

Brand development and rapid expansion in retail distribution is driving Montec's strategy to establish a strong base in China with premium products in the rapidly growing market for dairy foods

DIRECTORS

Terry Cuthbertson, Chairman
Peter Herd, Managing Director
Dr Xueqin Du, Executive Director
Lin Yuansheng, Non- Executive Director
Jim Manny, Non- Executive Director

SENIOR MANAGEMENT

Peter Herd, Managing Director
Nick Geddes, Company Secretary
Ian Maltman, CFO
Dr Xueqin Du, Director – Product Development

MARKET DATA

ASX Code:	MTI
Shares on Issue:	74.3 million
Options on Issue:	4.6 million
52 week Share Price Range:	\$0.07 - \$0.35

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KEY POINTS

Whilst Montec generates some fee income in Australia, its growth opportunity lies in the US\$11 billion China dairy market which has been growing at 10% annually. Liquid milk, which has been growing in line with the overall industry, represents about one-third of the industry by volume and 7% by value.

Montec's "dairypure" and "Meng Tai" brands of monounsaturated plain and flavoured milk are available in over 2,700 retail outlets in Shanghai, Beijing, Qingdao and Dalian. The target is 6,000 outlets by mid-2007 and 10,000 by the end of 2007.

"Dairypure" is positioned as a premium product and its distribution strategy has been focussed on building a strong presence in the affluent AB demographic. Accordingly, a strong distribution capability has been established with key retailers including Carrefour and Jingkelong hypermarkets, major supermarket chains such as Huarun and major convenience store groups such as Lianhua Kuik and Lawson.

In mid-January 2007, a 47,000 litres production run of "dairypure" and "Meng Tai" product was completed. Of this, nearly 42% was chocolate and strawberry flavoured milk, indicating broad acceptance of the current product offering. A further 35,000 litre production run was completed in late March.

The company plans to launch ice cream and yoghurt product extensions in 2007 and 2008.

Montec remains committed in the medium to longer term to developing a licensing model as the most effective means of expanding market penetration in China.

BACKGROUND

Montec International owns certain rights to a unique technology that enables the production of monounsaturated, cholesterol-free dairy products. Dairy Farmers has been licensed by Montec to market milk in Australia using the technology but, at this stage, has retained the rights for its own use in certain countries within Asia.

Montec's principal focus is in developing the market for monounsaturated, cholesterol-free dairy products in China using the technology. The company is currently building its range of white, chocolate and strawberry flavoured milk under the "dairypure" and "Meng Tai" brands with distribution through more than 2,700 outlets predominantly in Beijing and Shanghai. Market development will follow with planned extensions into ice cream, yoghurts, shakes and other products.

The Chinese dairy industry has enjoyed 10% plus annual growth since the late 1990's in response to rising incomes, rapid increase in the availability of raw milk from an expanding domestic herd, a broader adoption of western-style foods, increased penetration of home refrigeration, improved cold chain distribution systems, and an increasingly sophisticated retail environment. Government support for better nutrition such as through children's milk programs has also been a positive factor in driving growth. The largest sectors of Chinese dairy market is ice cream (72% by value and 54% by volume) followed by yoghurt (19% by value and 12% by volume) and liquid milk (7% by value and 33% by volume).

When the company listed on the ASX in late 2003 the objective was to quickly establish licensing arrangements with dairy processors who would drive growth. It was intended that these processors would control all stages of the value chain including production, distribution, sales and marketing. However, despite some promising negotiations and relationship building, this objective could not be achieved without proven product acceptance. Accordingly, Montec has revised its strategies to build a meaningful presence in this promising market.

Whilst Montec remains committed to the licensing strategy in the long term, it is now responsible for

sales and marketing. It is anticipated that once the dairypure brand, in particular, is established and consumer acceptance is demonstrated, dairy processors will be more favourably disposed to the licensing model.

Montec's market development strategies have been strengthened through a partnership with Beijing Sanyuan Foods (BSF), one of China's largest dairy processors, who has also taken a significant equity position in Montec International.

The revised model requires considerably more working capital than envisaged due to the funding of inventory, receivables and marketing. Accordingly, Montec is presently seeking additional capital to enable it to fully develop this strategy.

GROWTH AND PROFITABILITY LEVERAGED TO RISING INCOMES AND INCREASING DEMAND FOR DAIRY FOODS IN CHINA

Montec's technology for producing monounsaturated, cholesterol-free dairy products is a premium product. The opportunity in China is enormous and will be driven by the steeply rising demand for dairy products in general. Accordingly, the key to establishing a significant presence in the market is to build brand awareness, extensions into the primary product categories and to demonstrate consistent and reliable product supply.

