

Management Discussion and Analysis



MARKET REVIEW

Despite the implementation macro-economic adjustment and control measures by the government, the economy in the PRC continued to grow robustly with a GDP growth of 10.7 percent in 2006. It is expected that the austere measures will continue in 2007 in the PRC but these will have minimal or no effect on the healthcare industry.

The PRC Government is committed to a sound and fast economic growth with emphasis on quality and efficiency of the growth. Most recently at the Fifth Session of the 10th National People's Congress, the PRC Government plans to reduce its GDP growth to approximately 8 percent in 2007 but at the same time announced a commitment to increase health budget for the rural medical system to RMB10.1 billion, an increase of over 74 percent over last year.

The PRC healthcare industry will continue to be modernized and has already become one of the fastest growing healthcare markets in the world over the last decade. Total health expenditure and per capita health expenditure have been growing at an annual average rate of over 16 percent. Underpinning such phenomenal growth are enhanced living standard, increase in per capita income, growth of the aging population, increasing healthcare consciousness, and the PRC Government's commitment to reform and to increase the healthcare budget for both the urban and rural medical systems as part of its committed effort to establish a harmonious society.

From 2001 to 2005, the per capita income of urban and rural residents in the PRC grew by annual averages of 9.2 percent and 5.2 percent respectively. Currently PRC's overall GDP ranks fourth in the world after decades of rapid economic development with GDP for 2006 at approximately US\$2.7 trillion. In 2006, the per capita income of urban and rural residents was approximately RMB11,759 and RMB3,587 respectively, representing a growth of 12.1 percent and 10.2 percent respectively over that of last year. The improved standard of living and the increase in healthcare consciousness have led to an increase on spending on healthcare products and services.

According to the World Health Report 2006 published by the World Health Organization, China lagged behind other developed countries on spending on healthcare services. Medical and healthcare services in the developed countries accounted for approximately 9.0 percent of GDP on average in 2003. Medical and healthcare services in the US represented 15.2 percent of GDP, while the figure for PRC was only 5.6 percent in 2003. It is widely expected that demand for medical and healthcare services will continue to grow as consumers become more affluent. The Group expects both the percentage and the GDP base to expand, making the healthcare industry to be a high growth sector in the economy.

Management Discussion and Analysis (Continued)

Equally important is the increase in State Basic Medical Insurance population for urban residents. According to the China Statistical Yearbook 2006, the eligible participants have grown from 37.8 million in 2000 to 137 million in 2005, representing an increase of over 99 million participants with annual averages of 29 percent. In the same period, the State Basic Medical Insurance Funds have also increased over 7 times to a gross total of RMB137.8 billion in 2005. Under the 11th Five Year Plan, it is estimated that the urban population in China will increase from 43 percent of total population to 47 percent of total population between 2005 and 2010, and the continual increase in urban population will bring an increasing awareness of quality healthcare services that include early screening and detection of diseases.

BUSINESS REVIEW

Following the disposal of the remaining Information Technology business operation, the objectives of operation strategic prioritization of resources (“SPOR”), involving the shifting of resources allocation from information technology products and services and property investment divisions to the high growth protein chips division, have been successfully completed. Major corporate activities undertaken in 2006 were summarized as follows:

Major Events and Issues in 2006

- | | |
|--------|--|
| 19 Jun | <p>Announced the acquisition of 51 percent equity interest in Shanghai Weiyi Hospital Investment & Management Co., Ltd on 16 June at a cash consideration of RMB60,000,000.</p> <p>The acquisition allowed the Group to achieve at least two specific objectives, namely (i) provides a medical infrastructure to provide better after sales service in Shanghai, and (ii) extends its cancer screening products to include a technologically advanced cervical cancer screening methods for women by way of an exclusive distribution arrangement in the Asia Pacific region for a period of 20 years.</p> |
| 3 Oct | <p>Announced the appointment of Mr. Lu Chung as Executive Director and Mr. Chien Hoe Yong, Henry, as Chief Executive Officer of the Company.</p> <p>Mr. Lu Chung is the younger brother of Mr. Yao Yuan, Chairman of the Company and Mr. Lu has been a Director of the Company’s wholly owned subsidiary, HD Global Limited since 2003. Mr. Lu’s corporate responsibility is in the area of development and maintenance of new sales channel including the life insurance companies, and investments for the Group.</p> <p>Mr. Chien Hoe Yong, Henry, has been an Executive Director of the Company since 2002 and has been responsible for the implementation of KM2003 Objectives and operation SPOR. Mr. Chien’s corporate responsibility is coordinating all management functions for the implementation of business plans and objectives for the Company.</p> |
| 7 Nov | <p>Announced a major transaction involving the disposal of the 51 percent equity interest in Shanghai Longxiang Computer Company Limited, the remaining information technology business operation.</p> <p>Following the disposal, the Company is entirely engaged in the business activities of biomedical products and services.</p> |

