carrying amounts is recognised in the consolidated income statement.

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Where the Group expects some or all of a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the consolidated income statement net of any reimbursement. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost.

Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the consolidated income statement, or in equity if it relates to items that are recognised in the same or a different period directly in equity.

Current income tax

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the balance sheet date.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Income tax *(continued)*

Deferred income tax

Deferred income tax is provided, using the liability method on temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred income tax liabilities are recognised for all taxable temporary differences, except:

- where the deferred income tax liability arises from goodwill or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interest in a joint venture, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carryforward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax credits and unused tax losses can be utilised, except:

- where the deferred income tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interest in a joint venture, deferred income tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised. Unrecognised deferred income tax assets are reassessed at each balance sheet date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Deferred income tax assets and deferred income tax liabilities are offset if a legally enforceable right exists to set off current income tax assets against current income tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably. The following specific recognition criteria must also be met before revenue is recognised:

Sale of goods

Revenue is recognised when the significant risks and rewards of ownership of the goods have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold.

Interest income

Revenue is recognised as interest accrues using the effective interest method by applying the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset.

Dividends

Revenue is recognised when the Group's right to receive the payment is established.

Government grants

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the period necessary to match the grant on a systematic basis to the costs that it is intended to compensate. Where the grant relates to an asset, the fair value is credited to a deferred income account and is released to the consolidated income statement over the expected useful life of the relevant asset by equal annual instalments.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e., assets that necessarily take a substantial period of time to prepare for their intended use, are capitalised as a part of the cost of those assets. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs capitalised.

All other borrowing costs are recognised as expenses in the consolidated income statement in the period in which they are incurred.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Leases

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement at the inception date of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset.

Operating leases

Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. When the Group is a lessee, operating lease payments are recognised as an expense in the consolidated income statement on the straight-line basis over the lease term.

Land use rights

Land use rights are initially stated at cost and subsequently recognised as an expense in the consolidated income statement on the straight-line basis over the lease terms of 50 years.

Foreign currency translation

Each entity in the Group determines its functional currency based on the assessment of its specific facts and circumstances. The Company, established in the Cayman Islands, uses the Hong Kong dollar as its functional currency and the subsidiaries, established in the PRC, use the RMB as their functional currency. As the Group mainly operates in Mainland China, RMB is used as the presentation currency of the Group. Transactions in foreign currencies are initially recorded at the functional currency rates ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rates of exchange ruling at the balance sheet date. All differences are taken to the consolidated income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

As at the reporting date, the assets and liabilities of companies whose functional currency differs from the presentation currency are translated into the presentation currency of the Group at the rates of exchange ruling at the balance sheet date and their income statements are translated at the weighted average exchange rates for the reporting period. The exchange differences arising on the retranslation are taken directly to a separate component of equity. On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the income statement.

For the purpose of the consolidated statement of cash flows, the cash flows of overseas subsidiaries are translated into RMB at the exchange rates ruling at the dates of the cash flows. Frequently recurring cash flows of overseas subsidiaries which arise throughout the year are translated into RMB at the weighted average exchange rates for the year.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Employee benefits

Retirement benefits

The Group's subsidiaries operating in Mainland China except for Hong Kong participate in a central defined contribution retirement plan managed by the local municipal government in the locations in which they operate. Contributions are made based on a percentage of the companies' payroll costs and are charged to the consolidated income statement as they become payable in accordance with the rules of the central pension scheme.

The Company also participates in the defined contribution Mandatory Provident Fund retirement scheme (the "MPF Scheme") in Hong Kong. Contributions are made to a separately administered fund based on a percentage of the employees' basic salaries and are charged to the consolidated income statement as they become payable in accordance with the rules of the MPF Scheme.

Share-based payment transactions

The Company operates a share option scheme for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. Employees (including directors) of the Group receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date on which they are granted. The fair value is determined by an external valuer using a binomial model, further details of which are given in note 40 to the financial statements. In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of the Company ("market conditions"), if applicable.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance and service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award (the "vesting date"). The cumulative expense recognised for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The charge or credit to the consolidated income statement for the period represents the movement in cumulative expense recognised as at the beginning and end of that period.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

Where the terms of an equity-settled award are modified, the minimum expense recognised is the expense if the terms had not been modified. An additional expense is recognised for any modification, which increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Employee benefits *(continued)*

Share-based payment transactions (continued)

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of earnings per share (further details are given in note 12).

Dividends

Final dividends proposed by the directors are classified as a separate allocation of retained earnings within the equity section of the balance sheet, until they have been approved by the shareholders in a general meeting. When these dividends are approved by the shareholders and declared, they are recognised as a liability.

Interim dividends are simultaneously proposed and declared, because the Company's memorandum and articles of association grant the directors the authority to declare interim dividends. Consequently, interim dividends are recognised directly as a liability when they are proposed and declared.

2.5 SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

The preparation of the Group's financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the reporting date. However, uncertainty about these assumptions and estimates could result in outcomes that could require a material adjustment to the carrying amounts of the assets or liabilities affected in the future.

Estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

Impairment of goodwill

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. Details of goodwill are given in note 21 to the financial statements.

2.5 SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES *(continued)*

Estimation uncertainty *(continued)*

Impairment of non-financial assets (other than goodwill)

The Group assesses whether there are any indicators of impairment for all non-financial assets at each reporting date. Indefinite life intangible assets are tested for impairment annually and at other times when such indicator exists. Other non-financial assets are tested for impairment when there are indicators that the carrying amounts may not be recoverable. When value in use calculations are undertaken, management must estimate the expected future cash flows from the asset or cash-generating unit and choose a suitable discount rate in order to calculate the present value of those cash flows.

Share-based payments

The Group measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. Estimating fair value requires determining the most appropriate valuation model for a grant of equity instruments, which is dependent on the terms and conditions of the grant. This also requires determining the most appropriate inputs to the valuation model including the expected life of the option, volatility and dividend yield and making assumptions about them. The assumptions and models used are disclosed in note 40 to the financial statements.

Judgements

Deferred tax assets

Deferred tax assets are recognised for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits, which affects the probability of utilisation and the tax rate to be used in the calculations. Details of deferred tax assets are contained in note 22 to the financial statements.

3. SEGMENT INFORMATION

The Group comprises the following business segments:

- Liquid milk products segment – manufacture and distribution of ultra-high temperature milk ("UHT milk"), milk beverages and yogurt;

- Ice cream products segment – manufacture and distribution of ice cream; and

- Other dairy products segment – manufacture and distribution of milk powder.

As the Group mainly operates and generates its revenue and results in Mainland China, no geographical segment analysis is presented.

Intersegment sales and transfers are transacted with reference to the selling prices used for sales made to third parties at the then prevailing market prices.

A discontinued operation which is principally engaged in raising milk cows and supplying raw milk is presented separately in the consolidated income statement as one-line item "Profit for the year from a discontinued operation". Assets and liabilities related to the discontinued operation are shown separately in the consolidated balance sheet as "Assets of a disposal group classified as held for sale" and "Liabilities of a disposal group classified as held for sale". Further details of the discontinued operation are disclosed in note 10 to the financial statements.

3. SEGMENT INFORMATION *(continued)*

The following tables present the revenue, results and certain asset and liability information of continuing operations for the Group's business segments for the year ended 31 December 2008:

Year ended 31 December 2008	Continuing operations Liquid milk products RMB'000	Ice cream products RMB'000	Other dairy products RMB'000	Eliminations RMB'000	Consolidated RMB'000
Segment revenue:					
Sales to external customers	21,068,097	2,626,515	170,363	–	23,864,975
Intersegment sales	214,891	52,308	11,460	(278,659)	–
Total	21,282,988	2,678,823	181,823	(278,659)	23,864,975
Segment results	(602,165)	(219,514)	(90,760)	–	(912,439)
Interest income					54,841
Finance costs					(39,394)
Share of profits and losses of associates					29,447
Unallocated corporate expenses					(221,730)
Loss before tax					(1,089,275)
Income tax income					161,454
Loss for the year					(927,821)
Assets and liabilities					
Segment assets	7,635,614	1,124,542	343,669	(1,776,719)	7,327,106
Unallocated corporate assets					3,609,218
Total assets					10,936,324
Segment liabilities	4,646,734	664,541	256,434	(1,776,719)	3,790,990
Unallocated corporate liabilities					2,503,665
Total liabilities					6,294,655
Other segment information:					
Depreciation and amortisation	510,425	93,382	7,822	–	611,629
Unallocated amounts					28,071
Total depreciation and amortisation					639,700
Capital expenditure	717,945	26,474	31,663	–	776,082
Unallocated capital expenditure					25,110
Total capital expenditure					801,192
Other non-cash expenses/(income)	233,555	12,937	(531)	–	245,961
Unallocated amounts					66,824
Total non-cash expenses					312,785

3. SEGMENT INFORMATION *(continued)*

Year ended 31 December 2007	Liquid milk products *RMB'000*	Ice cream products *RMB'000*	Other dairy products *RMB'000*	Eliminations *RMB'000*	Consolidated *RMB'000*
Segment revenue:					
Sales to external customers	19,148,856	1,991,728	177,478	–	21,318,062
Intersegment sales	150,016	37,141	–	(187,157)	–
Total	19,298,872	2,028,869	177,478	(187,157)	21,318,062
Segment results	1,249,599	85,228	(31,994)	–	1,302,833
Interest income					43,566
Finance costs					(50,060)
Share of profits and losses of associates					20,954
Unallocated corporate expenses					(186,983)
Profit before tax					1,130,310
Income tax expense					(21,658)
Profit for the year					1,108,652
Assets and liabilities					
Segment assets	7,042,655	966,557	230,324	(1,402,477)	6,837,059
Unallocated corporate assets					2,844,220
Total assets					9,681,279
Segment liabilities	3,920,366	470,352	165,928	(1,402,477)	3,154,169
Unallocated corporate liabilities					692,406
Total liabilities					3,846,575
Other segment information:					
Depreciation and amortisation	416,032	91,862	4,718	–	512,612
Unallocated amounts					17,863
Total depreciation and amortisation					530,475
Capital expenditure	1,071,931	71,782	127,295	–	1,271,008
Unallocated amounts					244,053
Total capital expenditure					1,515,061
Other non-cash expenses	12,772	3,336	4,687	–	20,795
Unallocated amounts					14,949
Total non-cash expenses					35,744

4. REVENUE, OTHER INCOME AND GAINS

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

An analysis of the Group's revenue, other income and gains is as follows:

	Notes	**2008** ***RMB'000***	2007 *RMB'000*
Revenue		**23,864,975**	21,318,062
Other income and gains:			
Government grants	(a)	**34,982**	41,737
Amortisation of deferred income	(b)	**12,545**	10,816
Foreign exchange gains, net		**65,825**	38,822
Others		**9,302**	6,721
		122,654	98,096
		23,987,629	21,416,158

Notes:

(a) The government grants have been received for the Group's contribution to the local economy with respect to the establishment of infrastructure relating to the dairy products industry. There are no unfulfilled conditions or contingences attaching to these grants.

(b) The Group has received certain government grants in the form of property, plant and equipment donations or cash donations to purchase property, plant and equipment. The grants are initially recorded as deferred income and amortised to match the depreciation charge of the underlying property, plant and equipment in accordance with the assets' estimated useful lives.

5. OTHER OPERATING EXPENSES

	Notes	2008 RMB'000	2007 RMB'000
Write-off of inventories	(a)	**655,216**	–
Write-down of inventories to net realisable value	(a)	**179,873**	4,413
Loss on disposal of items of property, plant and equipment		**6,227**	8,298
Donation		**20,050**	6,922
Cash contribution to the Medical Compensation Fund	(b)	**4,985**	–
Others		**9,682**	2,196
		876,033	21,829

Notes:

(a) In September 2008, certain dairy products manufactured by the Group were found to contain melamine under the laboratory testing by the General Administration of Quality Supervision, Inspection and Quarantine of the People's Republic of China. As a consequence of the Group's action in the event, the Group wrote off inventories at a cost of RMB655,216,000. As at 31 December 2008, the Group also made an impairment provision for the dairy products held in inventories as at 31 December 2008 at the amount of RMB179,873,000 (note 24).

(b) Mengniu Arla (Inner Mongolia) Dairy Products Co., Ltd., a 50% joint venture of the Group and the sole milk powder producer within the Group, contributed the amount of RMB9,970,000 to a medical compensation fund centrally managed by the government (hereafter "the Medical Compensation Fund") in December 2008.