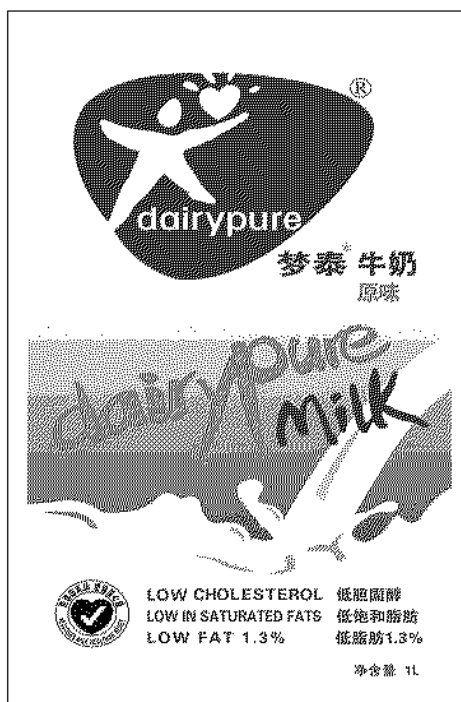
The key to meeting these objectives is to maximise retail distribution opportunities in China's largest and most affluent cities including Beijing, Shanghai, Qingdao, Dalian and Guangzhou.

In this first stage, distribution has been achieved through 2,700 outlets. The objective is to reach 6,000 outlets by the end of June 2007 and 10,000 outlets by the end of December 2007.

The second step is to boost the current low sales rate per outlet.

A key factor in driving sales rates per outlet will be the development

of a broader product base. Currently, Montec is marketing plain, chocolate and strawberry milk. Nearly 42% of the January production run was flavoured milk indicating broad acceptance of the current product offering. Montec is currently developing a range of product extensions for the key ice cream and yoghurt categories, which will be released over the next year.



Once consumer acceptance can be demonstrated, it is expected that regional dairy processors would seek licensing arrangements. As production licences are taken up, distribution and sales throughout China are likely to accelerate. Moreover, a shift to the licensing model will greatly reduce Montec's working capital requirements.

As Beijing and Shanghai account for only about 5% of the national market for dairy products, expansion throughout the country is imperative to build critical mass. Licensing is the only practical way to achieve this due to the extensive resources and very large working capital that would otherwise be required.

THE BUSINESS MODEL

Although Montec holds certain rights to the technology in Australia and New Zealand, the immediate business opportunity is in China. NSW based processor Dairy Farmers has been licensed to market milk with the technology in Australia. However, due to Dairy Farmers limited presence outside of its home market, volumes are not large and unlikely to grow significantly in the short to medium term. Nonetheless, fees from Dairy Farmers amount to about \$300K annually.

Montec's business model in China is currently based on the company as principal. The company has outsourced packaging, logistics and sales to third parties but directly controls marketing and product development.

This business model is underpinned by a production and distribution partnership with Beijing Sanyuan Foods (BSF). BSF packages dairypure and Meng Tai branded milk for Montec and provides logistics services.

BSF principally manufactures milk and dairy products, under the brand Sanyuan. Headquartered in Beijing, the company has established milk source bases in Hebei Province and the Inner Mongolia Autonomous Region. The company is one of the largest dairy groups in the country with processing facilities throughout north east China. It is also one of only a few companies with a nationwide cold chain distribution capability. The company has established strong connections with major global food groups and has major equity interests in the Beijing operations of McDonalds and Starbucks.

Sales to the retail channel are undertaken in China by three groups and co-ordinated by MTR, Montec's counter-party. MTR is focussed on Beijing, Shanghai and Qingdao, a specialised food industry agent, National Agency Network (NAN) focuses on Liaoning and Fujian provinces and BSF focuses on selected channels in Shanghai and Beijing.

The mix of stores achieved to date, including Carrefour and Jingkelong hypermarkets, major

supermarket chains such as Huarun and major convenience store groups such as Lianhua Kuik and Lawson, reflects careful selection by these sales development teams.

The company has a product development team in China under the direction of Dr Xueqin Du. This team is responsible for developing product extensions and formulations that are suitable to Chinese tastes. Over the next year, several new products are expected to be launched giving the dairypure brand a strong presence in the market and establish the brand as a more attractive proposition for retailers.

The business model as it now stands is working capital intensive as Montec is required to fund packaged milk inventories ex BSF, receivables from the retailers and shelf access fees to retailers as well as marketing and business development costs.