Management Discussion and Analysis (Continued)

20 Dec

Announced that SHMY HealthDigit Biochip Company Limited (“HD Biochip”), a wholly-owned subsidiary of the Company, entered into a cooperation agreement with China Life Insurance Company Limited, Shanghai Branch (“CLS”) on 19th December, 2006 whereby CLS will engage HD Biochip for the use of the Group’s proprietary multi-tumor marker detection systems to evaluate interested applicants who intend to acquire insurance protection under a new Cancer Care Insurance Policy to be launched by CLS shortly in Shanghai, the PRC.

The cooperation agreement marked a further collaboration with China Life Insurance Company Limited (“CL”), the largest life insurance provider in the PRC and an milestone for the Company in a successful expansion of the products sales into one of the largest and most established retail sales network in the PRC with over 640,000 individual agents, 12,000 group sales staff and over 90,000 cooperating bank branches and post offices.

Mission Statement – Innovative Medicare Solutions Partnership

The Group is a leading supplier of biomedical solutions in China and has sold more than 3 million protein chips to date for cancer screening from its own proprietary intellectual property (“PIP”) protein chip platform.

Founded in 2000, the Group is a pioneer that dedicates itself for the provision of low cost, non-invasive, and innovative medicare solutions in the areas of early detection and prevention of diseases, enhance human health and quality of life, and to provide a new approach to life insurance industries in the evaluation of health status and life span. It has been accepted that early detection of potential diseases including life threatening diseases would significantly improves the chances of successful medical therapy and treatment, raises the survival rate and improves the quality of life for patients.

Currently, the Group manufactures and distributes C-12 protein chips and related systems (“C-12 products”) to hospitals and life insurance companies in China. The C-12 products are capable of detecting up to twelve tumor markers simultaneously and assisting in early detection of ten prevalent cancer tumor types. During the year, the Group continued to experience an excellent growth in both order and sales of C-12 products. As a proven and leading supplier of protein chips in China, the Group began to supply C-12 products to life insurance companies based in China for the pre-screening and general health appraisal of life policy applicants. The Group expects the overall growth for the protein chips sales to be promising and sustainable in the future.

The Group continued to experience rapid growth in its protein chips business operations and sold a total of 1.5 million protein chips (2005: 1.19 million), representing an increase of 26.1 percent over that of last year.

The increase in the sale of chips was due mainly to a number of the following factors:

Sales Strategy

The Group’s sales strategy involves the setting up of sales’ channels, the establishment of a comprehensive pricing structure for the different sales’ channels, the strengthening of technical support structures and the building up a sustainable distribution network.

The Group’s sales strategy has been implemented successfully with increases in both turnover of number of chips sold. The Group will review its strategy continuously and is prepared to make revisions from time to time.

Sales channels

The Group continued to strengthen its sales platform and has expanded beyond the distributorship channel where historically most of the sales were generated. The Group has successfully established direct sales channels for life insurance industry and corporations in China. It is the long term strategy of the Group that the portfolios will be further developed to achieve a more balanced sales category platform and more importantly to reduce reliance on any particular sales channel.

Shanghai Weiyi Hospital Investment & Management Co., Ltd. (“Weiyi”)

On 16th June, 2006, Shanghai HealthDigit Company Limited (“Shanghai HealthDigit”), a wholly-owned subsidiary of the Company, entered into an acquisition agreement to acquire 51 percent equity interest in Weiyi at a consideration of RMB60,000,000 (equivalent to approximately HK\$60,000,000).

Founded in July 2003, Weiyi is principally engaged in two major business activities, namely (1) the operation of Shanghai Woman and Child Healthcare Hospital of Hong-Kou District, an established woman and infants specialty hospital in Shanghai founded in November 1982, and (2) the distribution of HPV Detection Products (HPV DNA diagnostic kits for cervical cancer screening) in the Asia Pacific region.

