

New product initiatives strengthen the brand and underpin 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, Executive Director
Dr Xueqin Du, Executive Director
Mei Zhan Yan, Non- Executive Director
Jim Manny, Non- Executive Director

SENIOR MANAGEMENT

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

MARKET DATA

ASX Code:	MTI
Shares on Issue:	151.4 million
Options on Issue:	100 million
52 week Share Price Range:	\$0.07 – \$0.03
Market Capitalisation:	\$4.5 million

CORPORATE DIRECTORY

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KEY POINTS

Montec's "dairypure" brand of monounsaturated plain and flavoured milk is available in an estimated 4,000 retail outlets in Shanghai, Beijing, Qingdao and Jinhua. The focus is now on building the distribution of the full product range and seeking new sales channels.

New initiatives commenced in late 2007 and early 2008 to build the company's business in China including the launch of children's drinking yoghurt and monounsaturated ice cream.

Production volumes and retail distribution of these new products continues to expand.

Montec has established a wholly owned subsidiary in China to absorb the sales, marketing and administration previously undertaken by agents.

Shareholder approval for a placement to Puji Wealth Management (SH) Co. Limited to raise \$1.1 million was provided in March 2008.

Important new relationships have been established through new product initiatives and the placement that are expected to drive further opportunities to build the business in China.

Momentum is building towards critical mass in China and is being driven by new product initiatives and now full control over the business activities in that market.

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

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" brand with distribution through an estimated 4,000 outlets. Market development is progressing with recently launched product extensions into children's drinking yoghurts and ice cream with planned extensions into adult yoghurts and other products.

The Chinese dairy industry has enjoyed 10% plus annual growth since the late 1990s 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 are 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).

The company has faced many challenges in building a base in China including resistance to the original licensing model, lack of a wholly owned subsidiary to oversee operations as well as high distribution and marketing costs due to a focus on building the number of outlets in the distribution channel.

It has been a steep learning curve for Montec, however, over the past year major initiatives have been undertaken that put the China business on a more secure footing and have enabled the company to establish a platform for growth. These initiatives include a marketing focus on sales per outlet rather than the number of outlets, launch of new products, new commercial relationships including a placement to a major investor and the establishment of a local subsidiary who has assumed full control over all sales, marketing, distribution and administration.

NEW PRODUCT INITIATIVES TO DRIVE MOMENTUM TOWARDS CRITICAL MASS

Montec's technology for producing monounsaturated, cholesterol-free dairy products delivers 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.

Montec has established key manufacturing partnerships with leading dairy products producers including Beijing Sanyuan Foods, Beijing Allied Faxi Foods (both subsidiaries of the giant Sanyuan Group) and Jinhua Jalo Dairy Company.

The company has also established retail distribution channels in key cities including Beijing, Shanghai, Qingdao, and Jinhua.

Manufacturing and retail distribution is now in place the key is to scale up the brand and leverage the infrastructure through the launch of new products.

UHT plain and flavoured milk is now well established and available through some 4,000 outlets. In the past year, the company has introduced new packaging options including 250ml multi-packs. The marketing focus is now on consolidating distribution of the total product range and testing new sales channels.

UHT is the company's entry level product and the strategy is to add a range of premium products under an overarching "Healthy Dairy Cabinet" program.

In November, 2007, Montec launched a branded range of yoghurt drinks specially formulated for children. The range of three fruit flavoured and one fibre enriched product is being produced by the Jinhua Jalo Dairy Company Limited and together with Montec's monounsaturated milk are being distributed in Jinhua, Qingdao and Beijing

The initial introduction of the "Bei Bei" children's drinking yoghurt focussed on testing the advertising strategy in Jinhua and alternate distribution strategies in Qingdao and Beijing. By mid January, "Bei Bei" had achieved distribution into over 900 retail outlets and sales volume reached 86,000 litres in January 2008, compared with sales of 8,450 litres in December 2007, the first full month following market introduction.