6. PROFIT/(LOSS) BEFORE TAX

The Group's profit/(loss) before tax is arrived at after charging/(crediting):

	2008 *RMB'000*	2007 *RMB'000*
Cost of inventories sold	**19,195,576**	16,514,557
Employee benefit expense (excluding directors' remuneration as disclosed in note 7)		
– Wages, salaries, housing benefits and other allowances	**889,211**	800,406
– Retirement benefit contributions	**68,503**	50,138
– Share-based payment expense (note 40)	**105,441**	35,352
	1,063,155	885,896
Depreciation of property, plant and equipment	**630,046**	522,706
Amortisation of land use rights	**5,604**	4,681
Amortisation of other intangible assets	**4,050**	3,088
Research and development costs – current year expenditure	**29,684**	13,949
Write-back of provision against trade receivables and other receivables	**(1,711)**	(7,903)
Minimum lease payments under operating leases on buildings and certain production equipment	**212,913**	205,846
Display space leasing fees	**273,804**	213,112
Auditors' remuneration	**3,785**	3,526

7. DIRECTORS' AND SENIOR EXECUTIVES' EMOLUMENTS

Directors' remuneration for the year, disclosed pursuant to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") and Section 161 of the Hong Kong Companies Ordinance, is as follows:

	2008 *RMB'000*	2007 *RMB'000*
Fees	**270**	270
Other emoluments		
– Basic salaries, housing benefits, other allowances and benefits in kind	**4,754**	3,844
– Retirement benefit contributions	**110**	51
	5,134	4,165

	Notes	Fees *RMB'000*	Basic salaries, housing benefits, other allowances and benefits in kind *RMB'000*	Retirement contributions *RMB'000*	Total remuneration *RMB'000*
2008					
Executive directors					
– Mr. Niu Gensheng		30	866	22	918
– Mr. Yang Wenjun		30	1,470	22	1,522
– Mr. Sun Yubin		30	584	22	636
– Mr. Yao Tongshan		15	413	22	450
– Mr. Bai Ying		15	1,421	22	1,458
Non-executive directors					
– Mr. Jiao Shuge	(b)	–	–	–	–
– Mr. Julian Juul Wolhardt	(b)	–	–	–	–
Independent non-executive directors					
– Mr. Wang Huaibao		50	–	–	50
– Mr. Zhang Julin		50	–	–	50
– Mr. Li Jianxin	(c)	50	–	–	50
		270	4,754	110	5,134

7. DIRECTORS' AND SENIOR EXECUTIVES' EMOLUMENTS *(continued)*

	Notes	Fees RMB'000	Basic salaries, housing benefits, other allowances and benefits in kind RMB'000	Retirement contributions RMB'000	Total remuneration RMB'000
2007					
Executive directors					
– Mr. Niu Gensheng		30	990	17	1,037
– Mr. Yang Wenjun		30	1,683	17	1,730
– Mr. Sun Yubin		30	1,001	17	1,048
Non-executive directors					
– Mr. Jiao Shuge	(b)	–	–	–	–
– Ms. Lu Jun	(a)	30	170	–	200
– Mr. Julian Juul Wolhardt	(b)	–	–	–	–
Independent non-executive directors					
– Mr. Wang Huaibao		50	–	–	50
– Mr. Zhang Julin		50	–	–	50
– Mr. Li Jianxin	(c)	50	–	–	50
		270	3,844	51	4,165

Notes:

(a) Ms. Lu Jun resigned as a non-executive director on 1 January 2008.

(b) The two (2007: two) non-executive directors agreed to waive their entitlements to directors' fees totaling RMB100,000 (2007: RMB100,000) for the year. Other than the aforementioned, there was no arrangement under which a director waived or agreed to waive any remuneration during the year.

(c) Mr. Li has passed away subsequent to the year end of 2008. Details are disclosed in the Company's announcement dated 23 February 2009.

(d) During the year, certain directors were granted share options in respect of their services to the Group under the share option scheme of the Company, further details of which are set out in note 40 to the financial statements. In accordance with IFRS 2, share option benefits represent the fair value at grant date of the share options issued under the share option scheme of the Company amortised to the consolidated income statement during the year disregarding whether the options have been vested/exercised or not. No share options were exercised by the directors during the year. During the year, the share option benefits relating to the share options granted to Mr. Yang Wenjun, Mr. Sun Yubin, Mr. Yao Tongshan and Mr. Bai Ying were approximately RMB15,256,000 (2007: RMB2,750,000), RMB4,091,000 (2007: RMB1,131,000), RMB3,095,000 (2007: RMB1,000,000), and RMB6,739,000 (2007: RMB1,373,000), respectively. The share option benefits relating to the share options granted to the four directors are not included in the above analysis.

7. DIRECTORS' AND SENIOR EXECUTIVES' EMOLUMENTS *(continued)*

Three (2007: Three) of the five highest paid individuals were directors whose emoluments have been shown above. Details of emoluments paid to the remaining two (2007: two) non-director, highest paid senior executives for the year were as follows:

	2008 *RMB'000*	2007 *RMB'000*
Basic salaries, housing benefits, other allowances and benefits in kind	**1,440**	2,801
Discretionary bonuses	**–**	–
Retirement scheme contributions	**110**	35
	1,550	2,836

The number of non-director, highest paid employees whose remuneration fell within the following bands is as follows:

	Number of employees	
	2008	2007
HK$500,001 to HK$1,000,000	**2**	–
HK$1,000,001 to HK$1,500,000	**–**	1
HK$1,500,001 to HK$2,000,000	**–**	1
	2	2

In the prior year, out of the above amount, approximately RMB1,275,000 and RMB1,561,000 were payable to Mr. Yao Tongshan and Mr. Bai Ying, respectively. They were appointed as executive directors in July 2008.

During the year, share options were granted to two non-director, highest paid employees in respect of their services to the Group, further details of which are set out in note 40 to the financial statements. During the year, the share option benefits relating to the share options granted to the two non-director, highest paid employees were approximately RMB6,954,000 (2007: RMB2,373,000) in aggregate. The share option benefits relating to the share options granted to the two non-director, highest paid employees are not included in the above analysis.

8. FINANCE COSTS

	2008 RMB'000	2007 RMB'000
Interest on long term payables	**16,505**	15,506
Interest on bank loans wholly repayable within five years	**26,796**	36,830
Less: Amounts capitalised	**(3,907)**	(2,276)
	39,394	50,060

The amounts capitalised are the borrowing costs related to funds borrowed specifically for the purpose of obtaining qualifying assets. The interest rate on such capitalised borrowings during the year was 5.96% (2007: 5.88%) per annum.

9. INCOME TAX (INCOME)/EXPENSE

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

Under the PRC income tax law, except for certain preferential treatment available to twenty-two (2007: twenty-one) of the Group's subsidiaries and jointly-controlled entities, the entities within the Group are subject to CIT at a rate of 25% on the taxable income as reported in their statutory accounts which are prepared in accordance with the PRC accounting standards and financial regulations.

	2008 RMB'000	2007 RMB'000
Current income tax	**19,125**	27,960
Deferred income tax (note 22)	**(180,579)**	(6,302)
	(161,454)	21,658

9. INCOME TAX (INCOME)/EXPENSE *(continued)*

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

	Note	2008 *RMB'000*	2007 *RMB'000*
Profit/(loss) before tax		**(1,089,275)**	1,130,310
At CIT rate of 25% (2007: 33%)	(a)	**(272,319)**	373,002
Non-taxable items and others, net		**26,450**	40,802
Adjustment recognised in the year for current tax of prior years		**3,819**	–
Effect of preferential tax rates	(b)	**150,658**	(44,061)
Effect on tax exemptions	(b)	**(89,990)**	(330,221)
Tax losses not recognised		**19,928**	–
Utilisation of previously unrecognised tax credits		**–**	(17,864)
At the effective income tax rate of 14.8% (2007: 1.9%)		**(161,454)**	21,658

Notes:

(a) On 16 March 2007, the Fifth Plenary Session of the Tenth National People's Congress passed the Corporate Income Tax Law of the People's Republic of China (hereafter "the New Tax Law"). According to the New Tax Law, the applicable tax rates of the Group's subsidiaries in the PRC are unified at 25% with effect from 1 January 2008.

(b) Twenty-two (2007: twenty-one) subsidiaries and a jointly-controlled entity were subject to tax concessions in 2008. The total deductible loss of the subsidiaries that are subject to tax concessions amounted to approximately RMB719,771,000 (2007: taxable profit of RMB1,134,188,000) in aggregate. Out of the twenty-two subsidiaries, nineteen (2007: seventeen) plus the jointly-controlled entity were granted tax concessions by the state tax bureau in accordance with the New Tax Law and the corresponding transitional tax concession policy and "The notice of preferential tax policies for companies located in West China. Three (2007: two) subsidiaries were granted tax concessions In accordance with the policy of "The notice of preferential tax policy for preliminary processing of agriculture products".

(c) The share of tax attributable to associates amounting to approximately RMB5,549,000 (2007: RMB10,428,000) is included in the share of profits and losses of associates on the face of the consolidated income statement.

10. ACQUISITION OF A SUBSIDIARY WITH A VIEW TO RESALE

On 5 September 2008, with a view for resale within one year, the Company acquired the entire equity interests of AustDairy Limited (hereafter "AustDairy"), an investment company whose net assets primarily comprised a 70% equity interest in Inner Mongolia Mengniu AustAsia Model Dairy Farm Company Limited (hereafter "AustAsia"). Prior to the acquisition, AustAsia was a 30% associate indirectly held by Inner Mongolia Mengniu Dairy (Group) Company Limited (hereafter "Mengniu"), a subsidiary of the Company. The subsidiary was acquired for the purpose of business reorganization of the Group.

The fair values of the identifiable assets and liabilities of AustDairy as at the date of acquisition and the corresponding carrying amounts immediately before the acquisition were as follows:

	Fair value recognised on acquisition *RMB'000*	**Previous carrying amounts** *RMB'000*
Total assets	385,309	397,060
Total liabilities	(253,580)	(253,580)
Net assets	131,729	143,480
Previously held equity interests in AustAsia measured at fair value	(39,519)	
Total net assets acquired	92,210	
Gain from the bargain purchase	(2,549)	
Consideration, satisfied by cash	89,661	

The acquisition related costs of approximately RMB300,000 and the gain of RMB4,328,000 as a result of remeasuring the fair value of previously held equity interests in AustAsia were recognized in the "profit for the year from a discontinued operation" on the face of the consolidated income statement for the year.

The operating results of AustAsia attributable to the Group before 5 September 2008 were included in "Share of profits and losses of associates" on the face of the consolidated income statement amounting to RMB18,664,000 (2007: RMB3,771,000).

By the end of 2008, AustDairy and Mengniu entered into equity transfer agreements with a third party to sell 70% and 30% equity interests in AustAsia, respectively. The disposal transaction is due to be completed within 2009. Upon the acquisition of AustDairy by the Company and as at 31 December 2008, the net assets of AustAsia have been classified as a disposal group held for sale and as a discontinued operation in the consolidated financial statements.

11. DIVIDENDS

	Note	2008 RMB'000	2007 RMB'000
Declared and paid during the year			
Equity dividends on ordinary shares		**187,667**	156,020
Proposed for approval at the AGM			
Equity dividends on ordinary shares:			
Proposed final – Nil (2007: RMB0.1315) per ordinary share	(a)	–	187,535

Note:

(a) The directors do not recommend the payment of a final dividend for the year ended 31 December 2008. The proposed total dividend for the year ended 31 December 2007 was calculated based on approximately 1,426,120,000 existing shares in issue. The proposed final dividend for that year was subject to the approval of the Company's shareholders at the forthcoming Annual General Meeting (the "AGM"). Such dividend was not recognised as a liability in the consolidated financial statements as at 31 December 2007 but was reflected as an appropriation of retained earnings for the year ended 31 December 2008.

12. EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY

The basic earnings per share for the year is calculated by dividing the profit/(loss) for the year attributable to ordinary equity holders of the Company by the weighted average number of ordinary shares outstanding during the year.

The diluted earnings per share was calculated by dividing the profit/(loss) for the year attributable to ordinary equity holders of the Company by the weighted average number of ordinary shares in issue during that year, as used in the basic earnings per share calculation; and the weighted average number of ordinary shares assumed to have been issued at no consideration on the deemed exercise of all share options during the year pursuant to contingent ordinary share provision in IAS 33 *Earnings per Share*.

12. EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY *(continued)*

Diluted loss per share amounts for loss for the year and for loss from continuing operations for the year ended 31 December 2008 have not been disclosed as the deemed exercise of share options during 2008 had an anti-dilutive effect on the basic loss per share.

The calculations of basic and diluted earnings per share are based on:

Earnings

	2008 ***RMB'000***	2007 *RMB'000*
Profit/(loss) attributable to ordinary equity share holders of the Company:		
From continuing operations	**(951,957)**	935,786
From a discontinued operation	**3,357**	–
	(948,600)	935,786

Shares

	2008 **Number of shares** ***'000***	2007 Number of shares *'000*
Weighted average number of ordinary shares for the purpose of the basic earnings per share calculation	**1,485,403**	1,408,911
Weighted average number of ordinary shares, assuming issued at no consideration on the deemed exercise of all share options during the year	**35**	859
Weighted average number of ordinary shares for the purpose of the diluted earnings per share calculation	**1,485,438**	1,409,770

13. PROPERTY, PLANT AND EQUIPMENT

Movements of the Group's property, plant and equipment during the year are as follows:

	Buildings and structures RMB'000	Plant and machinery RMB'000	Office equipment RMB'000	Motor vehicles RMB'000	Total RMB'000
At 1 January 2008, net of accumulated depreciation	1,368,004	3,534,342	98,898	41,404	5,042,648
Additions	74,475	143,878	32,773	12,309	263,435
Transfers from construction in progress (note 14)	100,262	476,225	19,797	–	596,284
Disposals	–	(24,507)	(343)	(399)	(25,249)
Depreciation provided during the year	(81,874)	(508,408)	(27,976)	(11,788)	(630,046)
At 31 December 2008, net of accumulated depreciation	1,460,867	3,621,530	123,149	41,526	5,247,072
At 1 January 2008					
Cost	1,561,686	4,673,230	170,416	83,352	6,488,684
Accumulated depreciation	(193,682)	(1,138,888)	(71,518)	(41,948)	(1,446,036)
Net carrying amount	1,368,004	3,534,342	98,898	41,404	5,042,648
At 31 December 2008					
Cost	1,736,423	5,257,081	221,927	96,703	7,312,134
Accumulated depreciation	(275,556)	(1,635,551)	(98,778)	(55,177)	(2,065,062)
Net carrying amount	1,460,867	3,621,530	123,149	41,526	5,247,072

13. PROPERTY, PLANT AND EQUIPMENT *(continued)*

	Buildings and structures	Plant and machinery	Office equipment	Motor vehicles	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
At 1 January 2007, net of accumulated depreciation	1,187,696	2,879,953	68,218	24,416	4,160,283
Additions	31,085	477,511	29,313	29,569	567,478
Transfers from construction in progress (note 14)	221,097	606,864	26,122	–	854,083
Disposals	(9,178)	(6,678)	(159)	(475)	(16,490)
Depreciation provided during the year	(62,696)	(423,308)	(24,596)	(12,106)	(522,706)
At 31 December 2007, net of accumulated depreciation	1,368,004	3,534,342	98,898	41,404	5,042,648
At 1 January 2007					
Cost	1,319,536	3,599,339	115,884	54,932	5,089,691
Accumulated depreciation	(131,840)	(719,386)	(47,666)	(30,516)	(929,408)
Net carrying amount	1,187,696	2,879,953	68,218	24,416	4,160,283
At 31 December 2007					
Cost	1,561,686	4,673,230	170,416	83,352	6,488,684
Accumulated depreciation	(193,682)	(1,138,888)	(71,518)	(41,948)	(1,446,036)
Net carrying amount	1,368,004	3,534,342	98,898	41,404	5,042,648

(a) All of the Group's buildings are located in Mainland China.

(b) Certain property, plant and equipment of the Group with a net book value of approximately RMB468,089,060 (2007: RMB644,828,000) have been pledged to secure the long term payables of the Group, details of which are set out in note 35 to the financial statements.

13. PROPERTY, PLANT AND EQUIPMENT *(continued)*

Movements of the Company's property, plant and equipment during the year, which comprise only office equipment, are as follows:

	Company	
	2008	2007
	RMB'000	*RMB'000*
At 1 January, net of accumulated depreciation	**65**	65
Additions	**22**	24
Depreciation provided during the year	**(39)**	(24)
At 31 December, net of accumulated depreciation	**48**	65
At 1 January		
Cost	**145**	121
Accumulated depreciation	**(80)**	(56)
Net carrying amount	**65**	65
At 31 December		
Cost	**167**	145
Accumulated depreciation	**(119)**	(80)
Net carrying amount	**48**	65

14. CONSTRUCTION IN PROGRESS

Movements of the Group's construction in progress, all of which are located in Mainland China, are as follows:

	Group	
	2008	2007
	RMB'000	*RMB'000*
Carrying amount at beginning of year	**313,439**	348,405
Additions during the year	**497,862**	819,117
Transfers to property, plant and equipment (note 13)	**(596,284)**	(854,083)
Carrying amount at end of year	**215,017**	313,439

15. OTHER INTANGIBLE ASSETS

Movements of the Group's other intangible assets are as follows:

	Patents and licenses *RMB'000*	Trademarks *RMB'000*	Computer software *RMB'000*	Total *RMB'000*
Cost at 1 January 2008, net of accumulated amortisation	**6,414**	**14,520**	**10,470**	**31,404**
Additions	**249**	**–**	**5,064**	**5,313**
Amortisation provided during the year	**(607)**	**(1,560)**	**(1,883)**	**(4,050)**
At 31 December 2008	**6,056**	**12,960**	**13,651**	**32,667**
At 31 December 2008				
Cost	**7,249**	**15,690**	**18,220**	**41,159**
Accumulated amortisation	**(1,193)**	**(2,730)**	**(4,569)**	**(8,492)**
Net carrying amount	**6,056**	**12,960**	**13,651**	**32,667**
Cost at 1 January 2007, net of accumulated amortisation	6,767	–	6,437	13,204
Additions	–	15,690	5,598	21,288
Amortisation provided during the year	(353)	(1,170)	(1,565)	(3,088)
At 31 December 2007	6,414	14,520	10,470	31,404
At 31 December 2007				
Cost	7,000	15,690	13,156	35,846
Accumulated amortisation	(586)	(1,170)	(2,686)	(4,442)
Net carrying amount	6,414	14,520	10,470	31,404

16. LAND USE RIGHTS

	Group	
	2008	2007
	RMB'000	*RMB'000*
Carrying amount at beginning of year	**233,503**	131,006
Additions during the year	**34,582**	107,178
Amortised during the year	**(5,604)**	(4,681)
Carrying amount at end of year	**262,481**	233,503
Current portion included in prepayments and deposits under current assets (note 27)	**5,957**	4,764
Non-current portion	**256,524**	228,739
	262,481	233,503

The leasehold land is held under a long term lease of 50 years and is situated in Mainland China.

17. INTERESTS IN SUBSIDIARIES

	Company	
	2008	2007
	RMB'000	*RMB'000*
Unlisted shares, at cost	**3,785,449**	826,927
Loan to a subsidiary	**806,136**	855,945
	4,591,585	1,682,872
Less: Interest in a subsidiary with a view to resale (note 10)	**(67,004)**	–
	4,524,581	1,682,872

The loan to a subsidiary included in the interests in subsidiaries above is unsecured, interest-free and has no fixed terms of repayment. The carrying amount of the loan to a subsidiary approximates to its fair value.

17. INTERESTS IN SUBSIDIARIES *(continued)*

Details of the Company's subsidiaries at 31 December 2008 are set out below:

Name	Date of incorporation/ establishment*	Issued share capital	Percentage of equity interest attributable to the Company Direct	Indirect	Principal activities
China Dairy Holdings (i)	5 June 2002	US$214	100%	–	Investment holding
China Dairy (Mauritius) Limited (i)	15 June 2002	US$100	–	100%	Investment holding
Inner Mongolia Mengniu Dairy (Group) Company Limited (iii) (內蒙古蒙牛乳業（集團）股份有限公司)	18 August 1999	RMB802,288,466	8.97%	84.32%	Manufacture and sale of dairy products
Beijing Mengniu Dairy Co., Ltd. (i) (ii) (iv) (北京蒙牛乳製品有限責任公司)	4 July 2000	RMB500,000	–	48.51%	Packaging and sale of dairy products
Inner Mongolia Mengniu Founding Industry Management Co., Ltd. (i) (ii) (內蒙古蒙牛方鼎產業管理有限責任公司)	9 February 2002	RMB45,000,000	–	93.29%	Investment holding
Mengniu Dairy (Wulanhaote) Co., Ltd. (i) (iii) (蒙牛乳業（烏蘭浩特）有限責任公司)	18 June 2002	RMB30,000,000	–	93.29%	Manufacture and sale of dairy products
Inner Mongolia Mengniu Dairy Keerqin Co., Ltd. (i) (iii) (內蒙古蒙牛乳業科爾沁有限責任公司)	19 June 2002	RMB35,000,000	–	93.29%	Manufacture and sale of dairy products
Mengniu Dairy (Dangyang) Co., Ltd. (i) (iii) (蒙牛乳業（當陽）有限責任公司)	7 November 2002	RMB42,000,000	–	93.29%	Manufacture and sale of dairy products
Mengniu Dairy (Beijing) Co., Ltd. (i) (iii) (蒙牛乳業（北京）有限責任公司)	11 November 2002	RMB120,000,000	26.70%	68.38%	Manufacture and sale of dairy products
Jinhua Mengniu Dairy Co., Ltd. (i) (ii) (iv) (金華蒙牛乳業有限公司)	19 February 2003	RMB500,000	–	47.58%	Manufacture and sale of dairy products
Mengniu Dairy (Shenyang) Co., Ltd. (i) (iii) (蒙牛乳業（瀋陽）有限責任公司)	4 December 2003	RMB100,000,000	26.05%	68.99%	Manufacture and sale of dairy products
Beijing Mengniu Hongda Dairy Co., Ltd (i) (ii) (iv) (北京蒙牛宏達乳製品有限責任公司)	12 September 2002	RMB20,000,000	–	48.51%	Packaging and sale of dairy products

17. INTERESTS IN SUBSIDIARIES *(continued)*

Name	Date of incorporation/ establishment*	Issued share capital	Percentage of equity interest attributable to the Company Direct	Indirect	Principal activities
Inner Mongolia Mengniu Dairy Baotou Co., Ltd. (i) (iii) (內蒙古蒙牛乳業包頭有限責任公司)	9 January 2003	RMB30,000,000	26.40%	68.66%	Manufacture and sale of dairy products
Mengniu Dairy (Dengkou Bayan Gaole) Co., Ltd. (i) (iii) (蒙牛乳業（磴口巴彥高勒）有限責任公司)	13 July 2003	RMB40,000,000	–	93.29%	Manufacture and sale of dairy products
Inner Mongolia Mengniu Dairy (Group) Shanxi Dairy Co., Ltd. (i) (ii) (內蒙古蒙牛乳業（集團）山西乳業有限公司)	14 July 2003	RMB10,000,000	–	83.96%	Manufacture and sale of dairy products
Mengniu Dairy (Jiaozuo) Co., Ltd. (i) (iii) (蒙牛乳業（焦作）有限公司)	6 November 2003	RMB110,000,000	–	93.29%	Manufacture and sale of dairy products
Mengniu Dairy Taian Co., Ltd. (i) (iii) (蒙牛乳業泰安有限責任公司)	18 November 2003	RMB110,000,000	26.03%	69.01%	Manufacture and sale of dairy products
Mengniu Dairy (Luannan) Co., Ltd. (i) (iii) (蒙牛乳業（灤南）有限責任公司)	31 March 2004	RMB56,000,000	26.06%	68.98%	Manufacture and sale of dairy products
Mengniu Dairy (Tangshan) Co., Ltd. (i) (iii) (蒙牛乳業（唐山）有限責任公司)	31 March 2004	RMB70,000,000	26.05%	68.99%	Manufacture and sale of dairy products
Mengniu Dairy (Maanshan) Co., Ltd. (i) (iii) (蒙牛乳業（馬鞍山）有限責任公司)	4 February 2005	RMB155,000,000	–	93.29%	Manufacture and sale of dairy products
Mengniu (Wuhan) Frealth Dairy Co., Ltd. (i) (iii) (蒙牛（武漢）友芝友乳業有限公司)	6 January 2006	RMB120,000,000	–	93.29%	Manufacture and sale of dairy products
Inner Mongolia Mengniu Breeding Biotech Co., Ltd. (i) (ii) (內蒙古蒙牛繁育生物技術有限公司)	31 July 2006	RMB20,000,000	–	60.64%	Cultivation and sale of cattle embryos
Inner Mongolia Mengniu Hi-tech Dairy Co., Ltd. (i) (ii) (內蒙古蒙牛高科乳業有限公司)	2 August 2006	RMB150,000,000	–	93.29%	Manufacture and sale of dairy products
Mengniu Dairy (Tai Yuan) Co., Ltd. (i) (ii) (蒙牛乳業（太原）有限公司)	13 April 2006	RMB116,670,000	–	93.29%	Manufacture and sale of dairy products
Mengniu Dairy (Shangzhi) Co., Ltd. (i) (ii) (蒙牛乳業（尚志）有限責任公司)	10 June 2005	RMB50,000,000	–	93.29%	Manufacture and sale of dairy products