Following completion of the acquisition agreement on 14th August, 2006, Shanghai HealthDigit holds 51 percent equity interest in Weiyi and is the sole distribution agent of HPV Products in the Asia Pacific region for a period of 20 year from 7th June, 2006 to 6th June, 2026 through an exclusive agency agreement with Genetel Pharmaceuticals (Shenzhen) Limited (“Genetel”). Under the strategic partnership with Genetel, Shanghai HealthDigit will also become the sole manufacturer of HPV Detection Products in China and collaborate closely with Genetel in research and development of biochips used for early detection of diseases.

The acquisition also provides an opportunity to the Group to transform part of the existing hospital facilities into a biomedical diagnostic laboratory for promotion and distribution of protein chips and HPV Detection Products. A strategic and synergistic opportunity is also generated to further strengthen the cancer screening product series into the area of cervical cancer screening and optimize its sales efforts in the established distribution network, particular in the China.

China Life Insurance Company Limited, Shanghai Branch (“CLS”)

On 19th December 2006, the Group has successfully established a new sales channel that will contribute significantly to the future revenue, profitability and growth of the Group. HD Biochips, a wholly-owned subsidiary of the Company entered into a cooperation agreement with CLS whereby the latter agreed to engage HD Biochip for the use of its proprietary multi-tumor marker detection systems on a new insurance policy known as the “Cancer Care Insurance Policy” which will be launched shortly in Shanghai, the PRC. The cooperation agreement with CLS represents a major milestone for the corporate development of the Company and will significantly increase the sale of its proprietary protein chips and systems in coming years.

The “Cancer Care Insurance Policy” is a new health insurance policy developed by China Life Insurance Company Limited (“CL”), the largest life insurance provider in the PRC. Being a major branch of CL, CLS has over 4,000 exclusive agents and over seven million customers. CLS is the life insurance company in Shanghai principally engaged in the provision of insurance products for four main categories, namely life, retirement, health and accident insurance.

The Cancer Care Insurance Policy seeks to provide protection for people against cancer for one year after a successful cancer screening test. Within the insured period, the policy holder will receive the appropriate compensation for medical care whether the cancer tumor is benign or malignant. Under the cooperation agreement, the Company will use its proprietary multi-tumor protein chips and systems to provide cancer screening testing and risk evaluation procedures for every customer who purchases Cancer Care Insurance Policy from CLS. The cancer screening testing and risk evaluation procedures will include a protein chip testing together with other medical tests. Under the cooperation agreement, CLS will pay to HD Biochip RMB192 for each successful policy applicant who receives the cancer screening testing and risk evaluation procedures. The cooperation agreement will last for a period of three years.

The Directors believes that the launch of the Cancer Care Insurance Policy in a metropolitan city like Shanghai is the first step and that the cancer care programs will gradually be made available to other branches of CL in the PRC. The Directors believes that the cooperation agreement with CLS provides the potential of accessing the CL’s extensive insurance distribution network in the PRC and further strengthening the Company’s position as a leading supplier of biomedical chips and could significantly increase the Company’s sales of its proprietary protein chips and systems in coming years.

Management Discussion and Analysis (Continued)

Chipreader optimization plan

As at 31st December, 2006, the Group had 406 (2005: 323) chipreaders in the market. The Group understands that the chipreader for the C-12 protein chips is a principal contributing factor for the sales volume and to this effect, the Group has been successful in increasing the utilization rate per chipreader per month by promoting the sharing of chipreaders among hospitals in the same location, reallocating some existing chipreaders to newly signed up hospitals and insurance companies, and increasing the production of chipreaders to meet new demands. During the year, the implementation of the optimization plan for chipreaders also contributed significantly to the increase in sales volume for the C-12 protein chips. The utilization rate per chipreader will be further increased should sales on C-12 products continue to experience growth in the future and other new products were introduced.

Chipset packaging diversification

The Group currently maintains three different sizes of packaging for its customers, namely 48 wells chipset for the simultaneous testing of 42 patients, 24 wells for the testing of 18 patients and 16 wells for the testing of 10 patients. The smaller packaging for 18 and 10 patients is more popular with regional hospitals and allows more regular processing of C-12 protein chips for patients. Nevertheless, the Group maintains a flexible policy on packaging based on a reasonable demand from its customers and will review the packaging from time to time.