With well planned and implemented marketing strategies, it is expected that by the end of 2007, the brand will be well accepted by consumers with an appropriate depth of product that will be attractive to dairy processors.

The company anticipates being able to shift to a licensing model at some stage with processors paying a fee for use of the brand and product formulations whilst being responsible for working capital and sales. Montec would retain responsibility for brand marketing support and product development.

HEALTH ISSUES UNDERPIN THE BUSINESS CASE

The business opportunity in China reflects the combination of rapid growth in the demand for dairy products and increasing awareness of the health issues associated with saturated fats and cholesterol.

Cardiovascular disease is a leading cause of death in many developed countries including Australia. With sharply rising levels of obesity, especially in young people, governments around the world are giving increasing policy attention to diet and nutrition.

In developing countries, cardiovascular disease is expected to be the leading cause of death by 2010. This reflects the change in diet that typically accompanies rapidly rising incomes and improved living standards. In China, heart and brain diseases have become the major cause of death. The highest incidence is in affluent North and North East China, with the highest incidence in Beijing.

Cardiovascular disease covers a group of disorders of the heart and blood vessels, which includes high blood pressure, heart attacks and stroke amongst others. In countries with established dairy industries, dairy foods are a leading source of dietary fat.

Accordingly, the dairy industry has been at the front line of pressure to develop healthier products.

Per capita dairy food consumption in Asia is low by western standards but is growing rapidly as diets change in response to rising incomes and improving living standards. Although consumption in China is particularly low, the total volume of dairy products sold is large and growing rapidly.

The growth in dairy consumption has also been aided by improved retail distribution, almost universal in-home refrigeration in urban areas and rising penetration in rural areas, greater availability of cold chain logistics, and the rapid transformation of the retail industry based on the western model, which includes supermarkets, hypermarkets and local convenience stores.

Industry analyst, Access Asia has forecast sustained high rates of growth for the dairy industry through to at least 2010. Access Asia has forecast about 60% growth in the value of dairy industry sales to about US\$18 billion through this period with each of the key categories, including liquid milk, having broadly similar growth rates.

DIRECTORS

Terry Cuthbertson, Chairman (Non-Executive)

Non-Executive Chairman of Austpac Resources N.L., S2 Net Limited and My Net Fone Limited, previously a Partner of KPMG and Director of KPMG Corporate Finance and NSW Partner in Charge of Mergers and Acquisitions, Group Finance Director of Tech Pacific Holding Limited, Director for Tech Pacific Holding Limited's businesses in Malaysia, Hong Kong, Singapore, India, Philippines, Indonesia and Thailand.

Peter Herd, Managing Director

Previously General Manager of Dairy Farmers' Milk and Beverage Division, previously Regional Director of Australasia for Coca-Cola South Pacific, Division President for Coca-Cola Far East in the Philippines and Country Manager for Hong Kong, Taiwan and Indonesia.

Dr Xueqin Du, Executive Director (Product Development)

Previously Vice Director of the Beijing Institute of Food Hygiene Inspection and Examination, Professional and Administrative Official of the Department of Nutrition and Food Hygiene within the Ministry of Public Health China and currently Research Fellow with the University of Sydney.

Lin Yuansheng, Director (Non-Executive)

Most recently Managing Director of BAIC Australia Pty Ltd, the Australian subsidiary of Beijing Sanyuan Group Co Limited (Sanyuan Group). Sanyuan Group is the largest food, beverage and dairy company in China. Beijing Sanyuan Foods Co Ltd is listed on the Shanghai stock exchange. Previously Managing Director of BAIC Scriven Ltd (Hong Kong). Through his association with Sanyuan Group, he was responsible for successfully introducing Kraft, Starbucks, Hormel and Baskin & Robbins to China. Key relationship holder with Beijing Sanyuan Foods, and integral to China business development and special project reviews within that country.

Jim Manny, Director (Non-Executive)

Currently Managing Director of Credit New Holland Group Limited and International Concert Attractions Limited. Has had extensive experience in the financial sector and been responsible for several business disciplines including, treasury, IPO project management and capital raising.

PROSPECTUS

Montec lodged a prospectus on 20 March 2007 and a supplementary prospectus on 23 March 2007 (**Disclosure Documents**) with the Australian Securities and Investments Commission in relation to its proposed rights issue and placement to raise up to \$4.291 million (**Offer**). The Offer is made in the Disclosure Documents. Anyone wishing to acquire Montec securities under the Offer will need to complete the application form that accompanies the Disclosure Documents.

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