17. INTERESTS IN SUBSIDIARIES *(continued)*

Name	Date of incorporation/ establishment*	Issued share capital	Percentage of equity interest attributable to the Company Direct	Indirect	Principal activities
Mengniu Dairy (Chabei) Co., Ltd. (i) (ii) (蒙牛乳業（察北）有限公司)	15 June 2005	RMB30,000,000	–	72.77%	Manufacture and sale of dairy products
Mengniu Dairy (Baoji) Co., Ltd. (i) (iii) (蒙牛乳業（寶雞）有限公司)	1 November 2005	RMB96,840,000	–	93.29%	Manufacture and sale of dairy products
Mengniu Dairy (Baoding) Co., Ltd. (ii) (蒙牛乳業（保定）有限公司)	22 January 2007	RMB62,000,000	–	93.29%	Manufacture and sale of dairy products
Beijing Mengniu Cheese Co., Ltd. (ii) (北京蒙牛奶酪有限公司)	23 May 2007	RMB5,000,000	–	93.29%	Manufacture and sale of dairy products
Mengniu Dairy Meishan Co., Ltd. (ii) (蒙牛乳業眉山有限公司)	29 August 2007	RMB60,000,000	–	93.29%	Manufacture and sale of dairy products
Mengniu Saibei Dairy Co., Ltd. (iii) (蒙牛塞北乳業有限公司)	29 August 2007	RMB67,121,418	26%	69.03%	Manufacture and sale of dairy products
Mengniu Dairy (Qiqihaer) Co., Ltd. (ii) (蒙牛乳業（齊齊哈爾）有限公司)	23 November 2007	RMB55,500,000	–	93.29%	Manufacture and sale of dairy products
AustDairy Limited (i)	18 September 2001	US$20,000,000	100%	–	Investment holding
Inner Mogolia Mengniu AustAisa Model Dairy Farm Company Limited (iii) (內蒙古蒙牛澳亞示範牧場有限責任公司)	12 July 2004	US$11,500,000	–	97.99%	Production of raw milk, planting of pastures and processing of milk

* Except for China Dairy Holdings, AustDairy Limited and China Dairy (Mauritius) Limited, which were incorporated in the Cayman Islands, the British Virgin Islands and Mauritius, respectively, all subsidiaries were incorporated in the PRC.

(i) Not audited by Ernst & Young Hong Kong or other member firm of the Ernst & Young global network.

(ii) The subsidiaries are registered as companies with limited liability under the PRC law.

(iii) The subsidiaries are registered as Sino-foreign equity joint ventures under the PRC law.

(iv) Since more than 50% of the equity interest of the subsidiaries was held by Mengniu in which the Company held a 93.29% equity interest, the Company had control over the subsidiaries even with less than 50% of equity interest held indirectly as at the balance sheet date.

18. INTERESTS IN ASSOCIATES

	Group	
	2008 RMB'000	2007 RMB'000
Share of net assets	**40,107**	57,573

Details of the Group's associates at 31 December 2008 are set out below:

Name	Particulars of issued shares held	Place of incorporation/ registration and operations	Percentage of equity interest attributable to the Group (indirect) 2008	2007	Principal activities
Xinjiang Tianxue Food Co., Ltd. (i) (新疆天雪食品有限公司)	Registered capital	Mainland China	23%	21%	Trading of dairy products
Fuzhou Mengxin Trading Co., Ltd. (i) (福州蒙鑫貿易有限公司)	Registered capital	Mainland China	43%	39%	Trading of dairy products
Shijiazhuang Mengniu Ice Cream Sales Co., Ltd. (i) (石家庄蒙牛冰淇淋銷售有限公司)	Registered capital	Mainland China	37%	34%	Trading of dairy products
Tianjin Mengniu Ice Cream Sales Co., Ltd. (i) (天津蒙牛冰淇淋銷售有限責任公司)	Registered capital	Mainland China	37%	34%	Trading of dairy products
Guangzhou Mengniu Dairy Trading Co., Ltd. (i) (廣州市蒙牛乳業貿易有限公司)	Registered capital	Mainland China	37%	34%	Trading of dairy products
Wuhan Mengniu Dairy Co., Ltd. (i) (武漢蒙牛乳業有限公司)	Registered capital	Mainland China	26%	24%	Trading of dairy products
Guilin Mengniu Dairy Sales Co., Ltd. (i) (桂林蒙牛乳業銷售有限公司)	Registered capital	Mainland China	37%	34%	Trading of dairy products

18. INTERESTS IN ASSOCIATES *(continued)*

Details of the Group's associates at 31 December 2008 are set out below: *(continued)*

Name	Particulars of issued shares held	Place of incorporation/ registration and operations	Percentage of equity interest attributable to the Group (indirect) 2008	2007	Principal activities
Tianjin Mengniu Dairy Sales Co., Ltd. (i) (天津市蒙牛乳業銷售有限公司)	Registered capital	Mainland China	37%	34%	Trading of dairy products
Wenzhou Mengniu Dairy Co., Ltd. (i) (溫州蒙牛乳業有限公司)	Registered capital	Mainland China	37%	34%	Trading of dairy products
Heilongjiang Mengniu Dairy Sales Co., Ltd. (i) (黑龍江蒙牛乳業銷售有限公司)	Registered capital	Mainland China	42%	38%	Trading of dairy products
Chengdu Mengniu Dairy Sales Co., Ltd (i) (成都蒙牛乳業銷售有限責任公司)	Registered capital	Mainland China	34%	34%	Trading of dairy products
Nanjing Mengniu Dairy Sales Co., Ltd. (i) (南京蒙牛乳業銷售有限公司)	Registered capital	Mainland China	42%	38%	Trading of dairy products
Shenyang Mengniu Dairy Co., Ltd. (i) (ii) (瀋陽蒙牛乳業有限公司)	Registered capital	Mainland China	19%	17%	Trading of dairy products
Jinan Mengniu Dairy Co., Ltd. (i) (濟南蒙牛乳業有限公司)	Registered capital	Mainland China	42%	38%	Trading of dairy products
Taiyuan Mengniu Dairy Co., Ltd. (i) (太原市蒙牛乳業有限公司)	Registered capital	Mainland China	37%	34%	Trading of dairy products
Nanchang Mengniu Dairy Sales Co., Ltd. (i) (南昌蒙牛乳業銷售有限責任公司)	Registered capital	Mainland China	42%	38%	Trading of dairy products
Chongqing Mengniu Dairy Sales Co., Ltd. (i) (重慶市蒙牛乳業銷售有限公司)	Registered capital	Mainland China	37%	38%	Trading of dairy products
Hefei Mengniu Dairy Sales Co., Ltd. (i) (合肥市蒙牛乳業銷售有限公司)	Registered capital	Mainland China	46%	38%	Trading of dairy products

18. INTERESTS IN ASSOCIATES *(continued)*

Details of the Group's associates at 31 December 2008 are set out below: *(continued)*

Name	Particulars of issued shares held	Place of incorporation/ registration and operations	Percentage of equity interest attributable to the Group (indirect) 2008	2007	Principal activities
Shijiazhuang Jinmengyuan Trading Co., Ltd. (i) (石家莊金蒙源貿易有限責任公司)	Registered capital	Mainland China	42%	38%	Trading of dairy products
Beijing Mengniu Technical Development Co., Ltd. (i) (ii) (北京蒙牛科技發展有限公司)	Registered capital	Mainland China	19%	17%	Technical development
Wulumuqi Mengniu Dairy Sales Co., Ltd. (i) (烏魯木齊蒙牛乳業銷售有限公司)	Registered capital	Mainland China	37%	34%	Trading of dairy products
Kunming Deluxe Commercial Trading Co., Ltd. (i) (昆明特侖蘇商貿有限公司)	Registered capital	Mainland China	42%	38%	Trading of dairy products
Changsha Mengniu Dairy Co., Ltd. (i) (長沙市蒙牛乳業有限責任公司)	Registered capital	Mainland China	37%	34%	Trading of dairy products
Xi'an Mengniu Dairy Sales Co., Ltd. (i) (西安蒙牛乳業銷售有限公司)	Registered capital	Mainland China	43%	39%	Trading of dairy products
Changchun Mengniu Dairy Sales Co., Ltd. (i) (長春蒙牛乳品銷售有限公司)	Registered capital	Mainland China	42%	38%	Trading of dairy products
Xuzhou Mengniu Dairy Sales Co., Ltd. (i) (徐州蒙牛乳業銷售有限公司)	Registered capital	Mainland China	37%	34%	Trading of dairy products
Foshan Mengniu Dairy Sales Co., Ltd. (i) (佛山市蒙牛乳業銷售有限公司)	Registered capital	Mainland China	33%	38%	Trading of dairy products

18. INTERESTS IN ASSOCIATES *(continued)*

Details of the Group's associates at 31 December 2008 are set out below: *(continued)*

Name	Particulars of issued shares held	Place of incorporation/ registration and operations	Percentage of equity interest attributable to the Group (indirect) 2008	2007	Principal activities
Guiyang Mengniu Dairy Trading Co., Ltd. (i) (貴陽蒙牛乳業貿易有限公司)	Registered capital	Mainland China	42%	38%	Trading of dairy products
Shengyang Mengniu Dairy Sales Co., Ltd. (i) (ii) (瀋陽蒙牛乳業銷售有限公司)	Registered capital	Mainland China	19%	17%	Trading of dairy products
Xiangfan Mengniu Dairy Sales Co., Ltd. (i) (襄樊市蒙牛乳業銷售有限公司)	Registered capital	Mainland China	46%	41%	Trading of dairy products
Hangzhou Mengniu Dairy Trading Co., Ltd. (i) (杭州蒙牛貿易有限公司)	Registered capital	Mainland China	42%	38%	Trading of dairy products
Suzhou Mengniu Dairy Sales Co., Ltd. (i) (蘇州蒙牛乳製品銷售有限公司)	Registered capital	Mainland China	42%	38%	Trading of dairy products
Guangzhou Mengniu Dairy Sales Co., Ltd. (i) (廣州市蒙牛乳業銷售有限公司)	Registered capital	Mainland China	29%	26%	Trading of dairy products
Shanghai Mengniu Food Sales Co., Ltd. (i) (上海蒙牛食品銷售有限公司)	Registered capital	Mainland China	42%	38%	Trading of dairy products
Hohhot Menglai Trading Co., Ltd. (i) (呼和浩特市蒙萊商貿有限責任公司)	Registered capital	Mainland China	42%	38%	Trading of dairy products
Cangzhou Mengniu Dairy Sales Co., Ltd. (i) (滄州市蒙牛乳業銷售有限公司)	Registered capital	Mainland China	42%	38%	Trading of dairy products

18. INTERESTS IN ASSOCIATES *(continued)*

Details of the Group's associates at 31 December 2008 are set out below: *(continued)*

Name	Particulars of issued shares held	Place of incorporation/ registration and operations	Percentage of equity interest attributable to the Group (indirect) 2008	2007	Principal activities
Changsha Mengniu Frealth Dairy Sales Co., Ltd. (i) (長沙蒙牛友芝友乳業銷售有限公司)	Registered capital	Mainland China	42%	–	Trading of dairy products
Changsha Mengniu Ice Cream Sales Co. Ltd. (i) (長沙蒙牛冰淇淋銷售有限公司)	Registered capital	Mainland China	42%	–	Trading of dairy products
Wuhan Mengniu Hongtai Sales Co., Ltd. (i) (武漢蒙牛宏泰食品銷售有限公司)	Registered capital	Mainland China	42%	–	Trading of dairy products
Nanjing Wanjiahao Mengniu Ice Cream Sales Co., Ltd. (i) (南京萬家好蒙牛冰淇淋銷售有限公司)	Registered capital	Mainland China	42%	–	Trading of dairy products
Hefei Mengniu Ice Cream Sales Co., Ltd. (i) (合肥蒙牛冰淇淋銷售有限公司)	Registered capital	Mainland China	42%	–	Trading of dairy products
Nanjing Mengniu Low Temperature Dairy Products Sales Co., Ltd. (i) (南京蒙牛乳業低溫乳品銷售有限公司)	Registered capital	Mainland China	42%	–	Trading of dairy products

(i) Not audited by Ernst & Young Hong Kong or other member firm of the Ernst & Young global network.