After sales service

The Group continues to strengthen after sales service to its customers and in house procedure has been developed to track down details of subsequent therapeutic treatments in hospitals for cancer patients being diagnosed. The after sales services not only indicate that our customers are actually being cared for. It also instills in our employees a sense of mission to assist our customers and their patients.

Information Technology Products and Services

Due to operation SPOR, the Group has successfully sold all the remaining information technology business operation in 2006 and contribution from this operation is no longer expected.

FINANCIAL PERFORMANCE

The consolidated turnover of the Group amounted to HK\$160.8 million (2005 (restated): HK\$127.0 million) for the year under review, representing an increase of approximately 26.6 percent over that of last year. The increase in turnover was mainly attributable to increase in sales of C-12 products.

The net profit attributable to shareholders of the parent amounted to HK\$73.6 million (2005: HK\$70.0 million), representing an increase of 5.1 percent over that of last year. Earnings per share was HK\$2.74 cents (2005: HK2.61 cents), representing an increase of approximately 5.0 percent.

The net profit attributable to shareholders of the parent for the year was affected by the application of a number of new Hong Kong Financial Reporting Standards ("HKFRSs"), Hong Kong Accounting Standards ("HKASs") and Interpretations (herein collectively referred to as "new HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants that are effective for accounting periods beginning on or after 1st January, 2005. The implementation of these new HKFRSs affected a number of accounting items and two areas are particularly affected, namely the convertible bonds and the employees share option scheme.

The Group applied new accounting and disclosure policies for its convertible bonds that was issued on 6th January, 2005 and employee share option scheme that was granted on 8th April, 2005. The net profit attributable to shareholders of the parent for the current year was reduced by approximately HK\$15.1 million (2005: HK\$19.4 million) upon application of new HKFRSs on these two areas.

Biomedical Products and Services

Turnover contributed by the sale of C-12 products amounted to HK\$150.9 million (2005: HK\$127.0 million), representing an increase of approximately 18.8 percent over that of last year. Segment profit amounted to HK\$103.1 million (2005: HK\$87.0 million), representing an increase of 18.5 percent over that of last year.

Hospital

Turnover contributed by this new division amounted to HK\$10.0 million (2005: Nil). Segment profit amounted to HK\$1.1 million (2005: Nil). This new division was acquired in the latter part of 2006 and future contribution from this division will be more significant.

Information Technology Products and Services

Turnover contributed by this division amounted to HK\$14.7 million (2005: HK\$144.3 million), representing a sharp decline of 89.8 percent over that of last year. Due to operation SPOR, the Group reduced its allocation of resources to this division and the division recorded a segment loss of HK\$738,000 (2005: HK\$114,000). The Group completed the disposal of the remaining information technology business operation in 2006. The Group does not expect any further contribution from this division in 2007.

PROSPECTS

At the World Health Organization during the 58th World Health Assembly in 2005, member states adopted a number of resolutions that included a common understanding on early detection and prevention of diseases by way of promoting national health programs to control and prevent diseases including cancers.

Being a pioneer in this field of early screening, detection and prevention of diseases and a leading supplier of biomedical solutions, the Group has seized first mover advantage to service the increasing health conscious and affluent group of customers in China who demand higher standard of healthcare service and are looking for ways to improve quality of life including early medical therapy and treatment of diseases through early detection. The Group's biomedical chips are designed for early detection of diseases. With increasing health conscious worldwide and increasingly tight medical resources, the Group believes the dynamic development of biomedical solutions provides a new trend in healthcare industry that is moving decisively in the direction of early detection and prevention of diseases. The accumulation of market experiences enables the Group to appreciate the opportunities and challenges for biomedical products and services, and structure its unique distribution network for growth.

During 2003, the Group laid down key milestones for its protein chips business division (referred to as "KM2003 Objectives") and the Group has since been implementing business plans and strategies in the direction of KM2003 Objectives with an intention to strengthen its leading position as a protein chip supplier in China which is one of the largest, fastest growth and most promising healthcare markets in the world.

Despite many challenges ahead, the outlook for the Group is extremely promising and business plans are being implemented with impressive results. Most importantly the Group is implementing its business plans from which it has successfully raised through equity and debt issues, and through operation SPOR in 2005.