There was some disruption to momentum in late February and March by unseasonably late winter storms and Chinese New Year. However, momentum is expected to be restored with the onset of warmer

weather. Further, it is planned to extend distribution into north eastern China which is expected to significantly boost sales.

In November 2007, Montec signed an agreement with Beijing Allied Faxi Co., Ltd (Faxi Foods) for the production and marketing of the company's monounsaturated ice cream. The Licence Agreement provides Montec a no cost market entry to the five billion litre China ice cream market in partnership with the major producer of premium ice cream in Beijing and access to Faxi Foods' established frozen distribution and marketing network. The first production run of 3 flavours was in March 2008, with distribution into 600 supermarkets in Beijing and Shanghai expected in May ahead of the summer season.

New product initiatives are essential in building the brand, in gaining scale benefits from the infrastructure that has been established and in building long term retailer support. Whilst this will be ongoing, the next challenge will be to broaden the geographic reach of the brand.

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 very large and unlikely to grow significantly in the short to medium term. Nonetheless, fees from Dairy Farmers amount to about \$250K annually.

With the exception of ice cream, 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 several production and distribution partnerships with the longest established being with Beijing Sanyuan Foods (BSF). BSF packages "dairypure" branded milk for Montec and provides sales and distribution services in Beijing.

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 an extensive 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.

The children's drinking yoghurt is produced in Jinhua under a new production partnership with the Zhejiang Jinhua Jalo Dairy. Jinhua is located in the middle of Zhejiang Province, southern wing of the Yangtze River Delta Economic Zone. It covers an area of 10,900 sq km with a population of 4.52 million people. The city is located close to the port cities of Shanghai and Ningbo.

In November 2007, the company signed an agreement with Beijing Allied Faxi Co., Ltd (Faxi Foods) for the production and marketing of the company's monounsaturated ice cream. Under the terms of the agreement Faxi Foods has been granted a licence to market monounsaturated ice cream, initially in three flavours in Beijing and Shanghai, co-branded with Faxi Food's "BAXY" and Montec's "dairypure" brands. The agreement provides for future geographical expansion through Faxi Foods national distribution channels and the addition of new flavours after initial market proving in Beijing and Shanghai. Montec retains the right to purchase product from Faxi Foods for distribution through its own sales network or appointed distributors as mutually agreed from time to time.

In late 2007, Montec incorporated a wholly owned subsidiary in China, Beijing Montec Commercial Limited, to take over the sales, marketing and administration previously undertaken by its local agent. Whilst its agent had very effectively established sales and marketing operations and built a sizable retail distribution channel, the arrangement complicated cash flow management and created lags and gaps in the flow of information back to Montec. The transfer of operations was completed during the first quarter of 2008 with most of the previous management transferring to Montec. With the new structure, Montec assumes full responsibility for its operations in China, and has full and immediate access to the cash flow and more effective and timely access to sales and market data.

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, more products are expected to be launched giving the "dairypure" brand a stronger presence in the market and to establish the brand as a more attractive proposition for retailers.

DAIRY INDUSTRY GROWTH AND ASSOCIATED 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.

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 incidences are in affluent North and North East China, with the highest incidence in Beijing.

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.

Mei Zhan Yan, Director (Non-Executive)

Managing Director of BAIC Australia Pty Ltd, the Australian subsidiary of Beijing Sanyuan Group Co Limited (Sanyuan Group). Sanyuan Group is a major food, beverage and dairy company in China. Mr. Yan is also Managing Director of Beijing Holdings BAIC Limited (Hong Kong) and Managing Director of BAIC Scriven Limited (Hong Kong), which are the subsidiaries of Sanyuan Group in Hong Kong, Director of Beijing Allied Faxi Food Co., Ltd., Director of Beijing Sunflower Building Co., Ltd and Director of Beijing Dong Yuan Estate Co., Ltd.

James Manny, (Non- Executive)

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

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