(ii) Since more than 20% of the equity interest of the associates was held by Mengniu, in which the Company held a 93.29% equity interest, the Company had significant influence over the associates even with less than 20% of equity interest held indirectly as at the balance sheet date.

18. INTERESTS IN ASSOCIATES *(continued)*

The following table illustrates the summarised financial information of the Group's associates extracted from their unaudited management accounts:

	2008 RMB'000	2007 RMB'000
Share of the associates' assets and liabilities:		
Current assets	**90,590**	148,778
Non-current assets	**10,619**	81,430
Current liabilities	**(61,102)**	(134,305)
Non-current liabilities	**–**	(38,330)
Net assets	**40,107**	57,573
Share of the associates' revenues and profits and losses:		
Revenues	**1,610,702**	1,494,631
Profits and losses	**29,447**	20,954

19. INTEREST IN A JOINTLY CONTROLLED ENTITY

Details of the Company's jointly controlled entity are set out below:

Name	Particulars of issued shares held	Place of establishment and operations	Percentage of equity interest attributable to the Group (indirect) 2008	2007	Principal activities
Mengniu Arla (Inner Mongolia) Dairy Products Co. Ltd. (i) (內蒙古蒙牛阿拉乳製品有限責任公司)	Registered capital	Mainland China	46.65%	42.16%	Manufacture and sale of dairy products

(i) Not audited by Ernst & Young Hong Kong or other member firm of the Ernst & Young global network.

19. INTEREST IN A JOINTLY CONTROLLED ENTITY *(continued)*

The share of the assets, liabilities, income and expenses of the jointly controlled entity at 31 December 2008 and for the year then ended, which is included in the consolidated financial statements, is as follows:

	2008 *RMB'000*	2007 *RMB'000*
Share of the assets and liabilities:		
Current assets	**68,448**	54,825
Non-current assets	**236,795**	193,819
Current liabilities	**(164,662)**	(125,460)
Non-current liabilities	**(65,308)**	(40,000)
Net assets	**75,273**	83,184
Share of the revenue and loss:		
Revenue	**145,035**	164,181
Cost of sales and operating expenses	**(232,861)**	(196,213)
Loss	**(87,826)**	(32,032)

20. AVAILABLE-FOR-SALE INVESTMENTS

	Group	
	2008 *RMB'000*	2007 *RMB'000*
Unlisted equity investments, at cost	**18,029**	17,316

21. GOODWILL

	Group	
	2008 *RMB'000*	2007 *RMB'000*
Carrying amount at 1 January	**199,143**	115,549
Acquisition of a minority interest (a)	**–**	83,594
Carrying amount at 31 December	**199,143**	199,143

(a) On 3 April 2007, the Group entered into an agreement to acquire a 48% equity interest in Mengniu (Wuhan) Frealth Dairy Co., Ltd. ("Mengniu Wuhan") from a minority shareholder at a consideration of RMB134,400,000. The acquisition gave rise to goodwill of RMB83,594,000. After the acquisition, Mengniu Wuhan became a wholly-owned subsidiary of Inner Mongolia Mengniu Dairy (Group) Company Limited. Details of the acquisition were disclosed in the Company's announcement dated 4 April 2007.

21. GOODWILL *(continued)*

Goodwill acquired through business combinations has been allocated to the following cash-generating units (the "CGUs"), which are reportable segments, for impairment testing:

– liquid milk products CGU;

– ice cream products CGU; and

– other dairy products CGU.

The recoverable amount of each CGU has been determined based on a value in use calculation using cash flow projections based on financial budgets or forecasts approved by senior management covering a five-year period. The growth rates used to extrapolate the cash flows beyond the five-year period are based on the estimated growth rate of each unit taking into account of the industry growth rate, past experience and the medium or long term growth target of each CGU. The growth rates for these CGUs are higher than the respective average industry growth rates. Senior management believes such growth rates are justified because:

– the growth rates of these CGUs have significantly exceeded those in the market in the past years;

– the new product launch and new market expansion have been successful in the past;

– strong brand equity and marketing capability contributing to the continuous growth in market share in past years; and

– expertise on product innovation, portfolio enhancement and marketing will be further leveraged.

The discount rates applied to cash flow projections and the growth rates used to extrapolate cash flows beyond the five-year period are as follows:

	Discount rate		**Growth rate**	
	2008	2007	**2008**	2007
Liquid milk products CGU	**12.04%**	10.8%	**4.0%**	6.0%
Ice cream products CGU	**12.06%**	10.8%	**3.0%**	3.0%
Other dairy products CGU	**11.64%**	10.8%	**4.0%**	6.0%

The carrying amounts of goodwill of approximately RMB199,143,000 (2007: RMB199,143,000) at 31 December 2008 allocated to the liquid milk products CGU, ice cream products CGU and other dairy products CGU were approximately RMB167,433,000 (2007: RMB167,433,000), RMB23,865,000 (2007: RMB23,865,000) and RMB7,845,000 (2007: RMB7,845,000), respectively.

21. GOODWILL *(continued)*

Key assumptions were used in the value in use calculation of each CGU. The following describes each key assumption on which management has based its cash flow projections to undertake impairment testing of goodwill:

(a) Budgeted gross margins – The basis used to determine the value assigned to the budgeted gross margins is the average gross margins achieved in the year immediately before the budget year, adjusted for expected efficiency improvements and expected increase in production costs.

(b) Discount rates – The discount rates used are before tax and reflect specific risks relating to the relevant CGUs.

(c) Raw materials price fluctuation – Reference is made to the actual past year data of countries from where raw materials are sourced.

The values assigned to key assumptions are consistent with external information sources.

22. DEFERRED TAX ASSETS

	Group	
	2008	2007
	RMB'000	*RMB'000*
At 1 January	**6,302**	–
Deferred tax credited to the consolidated income statement during the year (note 9)	**180,579**	6,302
Gross deferred tax assets at 31 December	**186,881**	6,302

Deferred income tax assets at 31 December 2008 related to the following:

	Consolidated balance sheet		Consolidated income statement	
	2008	2007	**2008**	2007
	RMB'000	*RMB'000*	***RMB'000***	*RMB'000*
Losses available for offseting against future taxable profits	**150,889**	–	**150,889**	–
Write-down of inventories to net realisable value	**26,992**	–	**26,992**	–
Un-invoiced accruals	**9,000**	6,302	**2,698**	6,302
Deferred tax assets	**186,881**	6,302		
Deferred income tax income			**180,579**	6,302

22. DEFERRED TAX ASSETS *(continued)*

Management expects it is probable that taxable profit will be available against which the above tax losses and deductible temporary differences can be utilised in the coming years.

Deferred tax assets have not been recognised in respect of the following items:

	Group	
	2008	2007
	RMB'000	*RMB'000*
Tax losses arising in Mainland China (i)	**203,317**	41,501
Tax credits related to purchases of domestic equipment (ii)	**88,814**	88,814
Deductible temporary differences	**172,063**	203,057
	464,194	333,372

(i) Tax losses can be carried forward over five years to offset the future taxable profit.

(ii) Tax credits can be carried forward over five to seven years to offset the tax payables if the future year tax exceeded the base year tax.

Pursuant to the New Tax Law, a 10% withholding tax is levied on dividends declared to foreign investors from the foreign investment enterprises established in Mainland China. The requirement is effective from 1 January 2008 and applies to earnings after 31 December 2007. A lower withholding tax rate may be applied if there is a tax treaty between China and jurisdiction of the foreign investors. For the Group, the applicable rate is 5%. The Group is therefore liable to withholding taxes on dividends distributed by those subsidiaries established in Mainland China in respect of earnings generated from 1 January 2008.

At 31 December 2008, no deferred tax liabilities have been recognised for the withholding taxes that would be payable on the unremitted earnings by Mengniu and other subsidiaries whose certain interests were directly held by the Company which were established in Mainland China as these subsidiaries incurred losses in 2008.

At 31 December 2008, there was no significant unrecognised deferred tax liabilities (2007: Nil) for taxes that would be payable on the unremitted earnings of certain of Mengniu's subsidiaries and associates, as Mengniu has no liability to additional tax should such amount be remitted.

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

Except for the amount disclosed above, the Group and the Company did not have any material unrecognised deferred tax liabilities or deferred tax assets at 31 December 2008.

23. OTHER FINANCIAL ASSETS

Other financial assets represented entrusted loans to certain dairy farmers via banks. A maturity analysis of the entrusted loans of the Group is as follows:

	Group	
	2008	2007
	RMB'000	*RMB'000*
Within 1 year	**9,413**	16,728
1 to 2 years	**8,460**	6,692
2 to 3 years	**9,873**	8,742
Over 3 years	**–**	5,705
Total entrusted loans	**27,746**	37,867
Less: Amount due within one year included in current assets under other receivables (note 28)	**(9,413)**	(16,728)
	18,333	21,139

The annual interest rates of the entrusted loans varied from 6.0% to 7.7% (2007: 6.0% to 7.2%).

24. INVENTORIES

	Group	
	2008	2007
	RMB'000	*RMB'000*
Raw materials	**483,765**	486,056
Finished goods	**340,688**	391,387
Total inventories at the lower of cost and net realisable value	**824,453**	877,443

The amount of write-down of inventories recognised as an expense was RMB179,873,000 (2007: RMB4,413,000) which was recognised in other operating expenses (note 5).

25. BILLS RECEIVABLE

An aged analysis of the bills receivable as at the balance sheet date, based on the invoice date, is as follows:

	Group	
	2008 RMB'000	2007 RMB'000
Within 3 months	**64,678**	114,832
4 to 6 months	**100**	50
	64,778	114,882

As at 31 December 2008, the bills receivable amounting to approximately RMB50,000,000 (2007: RMB77,250,000) were factored with recourse to financial institutions. The corresponding amount was recorded as short term bank loans (note 33).

The amounts due from associates of approximately RMB488,000 (2007: RMB12,069,000) are included in the above balances.

26. TRADE RECEIVABLES

	Group	
	2008 RMB'000	2007 RMB'000
Trade receivables	**285,823**	265,187
Impairment	**(1,744)**	(3,822)
	284,079	261,365

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

26. TRADE RECEIVABLES *(continued)*

An aged analysis of the trade receivables of the Group, net of provision for doubtful debts, based on the invoice date, is as follows:

	Group	
	2008	2007
	RMB'000	*RMB'000*
Within 3 months	**251,774**	226,011
4 to 6 months	**25,587**	24,136
7 to 12 months	**5,716**	10,828
Over 1 year	**1,002**	390
	284,079	261,365

The movements in provision for impairment of trade receivables are as follows:

	Group	
	2008	2007
	RMB'000	*RMB'000*
At 1 January	**3,822**	11,661
Impairment losses recognised	**587**	476
Amount written off as uncollectible	**(398)**	(33)
Impairment losses reversed	**(2,267)**	(8,282)
At 31 December	**1,744**	3,822

The aged analysis of the trade receivables that are not considered to be impaired is as follows:

	Group	
	2008	2007
	RMB'000	*RMB'000*
Neither past due nor impaired	**247,008**	234,144
Past due but not impaired		
Within 3 months	**6,663**	21,437
	253,671	255,581

26. TRADE RECEIVABLES *(continued)*

Receivables that were neither past due nor impaired relate to a large number of diversified customers for whom there was no recent history of default.

Receivables that were past due but not impaired relate to a number of independent customers that have a good track record with the Group. Based on past experience, the directors of the Company are of the opinion that no provision for impairment is necessary in respect of these balances as there has not been a significant change in credit quality and the balances are still considered fully recoverable. The Group does not hold any collateral or other credit enhancements over these balances.