The Group continues to comply with a disciplined cost control philosophy and adopt a methodical approach towards the implementation of its business plan that includes strengthening distribution network and systems, strengthening after sales services, upgrading production and quality control processes, and reviewing of its research and development efforts and effectiveness, etc. The Group believes that early screening and diagnosis of potentially fatal diseases significantly improve the chances of successful treatment and raise the survival rate of patients. The Group intends to provide early screening of diseases that may be cured via proper dieting and drug therapy and thus raising the quality of life for patients.

Management Discussion and Analysis (Continued)

Key Milestones Progress

Based on KM2003 Objectives, the Group is committed to achieving key milestones and a summary of their respective progress are provided below:

(1) *Expand production capacity for the protein chips.*

The Group is constructing a new factory to expand its production capacity in the Fengxian MA District of Shanghai. The progress of the construction is satisfactory, and is regularly inspected and approved by the relevant government departments in accordance with the construction schedule.

The new factory is built on a site area of approximately 81,764 sq.m. at an estimated total cost of HK\$200 million. Upon completion, the new plant will have a total production capacity of 8 million chips and will be a production base for a range of protein chips used for screening and diagnosis of different diseases.

Relevant applications have been made to the China State Food and Drug Administration (“SFDA”) for a Good Manufacturing Practice Certificate (commonly known as “GMP”) for the new plant. It is expected that Phase I of the new plant with 4 million production capacity will be operational by the end of April 2007.

(2) *Commence mass production of various protein chips and systems.*

The existing GMP compliant plant at the Huzhou Economic & Technological Development Zone in the Zhejiang Province (the “Huzhou Plant”) is currently operating at a full production capacity of 1.5 million chips per annum. Prior to the full operation of the new factory in Shanghai and to meet an increasing demand for its C-12 protein chips, the Group has temporarily expanded the production capacity at the Huzhou Plant from 1.5 million chips to 2.0 million chips at the beginning of 2007.

(3) *Build and strengthen the distribution channels and after sales support services.*

The Group currently distributes its C-12 products to over 45 health centers of major insurance companies and over 600 hospitals in China through regional distributorships and direct sales. The Group intends to expand the points of service to a total of 1000 hospitals and health centers of insurance companies. At the new plant site, the Group will build a composite training center to train medical and healthcare personnel on handling of protein chips and systems and provide after sales services for customers.

The arrangement with CLS to support the cancer evaluation process on the Cancer Care Insurance Policy in Shanghai will contribute significantly to the sale of the C-12 products and the Group expects other branches of CL will start making the policy program available to their customers across China shortly. CL is the largest life insurance company in China and its distribution network, comprised of exclusive agents, direct sales representatives, and dedicated and non-dedicated agencies, is also the most extensive one in China. Being China’s premier life insurance company, CL’s products and services include life insurance, group life insurance, accident and health insurance. Leveraging on the existing distribution network of CL in China, the Directors are confident that the Group’s revenue base will increase significantly and the distribution points will grow in multiples in the coming years.

(4) Commit resources in marketing and promotional activities.

The Group markets and promotes protein chips under the brand name "HealthDigit". Currently, the Group is gaining increasing recognition for its product quality and corporate credibility. The Group intends to further leverage its first mover advantage and market leadership position by investing additional resources on the promotion and cultivation of the brand name "HealthDigit" and the Group's biomedical products and services.

The Group plans to establish a Marketing Department in 2007 with a focus to set up marketing and promotional programs to further raise the corporate profile of the Company, and products in China and to bring together scientists, medical practitioners, and laboratory technicians to further promote the application of biomedical solutions for the early screening, detection and prevention of diseases including cancer.

(5) Pursue new research, discovery and product innovations.

The Group continues to conduct research in-house on different applications of protein chips to be used for early detection of diseases based on the existing protein technology platform and the emphasis will be on product development of cancer or cardiac related screening products.

The Group understands the importance of technological leading edge in the biomedical industry and benefits of working with possible competitors by becoming strategic partners. In 2006, the Group has successfully diversified its revenue sources and its product platform by establishing a second revenue source, in addition to its own PIP protein chip platform, by way of a licensed intellectual property ("LIP") product platform. The Group intends to work with established research based institutions as partners in commercialization of successfully researched and licensed products which are used for early screening of diseases and which are complimentary to the existing products of the Group. The Group places emphasis to develop its product platform into three major revenue sources, namely cancer, cardiac and other diseases series based on both PIP and LIP sources.

By engaging a new revenue source from LIP product platform, the Group has entered into a 20-year exclusive distribution and production agreement with Genetal whereby the Group will distribute the SNIPERTM HPV product series for cervical cancer screening in the Asia Pacific region. The Group is confident that the partnership will be mutually beneficial and provide a new direction in product development for new revenue source and a model for further cooperation. The Group will continue to seek opportunities to work with established scientific research institutions and laboratories on the discovery and research of new product and applications. The Group will over time increase its library of products and will launch them as and when the market condition is ready.

(6) Establish global platform for the protein chips and systems.

While the major market for the Group is China, the Group has commenced feasibility studies on various markets outside China and intends to work with partners and regulators in their respective native countries for the distribution of "HealthDigit" protein chips and systems.

In 2006, Biomarkers Sdn Bhd. ("BIO"), the Group's sole and exclusive distributor for C-12 protein chips in Malaysia, Indonesia and Brunei has made progress in the promotion and sales of the products. BIO is an affiliation of HSC Medical Center ("HSC") in Kuala Lumpur, HSC is one of the world's leading one-stop medical, heart and diagnostic center specializing in early detection and treatment of heart, stroke and cancer with utilization of the latest medical technology.

The Group plans to work in partnership with established medical professionals and centers in their respective countries for a more orderly distribution of the both the C-12 products and systems, and the SNIPERTM HPV product series. The Group plans to enter other Asian markets, including Singapore, Thailand, Hong Kong and Taiwan and to appoint suitable distributors in these respective countries or region.

New Line of Biomedical Testing Kits and Chips for the Early Detection of Diseases

By way of both PIP and LIP sources, the Group intends to strengthen its leadership position in the biomedical industry by further diversifying its biomedical product series that contain the characteristics of both screening and diagnostic value and the Group plans to introduce the following biomedical products in the coming years:

- ***SNIPER™ HPV DNA Detection Kits for Cervical Cancer Screening***

Cervical cancer is the second biggest cause of female mortality worldwide with over 288,000 deaths and 500,000 new cases every year. In the PRC, cervical cancer causes over 50,000 deaths and over 130,000 new infections every year. Currently, it is estimated that over 300 million women worldwide undergo some form of pap smear tests every year with much lower detection rate for cervical cancer.

According to the World Health Organization, cervical cancer is fully preventable and curable if pre-cancerous lesions are detected and treated early. Cervical cancer is caused by a common virus called human papillomavirus ("HPV"). High-risk, cancer-causing types of HPV can be detected using DNA technology. Women above age 18 are recommended to take annual examination to screen cervical disease or cancer.

The DNA-based diagnostic technology platform has been developed for the early screening and diagnosis of infectious and genetic diseases and involves a panel of techniques based on sensitive fluorescence detection, cost-effective microplate hybridization, and DNA microarray genotyping of amplified DNA products.

The proprietary technology platform is developed based on more than 12 years of applied research work carried out in the City University of Hong Kong and is protected by 10 patents/patent filings in China and USA.

The SNIPER™ HPV DNA Detection Kits for Cervical Cancer Screening includes a fluorescence PCR kit for 13 high-risk HPV DNA detection (FPCR Kit), a microplate hybridization kit for 13 high-risk HPV DNA detection (MHC Kit), and a DNA microarray genotyping kit for identification of 29 HPV subtypes (GENO Kit). The product series covers the broadest spectrum of service providers and customers ranging from large hospitals and centralized laboratories (FPCR Kit/GENO Kit) to small-to-medium size hospitals and clinics with low resource setting (MHC Kit), providing medical practitioners with the most comprehensive information on cervical cancer screening, diagnosis, prognosis, vaccination, and therapeutic intervention.

The HPV product series offers superior sensitivity (>95%) for early screening cervical cancer compared with conventional pap-smear test (50-60%), yet it does not require a large upfront capital investment on specialized equipment, and is only a fraction of the costs of other competitive products. The SNIPER™ FPCR Kit has successfully obtained approval from the SFDA in May 2006 and the kits are already being used by over 10 hospitals in China. It is also expected that the two other products including SNIPER™ MHC Kit and GENO Kit will obtained approval from the SFDA in 2007.