The amounts due from associates of approximately RMB137,244,000 (2007: RMB82,480,000) and an amount due from a jointly-controlled entity of approximately RMB9,257,000 (2007: RMB4,847,000) are included in the above balances. These balances are unsecured, non-interest-bearing and are repayable on credit terms similar to those offered to other major customers of the Group.

27. PREPAYMENTS AND DEPOSITS

	Group	
	2008	2007
	RMB'000	*RMB'000*
Deposits	**2,218**	1,869
Prepayments	**137,716**	207,731
Value-added tax recoverable	**185,651**	–
Corporate income tax recoverable	**43,362**	–
Land use rights – current portion (note 16)	**5,957**	4,764
	374,904	214,364

The amount due from an associate of approximately RMB1,449,000 (2007: RMB2,639,000) is included in the above balances.

28. OTHER RECEIVABLES

The balance of other receivables can be analysed as follows:

	Group	
	2008	2007
	RMB'000	*RMB'000*
Dividends receivable	**11,216**	–
Other financial assets (note 23)	**9,413**	16,728
Others	**70,050**	23,470
Total	**90,679**	40,198

	Company	
	2008	2007
	RMB'000	*RMB'000*
Loan to a subsidiary	**955,198**	281,151
Others	**86**	–
Total	**955,284**	281,151

The loan to a subsidiary included in other receivables above is unsecured, interest-bearing and repayable within one year. The carrying amount of the loan to a subsidiary approximates to its fair value.

29. CASH AND BANK BALANCES AND PLEDGED DEPOSITS

	Group	
	2008	2007
	RMB'000	*RMB'000*
Cash and cash equivalents	**2,218,965**	1,756,818
Pledged deposits	**41,693**	44,506
Time deposits with original maturity of more than three months	**823,000**	454,000
	3,083,658	2,255,324
Less: Deposits pledged for banking facilities (note 31)	**(41,693)**	(44,506)
Cash and bank balances	**3,041,965**	2,210,818

	Company	
	2008	2007
	RMB'000	*RMB'000*
Cash and bank balances	**54,058**	737,085

Cash at banks earns interest at the prevailing market interest rates. The bank balances and pledged deposits are deposited with creditworthy banks with no recent history of default. Cash and bank balances amounting to approximately RMB2,991,463,000 (2007: RMB1,481,977,000) were denominated in Renminbi, which is not freely convertible in the international foreign exchange market and its exchange rate is determined by the People's Bank of China.

30. TRADE PAYABLES

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

	Group	
	2008	2007
	RMB'000	*RMB'000*
Within 3 months	**2,033,138**	1,238,629
4 to 6 months	**112,082**	65,590
7 to 12 months	**8,289**	7,904
Over 1 year	**1,756**	3,272
	2,155,265	1,315,395

An amount due to an associate of approximately RMB306,000 (2007: RMB1,924,000) is included in the above balances. The balance is unsecured, non-interest-bearing and repayable on demand.

The Group's trade payables are unsecured and non-interest-bearing.

31. BILLS PAYABLE

An aged analysis of the bills payable of the Group, based on the invoice date, is as follows:

	Group	
	2008	2007
	RMB'000	*RMB'000*
Within 3 months	**239,145**	164,684
4 to 6 months	**200**	94,381
	239,345	259,065

Except for an aggregate balance of approximately RMB161,528,000 (2007: RMB74,038,000) secured by the pledge of certain of the Group's deposits amounting to approximately RMB39,139,000 (2007: RMB15,341,000) (note 29), bills payable are unsecured. The above balances are non-interest-bearing.

32. ACCRUALS AND CUSTOMERS' DEPOSITS

	Group	
	2008	2007
	RMB'000	*RMB'000*
Advances from customers	**609,639**	402,096
Salary and welfare payables	**135,896**	142,566
	745,535	544,662

The amounts due to associates of approximately RMB87,278,000 (2007: RMB69,155,000) are included in the above balances. The balances are unsecured, non-interest-bearing and are repayable on demand.

33. INTEREST-BEARING BANK LOANS

	Group					
	2008			2007		
	Maturity	Fixed rate *RMB'000*	Floating rate *RMB'000*	Maturity	Fixed rate *RMB'000*	Floating rate *RMB'000*
Short term bank loans, secured	**2009**	**50,000**	**–**	2008	77,250	–
Short term bank loans, unsecured	**2009**	**670,252**	**488,408**	2008	72,305	33,601
Long term bank loans, unsecured	**2010-2011**	**–**	**520,000**	2009-2010	–	80,000
		720,252	**1,008,408**		149,555	113,601

At 31 December 2008, short term bank loans of approximately RMB50,000,000 (2007: RMB77,250,000) were secured by certain bills receivable of the Group (note 25).

During the year, the annual interest rates of the short term bank loans and the long term bank loans varied from 5.02% to 6.93% and from 3.53% to 7.43% (2007: varied from 3.00% to 6.48% and from 3.00% to 6.90%), respectively. As at 31 December 2008, except for a short term bank loan of US$4,925,000 equivalent to approximately RMB33,660,000 (2007: US$5,600,000) denominated in United States dollars, all the Group's interest-bearing bank loans were denominated in RMB.

33. INTEREST-BEARING BANK LOANS *(continued)*

The repayment schedule of the bank loans is as follows:

	Group	
	2008	2007
	RMB'000	*RMB'000*
Within 1 year	**1,208,660**	183,156
1 to 2 years	**400,000**	20,000
2 to 5 years	**120,000**	60,000
Total interest-bearing bank loans	**1,728,660**	263,156
Less: Amount due within 1 year included in current liabilities	**(1,208,660)**	(183,156)
	520,000	80,000

34. OTHER LOANS

	Group	
	2008	2007
	RMB'000	*RMB'000*
Short term, unsecured	**72,942**	36,004

The other loans represented unsecured and interest-free loans from various local government authorities to support the Group's establishment of production plants in various locations in the PRC.

35. LONG TERM PAYABLES

The Group's long term payables represent the amortised costs of the outstanding instalments payable for the purchase of production equipment. The effective interest rate used for the amortisation is the prevailing market interest rate. The balances are repayable as follows:

	Group	
	2008	2007
	RMB'000	*RMB'000*
Within 1 year	**168,795**	171,939
1 to 2 years	**84,910**	141,609
2 to 5 years	**20,254**	82,583
Over 5 years	**2,824**	–
Total long term payables	**276,783**	396,131
Less: Amount due within 1 year included in current liabilities under other payables	**(168,795)**	(171,939)
	107,988	224,192

Certain long term payables are secured by the Group's property, plant and equipment (note 13(b)).

36. DEFERRED INCOME

Various local government authorities have granted certain property, plant and equipment to the Group for nil consideration and provided finance to the Group to purchase certain property, plant and equipment by way of a cash donation. Both the property, plant and equipment and grants are recorded initially at fair value. The grants received are regarded as deferred income, which is amortised to match the depreciation charge of such property, plant and equipment granted or purchased in accordance with their estimated useful lives. Movements of the balances during the year are as follows:

	Group	
	2008	2007
	RMB'000	*RMB'000*
At beginning of year	**190,745**	128,388
Received during the year	**17,928**	73,173
Amortisation during the year	**(12,545)**	(10,816)
At end of year	**196,128**	190,745
Current portion	**12,918**	11,752
Non-current portion	**183,210**	178,993
	196,128	190,745

37. SHARE CAPITAL

	2008 RMB'000	2007 RMB'000
Authorised:		
3,000,000,000 ordinary shares of HK$0.1 each	**319,235**	319,235

	Notes	**Number of ordinary shares** *'000*	*RMB'000*
At 1 January 2008		**1,426,120**	**151,277**
Issue of shares	(a)	**135,328**	**11,843**
Shares issued under the employee share option scheme	(b)	**192**	**17**
At 31 December 2008		**1,561,640**	**163,137**

	Notes	**Number of ordinary shares** *'000*	*RMB'000*
At 1 January 2007		1,368,416	145,573
Issue of shares	(c)	57,460	5,682
Shares issued under employee share option scheme	(b)	244	22
At 31 December 2007		1,426,120	151,277

37. SHARE CAPITAL *(continued)*

(a) On 25 July 2008, the Company acquired an additional 8.97% equity interest in Mengniu from certain sellers (the "Sellers") by allotting and issuing 135,328,255 ordinary shares of the Company (the "Consideration Shares") to the Sellers with a par value of HK$0.1 each. The Consideration Shares represented approximately 9.49% and 8.67% of the issued share capital of the Company as at 25 July 2008, prior to and post the issue of the Consideration Shares, respectively.

The closing stock price of the Company on 25 July 2008 was HK$23.50 (equivalent to RMB20.57) per share, resulting in proceeds of approximately HK$3,180,214,000 (equivalent to approximately RMB2,783,037,000). The placing gave rise to a share premium of HK$3,166,681,000 (equivalent to approximately RMB2,771,194,000), being the excess of the gross proceeds over the par value of the new shares issued of HK$13,532,826 (equivalent to approximately RMB11,843,000) in the financial statements of the Company.

The carrying amount of the additional interest of Mengniu acquired by the Company was RMB433,984,000 on 25 July 2008. The excess of fair value of the ordinary share of the Company issued to effect the acquisition over the carrying amount of the additional interest acquired by the Company of RMB2,349,053,000 was recognised by the Group in the share premium account, resulting in a net impact of RMB422,141,000 to the consolidated share premium account as a result of the acquisition of an additional interest in Mengniu.

(b) Details of the Company's share option scheme and the share options issued under the scheme are included in note 40 to the financial statements.

(c) On 26 April 2007, the Company completed the placing of 57,460,000 new shares of the Company with a par value of HK$0.1 each at the placing price of HK$24 (equivalent to RMB23.73) per share, resulting in proceeds, net of share issue expenses, of approximately HK$1,363,404,000 (equivalent to approximately RMB1,348,229,000). The placing gave rise to a share premium of HK$1,357,658,000 (equivalent to approximately RMB1,342,547,000), being the excess of the gross proceeds less share issue expenses over the par value of the new shares issued of HK$5,746,000 (equivalent to approximately RMB5,682,000).

38. RESERVES

(A) Group

Movements in the other reserves of the Group during the year are as follows:

	Share premium RMB'000	Contributed surplus RMB'000 Note (a)	Statutory reserves RMB'000 Note (b)	Currency translation differences RMB'000	Share option reserve RMB'000 Note 40	Total RMB'000
At 1 January 2007	1,127,581	232,020	495,063	1,697	3,108	1,859,469
Issue of shares	1,342,547	–	–	–	–	1,342,547
Transfer to statutory reserves	–	–	225,855	–	–	225,855
Shares issued under equity-settled share option arrangements	3,044	–	–	–	–	3,044
Currency translation differences	–	–	–	(57,529)	–	(57,529)
Equity-settled share option arrangements	–	–	–	–	39,233	39,233
At 1 January 2008	**2,473,172**	**232,020**	**720,918**	**(55,832)**	**42,341**	**3,412,619**
Issue of shares for acquisition of additional interests in a subsidiary (note 37)	**422,141**	**–**	**–**	**–**	**–**	**422,141**
Transfer to statutory reserves	**–**	**–**	**47,911**	**–**	**–**	**47,911**
Shares issued under equity-settled share option arrangements	**2,245**	**–**	**–**	**–**	**–**	**2,245**
Currency translation differences	**–**	**–**	**–**	**(81,614)**	**–**	**(81,614)**
Equity-settled share option arrangements	**–**	**–**	**–**	**–**	**134,622**	**134,622**
At 31 December 2008	**2,897,558**	**232,020**	**768,829**	**(137,446)**	**176,963**	**3,937,924**

38. RESERVES *(continued)*

(B) Company

Movements in the reserves of the Company during the year are as follows:

	Share premium *RMB'000*	Contributed surplus *RMB'000* Note (a)	Currency translation differences *RMB'000*	Retained earnings *RMB'000*	Share option reserve *RMB'000* Note 40	Total *RMB'000*
At 1 January 2007	1,127,581	387,574	3,364	51,494	3,108	1,573,121
Profit for the year (note (d))	–	–	–	210,743	–	210,743
Dividends paid	–	–	–	(156,020)	–	(156,020)
Issue of shares	1,342,547	–	–	–	–	1,342,547
Shares issued under equity-settled share option arrangements	3,044	–	–	–	–	3,044
Equity-settled share option arrangements	–	–	–	–	39,233	39,233
Currency translation differences	–	–	(271,377)	–	–	(271,377)
At 1 January 2008	**2,473,172**	**387,574**	**(268,013)**	**106,217**	**42,341**	**2,741,291**
Profit for the year (note (d))	**–**	**–**	**–**	**203,319**	**–**	**203,319**
Dividends paid	**–**	**–**	**–**	**(187,667)**	**–**	**(187,667)**
Issue of shares for acquisition of additional interest in a subsidiary	**2,771,194**	**–**	**–**	**–**	**–**	**2,771,194**
Shares issued under equity-settled share option arrangements	**2,245**	**–**	**–**	**–**	**–**	**2,245**
Equity-settled share option arrangements	**–**	**–**	**–**	**–**	**134,622**	**134,622**
Currency translation differences	**–**	**–**	**(154,165)**	**–**	**–**	**(154,165)**
At 31 December 2008	**5,246,611**	**387,574**	**(422,178)**	**121,869**	**176,963**	**5,510,839**

Notes:

(a) Contributed surplus

The balance of the contributed surplus of the Group represents the difference between the nominal value of the share capital of the subsidiaries acquired pursuant to the group reorganisation over the nominal value of the shares of the Company issued in exchange therefore and the excess of the amount of capital injected by the minority shareholder over its additional interest in the subsidiary's net assets attributable to the Company's equity holders was recorded as contributed surplus of the Group.

The contributed surplus of the Company represents the difference between the then combined net asset value of the subsidiaries acquired pursuant to the group reorganisation over the nominal value of the shares of the Company issued in exchange therefor.

38. RESERVES *(continued)*

(B) Company *(continued)*

Notes: *(continued)*

(b) Statutory reserves

In accordance with the relevant PRC laws and regulations, the PRC domestic companies are required to transfer 10% of their profit after income tax, as determined under the PRC accounting standards and financial regulations, to the statutory common reserve. Subject to certain restrictions as set out in the relevant PRC laws and regulations, the statutory common reserve may be used to offset against the accumulated losses, if any.

(c) Distributable reserves

Under the Companies Law (2004 Revision) of the Cayman Islands, the share premium and contributed surplus of the Company are distributable to shareholders, provided that immediately following the distribution of the dividend, the Company is able to pay off its debts as and when they fall due in the ordinary course of business.

(d) The profit attributable to equity holders of the Company for the year ended 31 December 2008 dealt with in the financial statements of the Company was RMB203,319,000 (2007: RMB210,743,000), including the dividend income from subsidiaries amounting to approximately RMB169,116,000(2007: RMB192,079,000).

39. NON-CASH TRANSACTIONS

In addition to the non-cash transactions detailed elsewhere in these financial statements, during the year, the Group purchased property, plant and equipment by means of long term payables amounting to approximately RMB89,696,000 (2007: RMB150,685,000).

40. SHARE-BASED PAYMENT PLAN

The Company operates a share option scheme (the “Scheme”) for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group’s operations. Eligible participants of the Scheme include the Company’s directors, including independent non-executive directors, other employees of the Group, suppliers of goods or services to the Group, customers and any person or entity that provides research, development or technological support to the Group. The Scheme became effective on 28 June 2005 and, unless otherwise cancelled or amended, will remain in force for 10 years from that date.

The maximum number of shares in respect of share options currently permitted to be granted under the Scheme is an amount equivalent, upon their exercise, to 10% of the total number of shares of the Company in issue as at 28 June 2005, which is approximately 136,842,000 shares. The maximum number of shares issuable under share options to each eligible participant in the Scheme within any 12-month period is limited to 1% of the total shares of the Company in issue at any time. Any further grant of share options in excess of these limits is subject to shareholders’ approval in a general meeting.

40. SHARE-BASED PAYMENT PLAN *(continued)*

Share options granted to a director, chief executive or substantial shareholder of the Company, or to any of their associates, are subject to approval in advance by the independent non-executive directors. In addition, any share options granted to a substantial shareholder or an independent non-executive director of the Company, or to any of their associates, in excess of 0.1% of the shares of the Company in issue at any time or with an aggregate value (based on the closing price of the Company's shares at the date of grant) in excess of HK$5,000,000, within any 12-month period, are subject to shareholders' approval in advance in a general meeting.

The offer of a grant of share options may be accepted within 20 business days from the date of offer, upon payment of a consideration of HK$1 in total by the grantee. The exercise period of the share options granted is determinable by the directors, and commences after a certain vesting period and ends on a date which is not later than six years from the date of offer of the share options or the expiry date of the Scheme, if earlier.

The exercise price of share options is determinable by the directors, but may not be less than the highest of (i) The Stock Exchange of Hong Kong Limited (the "Stock Exchange") closing price of the Company's shares on the offer date of the share options; (ii) the average Stock Exchange closing price of the Company's shares for the five business days immediately preceding the offer date; and (iii) the nominal value of the shares.

Share options do not confer rights on the holders to dividends or to vote at shareholders' meetings.

Particulars of share options

Date of grant	**Exercise period of share options (both dates inclusive)**	**Exercise price per share option** (note c)
		(HK$)
26 October 2006	26 October 2007 to 25 October 2012 (note a)	13.40
9 November 2007	9 November 2009 to 8 November 2013 (note b)	32.24
18 August 2008	18 August 2010 to 17 August 2014 (note b)	22.03

(a) The share options will be vested in four equal batches with 25% of the share options granted vesting on the first, second, third and forth anniversary of the date of grant. In addition, the share options will only be vested if and when the pre-set performance targets of the Group, the division of the grantee and the grantee are achieved. Unless all of these targets are met, the share options will lapse.

(b) The share options will be vested in two equal batches with 50% of the share options granted vesting on the second and third anniversary of the date of grant. In addition, the share options will only be vested if and when the pre-set performance targets of the Group, the division of the grantee and the grantee are achieved. Unless all of these targets are met, the share options will lapse.

(c) The exercise price per share option was the average closing share price for the five business days immediately preceding the grant date.

40. SHARE-BASED PAYMENT PLAN *(continued)*

Movements of share options

2008

Date of grant	**As at 1 January 2008**	**Granted during the year**	**Exercised during the year**	**Lapsed during the year**	**As at 31 December 2008**
26 October 2006	**6,254,561**	**–**	**(192,065)**	**(610,095)**	**5,452,401**
9 November 2007	**44,605,000**	**–**	**–**	**(1,473,000)**	**43,132,000**
18 August 2008	**–**	**80,540,000**	**–**	**(1,422,000)**	**79,118,000**
Total	**50,859,561**	**80,540,000**	**(192,065)**	**(3,505,095)**	**127,702,401**

2007

Date of grant	As at 1 January 2007	Granted during the year	Exercised during the year	Lapsed during the year	As at 31 December 2007
26 October 2006	6,803,000	–	(244,351)	(304,088)	6,254,561
9 November 2007	–	44,605,000	–	–	44,605,000
Total	6,803,000	44,605,000	(244,351)	(304,088)	50,859,561

The average fair value of the share options granted during the year is estimated to be RMB6.68 each (2007: RMB9.76) at the grant date, using a binomial model, taking into account the terms and conditions upon which the instruments were granted. The contractual life of each option granted is six years. There are no cash settlement alternatives. The Group recognised an expense of RMB134,622,000 (note 6 and note 7) during the year ended 31 December 2008 (2007: RMB39,233,000).

Subsequent to the balance sheet date, out of the total outstanding share options of 127,702,401 units as at 31 December 2008, 23,098,250 units of share options were lapsed due to the unfullfillment of vesting conditions attached.

40. SHARE-BASED PAYMENT PLAN *(continued)*

The following table lists the inputs to the model used:

	2008	2007
Dividend yield (%)	**1.0**	1.0
Expected volatility (%)	**40**	35
Risk-free interest rate (%)	**3.0**	3.1
Expected life of option (years)	**6**	6
Spot price (HK$)	**21.90**	31.90
Exercise price (HK$)	**22.03**	32.24

In light of the lack of an historical exercise record, the expected life of the options is based on the results of empirical studies performed in the United States and is not necessarily indicative of exercise patterns that may occur. The expected volatility reflects the assumption that the historical volatility is indicative of future trends, which may also not necessarily be the actual outcome. The spot price is the closing price of the Company's shares at the grant date. The exercise price is the average closing share price for the five business days immediately preceding the grant date.

The 192,065 share options (2007: 244,351) exercised during the year resulted in the issue of 192,065 (2007: 244,351) ordinary shares of the Company and new share capital of RMB17,000 (2007: RMB22,000) and share premium of RMB2,245,000 (2007: RMB3,044,000), as further detailed in note 37 to the financial statements. The weighted average share price at the date of exercise for these options was HK$24.70 (2007: HK$32.40).

At the balance sheet date, the Company had 2,387,901 (2007: 1,384,061) share options being vested outstanding under the Scheme. The exercise in full of the remaining share options would, under the present capital structure of the Company, result in the issue of 2,387,901 (2007: 1,384,061) additional ordinary shares of the Company and additional share capital of RMB211,000 (2007: RMB130,000) and share premium of RMB28,008,000 (2007: RMB17,237,000) (before issue expenses).

41. COMMITMENTS

(a) Capital commitments

The Group had the following outstanding capital commitments in respect of the purchase and construction of property, plant and equipment as at the balance sheet date:

	Group	
	2008	2007
	RMB'000	*RMB'000*
Contracted, but not provided for	**100,059**	303,454

Included in the above amount, the commitments of approximately nil (2007: RMB9,287,000) were in relation to the Group's share of a jointly-controlled entity's own capital commitments.

Subsequent to the balance sheet date, the board of directors approved the capital expenditure (not contracted for) amounting to approximately RMB875,750,000 (2007: RMB791,815,000), out of which nil (2007: RMB14,900,000) was related to the Group's interest in a jointly-controlled entity.

(b) Operating lease commitments

At the balance sheet date, the Group had total future minimum lease payments under non-cancellable operating leases in respect of buildings and certain production equipment as follows:

	Group	
	2008	2007
	RMB'000	*RMB'000*
Within one year	**19,225**	6,381
In the second to fifth years, inclusive	**49,381**	11,956
Over five years	**24,798**	5,703
	93,404	24,040

The Company did not have any significant commitments at the balance sheet date.

42. CONTINGENT LIABILITIES

The Group is contingently liable in respect of loan guarantees granted to certain banks in favour of certain suppliers of raw milk (the "Suppliers"). The amount of guarantees granted as at 31 December 2008 was approximately RMB73,820,000 (2007: RMB109,800,000). Approximately RMB73,820,000 (2007: RMB89,800,000) of the above guarantees are cross-guaranteed and secured by assets owned by these suppliers who are independent third parties. Securities under these counter-guarantees included property, dairy cattle and other assets owned by the Suppliers.

Save as the above and the disclosure in note 44(i), the Group did not have any significant contingent liabilities at the balance sheet date.

The Company did not have any significant contingent liabilities at the balance sheet date.

43. FAIR VALUES OF FINANCIAL INSTRUMENTS

The carrying amounts of the Group's financial assets and liabilities (which are classified as current assets and liabilities) approximated to their fair values at 31 December 2008 because of the short maturity of these instruments.

The carrying amounts of the Group's long term interest-bearing borrowings approximated to their fair values based on borrowing rates currently charged for loans with similar terms and maturities.

The carrying amounts of the Group's long term payables approximated to their fair values based on the implicit interest rate currently used to arrive at the cash price for purchase on normal credit terms.

44. RELATED PARTY TRANSACTIONS

In addition to the transactions and balances which are disclosed elsewhere in these financial statements, the Group had the following significant transactions with its associates, a jointly-controlled entity and other related parties.

			Group	
			2008	2007
		Notes	***RMB'000***	*RMB'000*
(a)	Sales of liquid milk products to associates	(i)	**3,627,586**	3,034,343
(b)	Sales of ice cream products to associates	(i)	**337,975**	121,564
(c)	Sales of other dairy products to associates	(i)	**10,890**	2,033
(d)	Purchase of raw materials from an associate	(i)	**(108,232)**	(107,078)
(e)	Sale of raw materials to a jointly-controlled entity	(ii)	**69,720**	30,691
(f)	Purchase of other dairy products from a jointly-controlled entity	(i)	**(6,830)**	–
(g)	Purchase of ice cream products from an associate	(i)	**(65,593)**	(60,436)
(h)	Sale of property, plant and equipment to a jointly-controlled entity	(iii)	**–**	2,881
(i)	Provision of guarantees to a jointly-controlled entity		**2,073**	–

44. RELATED PARTY TRANSACTIONS *(continued)*

Notes:

(i) The considerations were determined with reference to the then prevailing market prices/rates and the prices charged to third parties.