- ***Protein Chip for Rheumatoid Autoimmune Diseases (referred to as "RAD")***

Autoimmune diseases affect an estimated 3 to 5 percent of the total population with the highest prevalence in the elderly. Being a major category of the autoimmune diseases, rheumatoid disorders are difficult to recognize in the early stage, but in late stages, multiple organs can be affected and damages can be irreversible.

The word "auto" is the Greek word for self. The immune system is a complicated network of cells and cell components (called molecules) that normally defends the body and eliminates infections caused by bacteria, viruses, and other invading microbes. If a person has an autoimmune disease, the immune system mistakenly attacks itself, targeting the cells, tissues, and organs of the person's own body. A collection of immune system cells and molecules at a target site is broadly referred as inflammation.

Rheumatoid disorders include systemic lupus erythematosus, rheumatoid arthritis, Sjogren's syndrome, scleroderma, polymyositis/dermatomyositis and mixed connective tissue disease.

Clinical tests for RAD protein chip have been successfully completed and it is estimated that over 50 million people in China suffered from rheumatoid autoimmune diseases.

Management Discussion and Analysis (Continued)

- **Protein Chip for Infertility and Sterility Diseases (referred to as "ISD")**

The protein chip is used to diagnose certain autoimmune disorders that cause infertility and sterility. Such disorders include endometriosis, recurrent spontaneous miscarriage, and dysfunction of the ovary and sperms.

Clinical tests for ISD have already been successfully completed in 2005 and it is estimated that over 20 million people in China suffered from infertility and sterility diseases.

Conclusion

The high growth rate in the Chinese economy has placed the Group in the most exciting part of the world to implement its business plans and operations and the Directors are pleased with the results on the implementation of the business objectives. As part of the PRC Government new effort to build a harmonious society, the Directors believe that a well funded and fair medical system is a vital contributor to building a lasting harmonious society and that the Company's early detection and prevention of diseases will save lives and promote the awareness of good healthcare.

Being a leading supplier of protein chips and solutions for early detection of diseases in the high growth healthcare industry in China, the Group appreciates the many challenges and risks that are associated with the high growth industry and believe that the Group is reasonably well placed to respond to the risks and challenges accordingly. The Group believes that the business plan for the revised KM2003 Objectives will be executed with precision and changes will only be made when there is a need to do so.

The Group also understands the constant evolution of biomedical science and its applications, and will continue to expedite its business growth by actively pursuing new medical related opportunities through alliances, licensing and acquisitions. The Group is optimistic about its future and is in a state of readiness to face the many new challenges in 2007.

DIVIDEND

An interim dividend in respect of the year ended 31st December, 2006 of HK1 cent (2005: Nil) per share was paid on 25th October, 2006. The directors have recommended for adoption at the forthcoming annual general meeting of the Company the payment of a final dividend for the year ended 31st December, 2006 of HK1 cent (2005: Nil) per share.

PLEDGE OF ASSETS

At the balance sheet date, following assets were pledged to secure general banking and credit facilities granted to the Group:

	2006 HK\$'000	2005 HK\$'000
Buildings	5,992	6,101
Buildings under construction	23,587	–
Pledged bank deposit	10,000	190
	39,579	6,291

Management Discussion and Analysis (Continued)

LIQUIDITY AND FINANCING

The Group adopts a prudent approach in managing its liquidity and treasury function and sets out guidelines to achieve these objectives. These guidelines cover the Group's debt profile, financing horizon and interest rate risks management.

At 31st December, 2006 the Group had cash and bank balances of HK\$451.6 million (2005: HK\$489.1 million). The Group's gearing ratio as at 31st December, 2006 was 50.8 percent (2005: 52.8 percent), based on bank and other borrowings of HK\$288.6 million (2005: HK\$259.7 million) and shareholders' fund of HK\$568.1 million (2005: HK\$492.3 million)

The Group's bank borrowings were denominated in Hong Kong Dollars and Renminbi. Bank borrowings totaling HK\$95.1 million were outstanding as at 31st December, 2006 (2005: HK\$76.5 million). The bank borrowings bear interest at prevailing market rates ranging from 4.92% to 6.04% per annum (2005: ranging from 4.45% to 6.89% per annum).

Revenue generated from protein chips operation, payment for purchases of materials, components, equipment and salaries are made in Renminbi. Use of financial instruments for hedging purposes is considered unnecessary and the exposure to exchange rate fluctuation is minimal.