(ii) Such transaction was conducted at cost, which approximated to the prevailing market price of the materials.

(iii) The sales price was determined by reference to the valuation performed by an external valuer.

(iv) The above transactions did not constitute connected transactions as defined in the Listing Rules.

(v) Key management compensation is detailed in note 7 to the financial statements.

45. FINANCIAL INSTRUMENTS BY CATEGORY

The carrying amounts of each of the categories of financial instruments as at the balance sheet date are as follows:

Financial assets

	Group					
	2008			2007		
	Loans and receivables	**Available-for-sale financial assets**	**Total**	Loans and receivables	Available-for-sale financial assets	Total
	RMB'000	***RMB'000***	***RMB'000***	*RMB'000*	*RMB'000*	*RMB'000*
Available-for-sale investments	**–**	**18,029**	**18,029**	–	17,316	17,316
Bills receivable	**64,778**	**–**	**64,778**	114,882	–	114,882
Trade receivables	**284,079**	**–**	**284,079**	261,365	–	261,365
Other receivables	**90,679**	**–**	**90,679**	40,198	–	40,198
Other financial assets	**18,333**	**–**	**18,333**	21,139	–	21,139
Pledged deposits	**41,693**	**–**	**41,693**	44,506	–	44,506
Cash and bank balances	**3,041,965**	**–**	**3,041,965**	2,210,818	–	2,210,818
	3,541,527	**18,029**	**3,559,556**	2,692,908	17,316	2,710,224

45. FINANCIAL INSTRUMENTS BY CATEGORY *(continued)*

Financial liabilities

	Group	
	2008	2007
	Financial liabilities at amortised cost	Financial liabilities at amortised cost
	RMB'000	*RMB'000*
Trade payables	**2,155,265**	1,315,395
Bills payable	**239,345**	259,065
Other payables	**1,048,792**	1,013,171
Interest-bearing bank loans	**1,728,660**	263,156
Other loans	**72,942**	36,004
Long term payables	**107,988**	224,192
	5,352,992	3,110,983

The carrying amounts of each of the categories of financial instruments as at balance sheet date are as follows:

Financial assets

	Company	
	2008	2007
	Loans and receivables	Loans and receivables
	RMB'000	*RMB'000*
Loan to a subsidiary included in interests in subsidiaries (note 17)	**806,136**	855,945
Financial assets included in prepayments, deposits and other receivables	**955,284**	281,151
Cash and cash equivalents	**54,058**	737,085
	1,815,478	1,874,181

45. FINANCIAL INSTRUMENTS BY CATEGORY *(continued)*

Financial liabilities

	Company	
	2008 Financial liabilities at amortised cost *RMB'000*	2007 Financial liabilities at amortised cost *RMB'000*
Financial liabilities included in accruals and other payables	**2,914**	1,665

46. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

Capital management

The primary objective of the Group's capital management is to safeguard the Group's ability to continue as a going concern and to maintain healthy capital ratios in order to support its business and maximise shareholders' value.

The Group manages its capital structure and makes adjustments to it, in light of changes in economic conditions. To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares. No changes were made in the objectives, policies or processes for managing capital during the years ended 31 December 2008 and 31 December 2007.

The Group monitors capital using a gearing ratio, which is net debt divided by the total capital plus net debt. The Group's policy is to maintain the gearing ratio between 20% and 50% normally. Net debt includes interest-bearing bank loans and other loans, trade, bills and other payables, accruals, less cash and bank balances, and excludes discontinued operations. Capital represents equity attributable to equity holders of the Company. The gearing ratios as at the balance sheet dates were as follows:

46. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(continued)*

Group

	2008 RMB'000	2007 RMB'000
Interest-bearing bank loans	**1,728,660**	263,156
Trade and bills payables	**2,394,610**	1,574,460
Accruals and customer's deposits	**745,535**	544,662
Other payables	**1,048,792**	1,013,171
Other loans	**72,942**	36,004
Income tax payable	**–**	185
Long term payables	**107,988**	224,192
Less: Cash and bank balances	**(3,041,965)**	(2,210,818)
Net debt	**3,056,562**	1,445,012
Equity attributable to equity holders	**4,464,616**	5,111,629
Capital and net debt	**7,521,178**	6,556,641
Gearing ratio	**41%**	22%

Financial risk management

The Group's principal financial instruments comprise cash and cash equivalents, trade receivables and payables, other receivables and payables, balances with related parties, interest-bearing bank loans, other loans and long term payables.

46. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(continued)*

Financial risk management *(continued)*

The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk, credit risk and liquidity risk. The board of directors and senior management meet periodically to analyse and formulate measures to manage the Group's exposure to those risks. Generally, the Group adopts reasonably prudent strategies on its risk management. As the Group's exposure to these risks is kept to a minimum, the Group has not used any derivatives and other instruments for hedging purposes. The Group does not hold or issue derivative financial instruments for trading purposes. The board of directors reviews and agrees policies for managing each of these risks and they are summarised below:

(i) *Interest rate risk*

The Group's exposure to the risk of changes in market interest rates relates primarily to the Group's borrowings with floating interest rates. The Group closely monitors its interest rate risk by performing periodic reviews and evaluations of its debt portfolio and gearing ratio. The interest rates and terms of repayment of the bank loans of the Group are disclosed in note 33 to the financial statements. In the opinion of the directors, the Group has no significant interest rate risk and has not used any interest rate swaps to hedge its exposure to interest rate risk.

The following table demonstrates the sensitivity to a reasonable possible change in interest rates, with all other variables held constant, of the Group's profit before tax (through the impact on floating rate borrowings):

	Group	
	Increase/ (decrease) in basis points	**Increase/ (decrease) in profit before tax** *RMB'000*
2008		
RMB	**50**	**(1,150)**
RMB	**(50)**	**1,150**
US dollar	**50**	**(53)**
US dollar	**(50)**	**53**
2007		
RMB	50	(1,070)
RMB	(50)	1,070
US dollar	50	(418)
US dollar	(50)	418

46. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(continued)*

Financial risk management *(continued)*

(ii) Foreign currency risk

The Group's businesses are principally located in Mainland China and substantially all transactions are conducted in RMB, except for the purchases of imported machinery and equipment and sales of dairy products to Hong Kong and Macau. As at 31 December 2008, substantially all of the Group's assets and liabilities were denominated in RMB except the cash and cash equivalents of approximately RMB31,791.000 (2007: RMB36,048,000), RMB56,146,000 (2007: RMB722,514,000) and RMB4,257,000 (2007: Nil) which were denominated in United States dollars, Hong Kong dollars and Euro, respectively, and the interest-bearing bank loans of approximately RMB33,660,000 (2007: RMB40,906,000) and long term payables of approximately RMB249,014,000 (2007: RMB309,822,000) which were denominated in United States dollars. The fluctuation of the exchange rates of RMB against foreign currencies could affect the Group's results of operations. However, in the opinion of the directors, the foreign currency risk exposure is under management's control.

The following table demonstrates the sensitivity to a reasonably possible change in the RMB exchange rate as compared to USD, with all other variables held constant, of the Group's profit before tax (due to changes in the fair value of monetary assets and liabilities):

	Increase/ (decrease) in RMB rate	**Increase/ (decrease) in profit before tax**
	%	*RMB'000*
2008	**5**	**3,291**
	(5)	**(3,291)**
2007	5	1,941
	(5)	(1,941)

46. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(continued)*

Financial risk management *(continued)*

(iii) Credit risk

The cash and bank balances, as well as the pledged deposits, of the Group are mainly deposited with state-owned commercial banks in Mainland China.

The majority of the Group's sales are conducted on a cash basis. The Group has implemented policies to ensure that sales of products are made to distributors, who wish to trade on credit terms, with an appropriate credit history which is subject to periodic reviews. Receivable balances are monitored on an ongoing basis and the Group's exposure to bad debts is not significant.

The credit risk of the Group's other financial assets, which comprise deposits and other receivables, arises from default of the counterparty, with a maximum exposure equal to the carrying amounts of these assets.

In addition, the Group's guarantees of the bank loans borrowed by certain suppliers of raw milk amounting to RMB73,820,000 (2007: RMB109,800,000) (note 42) represent the Group's other exposure to credit risk. RMB73,820,000 (2007: RMB89,800,000) of the above guarantees are cross-guaranteed and secured by assets owned by these suppliers.

Except for the above, the Group has no significant concentration of credit risk, with exposure spread over a number of counterparties.

Further quantitative data in respect of the Group's exposure to credit risk arising from trade receivables are disclosed in note 26 to the financial statements.

(iv) Liquidity risk

The Group closely monitors its liquidity risk by performing periodic reviews and evaluations of its liquidity with regard to the industry characteristics, market conditions, business strategies and changes in the Group's state of affairs and adjusting the current and non-current portions of the Group's debt portfolio on a proper and timely basis. In addition, the Group aims to ensure a continuity of fund and flexibility through the use of various means of financing and by keeping committed credit lines available.

The table below summarises the maturity profile of the Group's financial liabilities at 31 December 2008 based on contractual undiscounted payments.

46. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(continued)*

Financial risk management *(continued)*

(iv) Liquidity risk (continued)

			2008		
	On demand	**Less than 1 year**	**1 to 5 years**	**More than 5 years**	**Total**
	RMB'000	***RMB'000***	***RMB'000***	***RMB'000***	***RMB'000***
Interest-bearing bank loans	**–**	**1,208,660**	**520,000**	**–**	**1,728,660**
Other loans	**72,942**	**–**	**–**	**–**	**72,942**
Trade and bill payables	**–**	**2,394,610**	**–**	**–**	**2,394,610**
Other payables, excluding current potion of long term payables	**–**	**879,997**	**–**	**–**	**879,997**
Long term payables	**–**	**173,797**	**113,160**	**3,185**	**290,142**

			2007		
	On demand	Less than 1 year	1 to 5 years	More than 5 years	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Interest-bearing bank loans	–	183,156	80,000	–	263,156
Other loans	36,004	–	–	–	36,004
Trade and bill payables	–	1,574,460	–	–	1,574,460
Other payables, excluding current potion of long term payables	–	841,232	–	–	841,232
Long term payables	–	173,466	245,236	–	418,702

47. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 16 April 2009.

Financial Summary

The following is a summary of the audited financial statements of China Mengniu Dairy Company Limited (the "Company") and its subsidiaries for the respective years as hereunder stated.

Results

	Year ended				
	2008	2007	2006	2005	2004
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Revenue	**23,864,975**	21,318,062	16,246,368	10,824,950	7,213,827
Profit/(loss) before tax	**(1,089,275)**	1,130,310	942,320	617,135	410,553
Income tax income/(expense)	**161,454**	(21,658)	(76,032)	(61,612)	(18,454)
Profit/(loss) for the year from continuing operations	**(927,821)**	1,108,652	866,288	555,523	392,099
Profit for the year from a discontinued operation	**3,357**	–	–	–	–
Profit/(loss) for the year	**(924,464)**	1,108,652	866,288	555,523	392,099
Attributable to:					
Equity holders of the Company	**(948,600)**	935,786	727,352	456,847	319,393
Non-controlling/minority interests	**24,136**	172,866	138,936	98,676	72,706
Proposed dividend	**–**	187,535	149,718	93,873	80,053
Earnings per share attributable to ordinary equity holders of the Company *(RMB)* (note (i))					
For profit/(loss) for the year					
– Basic	**(0.639)**	0.664	0.532	0.365	0.357
– Diluted	**N/A**	0.664	0.532	0.334	0.285

Assets, liabilities and equity

	At 31 December				
	2008	2007	2006	2005	2004
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Total assets	**11,315,275**	9,681,279	7,763,678	6,087,105	4,836,384
Total liabilities	**6,577,304**	3,846,575	4,130,998	3,320,026	2,533,256
Equity attributable to equity holders of the Company	**4,464,616**	5,111,629	2,998,864	2,330,621	1,954,474
Non-controlling/minority interests	**273,355**	723,075	633,816	436,458	348,654

Note:

(i) Calculation basis for the earnings per share attributable to ordinary equity holders of the Company are set out in note 12 to the consolidated financial statements.

China Mengniu Dairy Company Limited
中國蒙牛乳業有限公司*

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